

# Trends in IT and their influence on outsourcing

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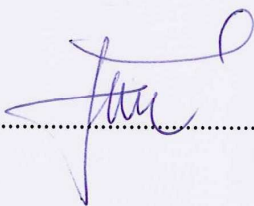
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## **ABSTRAKT**

Bakalářská práce „Trendy v IT a jejich vliv na outsourcing“ se skládá ze dvou částí. V teoretické části se zabývám outsourcingem ve všeobecném pojetí. Popisuju hlavní pojmy, historii outsourcingu, výhody, nevýhody, outsourcingový proces a nejběžnější rozdělení. V praktické části se nachází SWOT analýza outsourcingu a tři případové studie, které mají za cíl objasnit teorii outsourcingu.

Klíčová slova: Outsourcing, výhody, nevýhody, riziko, vytěsnění, poskytovatel, offshoring, služby, služby, outsourcingový proces, IT, trendy, případové studie

## **ABSTRACT**

Bachelor thesis “Trends in IT and their influence on outsourcing” is structured into two parts. In the theoretical part, I deal with outsourcing in general conception. I describe main terms, history of outsourcing, advantages, disadvantages, outsourcing process and the most common divisions. The practical part contains SWOT analysis of outsourcing and three case studies which should clarify the theory of outsourcing.

Keywords: Outsourcing, advantages, disadvantages, risk, displacement, provider, offshoring, services, outsourcing process, IT, trends, case studies

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## INTRODUCTION

Outsourcing has become a widespread trend in recent years. It has turned out to be one of the main tools for improving performance. Companies all over the world use advantages arising from subcontracting a service to a third-party. In many companies outsourcing has helped to initialize strategic changes that highly increased profitability. With fast growing companies which have started to specialize their services more and more, outsourcing has become one of the best options how to deal with highly complex and qualified functions.

We come across outsourcing in everyday life and we do not even notice it. There are many services which can be called outsourcing but we do not realize it. That is why I think that analyzing outsourcing closer could help us to understand what outsourcing really is and what benefits it brings.

The aim of this bachelor thesis is to give a wide overview of outsourcing. I will focus on why outsourcing is such an appealing option, what advantages it brings and it will study all other aspects concerning outsourcing to understand outsourcing as an entrepreneurial and organizational tool.

Furthermore, this thesis will incorporate description of outsourcing process to comprehend how outsourcing is realized, from deciding for outsourcing to closing a contract.

In the following chapters, I would like to focus on IT services and demonstrate that services nowadays are trend by itself and to point out that services are closely connected with outsourcing. That is why I find these chapters as essential for my thesis.

Ultimately this thesis will evaluate outsourcing according to SWOT analysis to understand better all aspects of outsourcing as strong and weak points, opportunities and threats. In the end I would like to bring out three study case studies of one Czech company which provides outsourcing services. My aim is to demonstrate theory of outsourcing on these three study cases to see what advantages or disadvantages it can bring to various companies.

## **I. THEORY**

## 1 OUTSOURCING

The term outsourcing itself originated from words “outside” and “resourcing”, this fact gives as an idea what outsourcing is about. *“Outsourcing is simply the farming out of services to a third party. With regards to information technology, outsourcing can include anything from outsourcing all management to outsourcing a very small and easily defined service, such as disaster recovery or data storage, and everything in between.”* [16] In other words we can say that outsourcing is a process when one company provides services from another company maintaining its ownership and complete responsibility for the processes. From this definition we can see that outsourcing is very useful and necessary tool for the companies in the present day.

The general reason for outsourcing is increasing shareholder value. Gaining profitability is possible by two options. Cutting costs or raising income. If these advantages would cut costs or bring more income, company should seriously consider outsourcing.

### 1.1 History of outsourcing

*“Outsourcing is not a new phenomenon, as many of us believe. Many thousands of years ago, our ancestors had understood the need for outsourcing. They realized that it would be impossible for them to fulfill all their needs by themselves, but they would have to depend on someone else to serve them. The service provider possessed specialized skills, which enabled him to do the work faster, cheaper and more efficiently. Thus, we observe that in early societies, every man had a part to play – he could be a farmer, a merchant, a soldier or a barber. He was, in modern parlance, a client as well as a service provider.”* [10]

In 1923 Henry Ford said that if there were something they could not do more effectively, cheaper and better as their competition, it is meaningless to do these activities and they should hire someone who would do it for them. Henry Ford was one of the biggest innovators of outsourcing considering eighties as new era of outsourcing. [15]

Kodak is indicated by many resources as a turning company in outsourcing the information technology systems and its mass usage (mostly in USA). Nowadays we can meet with terms as “before Kodak” and “after Kodak” period. [4] It started with a huge contract signed by Eastman Kodak In 1989. He gave an order worth \$250 million to IBM. *“The deal took place because Kodak had identified its core competencies, realized that IT was not one of them, and wanted to partner with a provider to deliver on this non-core activity while it focused on its own core competencies.”* [11] *“They were quickly followed by*

*dozens of major corporations whose managers had determined it was not necessary to own the technology to get access to information they needed.” [9]*

After Kodak’s decision, it did not take long and other companies realized that it is not necessary to own technology and knowledge. With Kodak’s big contract, companies had to face boom of outsourcing and had to get used to outsourcing. Organizations started to outsource jobs to local companies on a large scale. Nowadays as the world entered the era of globalization, development of the Internet and communication technologies, the recent trend for organizations from developed countries is to turn to companies from developing parts of the world for the manpower needs. [23]

Another trend is toward forming strategic partnership. Some companies are ready to outsource even their core activities if it means any extra profit. Nowadays, outsourcing has become essential part of almost every large organization. [10]

## **1.2 “Make” or “Buy” strategy**

Outsourcing can be one of the options of “make or buy” strategy. Before thinking an implementation of outsourcing, company should consider if it is more profitable to make or to buy. The gist of this strategy is based on the choice of two basic variants. The question is, if it is possible to realize the specific process or activity in the scope of own production process or it is better to choose a supplier. Consideration about this strategy can have many forms:

- The choice of production of smaller parts for a bigger and more complex product
- The choice of the system or subsystem of the production (if the car company should also make engines for their cars or leave it for another company)
- The choice of specific production process (the question can be if to buy a new specialized device or to hire a subcontractor for this process) [17]

### **1.2.1 “Make” or “Buy” strategy decision factors**

The companies, which are considering the idea of this strategy within the scope of their business activity, should organize quality project team and make a “process guide”. The best option is to make a decision tree based on specific questions and answers. It gives a space for making compromises or choices for qualifying sources. In the beginning of this decision tree, the possibilities of sales are found out, and then it should continue with analyses and various decisions. However, in practice the decision tree simple like this is

very rare. Managers mostly have to face more sophisticated problems than we can put in the simple scheme of the decision tree. It is similar in the "make or buy" strategy. This strategy is influenced by many factors. As for example:

- The market position of the company and the trends of its development
- Products and operational abilities
- Competition, customers and suppliers
- Cost analysis and comparison with other companies
- Projection

When a company will solve this problem and will decide for "buy" instead of "make", then we can consider outsourcing as an option for a company. Company should also consider possible advantages, disadvantages or risks. [17]



Figure 1: The choice of „MAKE“ strategy [17]

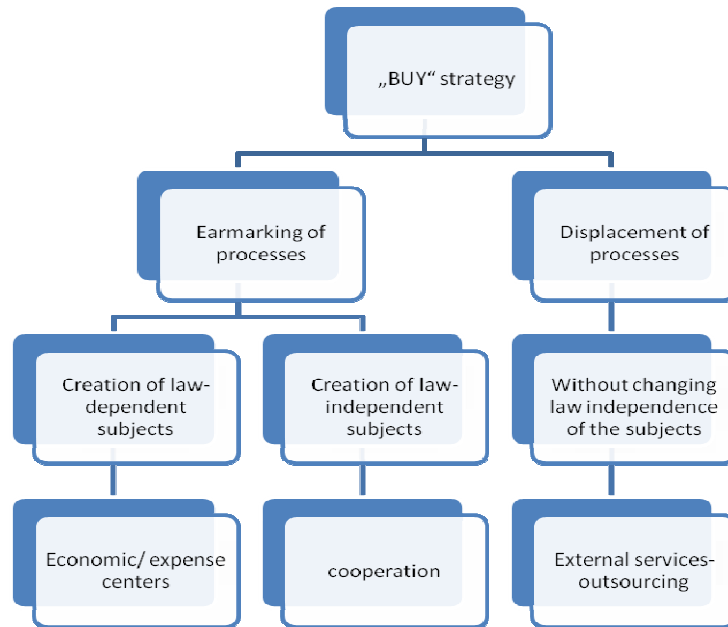


Figure 2: The choice of „BUY“ strategy [17]

Now, when a company has decided for “BUY” strategy, we can think of outsourcing as an option and we can specify its characteristics.

### 1.3 Advantages of outsourcing

The main reasons why companies use outsourcing more and more are simple. It brings lot of advantages. The most important ones are:

- The ability to focus on core competencies by ridding of peripheral ones.

*“Back office operations of a company require high maintenance and specialized attention. Yet most of them are critical for the company's everyday activities. By outsourcing their back office operations businesses can concentrate on their core competencies while their back office operations are being managed smoothly by a specialized third party company.”* [1]

- Cutting costs and getting the work done more effectively and efficiently.

*“By employing skilled manpower in larger numbers at lower costs companies can really increase their productivity. This in turn would result in better customer satisfaction and increased profitability.”* [1]

- Expertise.

*“Experienced outsourcing houses possess profound knowledge of the latest technologies essential for businessmen to achieve fixed business goals.”* [31]

- Reducing overhead costs.

As an example, a company resides in a very expensive locality and they want to expand, it is cheaper to outsource peripheral operations from different company rather than extending their offices.

- Staffing flexibility.

This advantage is very useful in seasonal jobs or when company needs extra help. For example, during tax and auditing periods.

Companies can also use different advantages of outsourcing as variable capacity, lack of in-house resources, access to innovation, improve business or customer focus, accelerate projects...

The general reason for outsourcing is increasing shareholder value. Gaining profitability is possible by two options. Cutting costs or raising income. If these advantages would cut costs or bring more income, company should seriously consider outsourcing. [1]

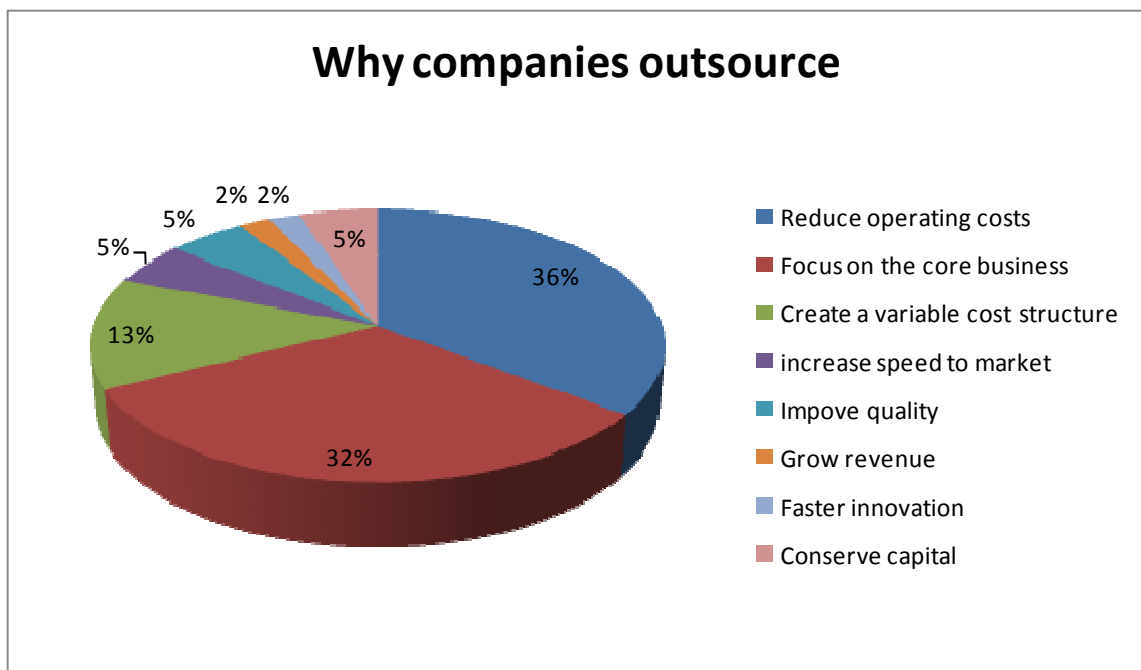


Figure: 3 Why companies outsource [33]

#### 1.4 Disadvantages of outsourcing

When deciding whether to start with outsourcing or not, company should have in mind that there can be certain disadvantages to this step.

- Loss of managerial control.

Putting away certain branches to outsource them can cause loss of managerial control.

The fact, that company has a contract with outsourcing company, does not mean that it



will have a control over the whole process. Managerial control will most probably belong to another company.

- Hidden costs.

Company should be aware of the fact, that during outsourcing process, some costs can go unexpectedly higher than estimated when signing a contract.

- Threat to security and confidentiality.

Letting other parties to see company's information is a dangerous step. This can be a threat to stealing data storage and confidential information. [30]

- Loss of flexibility

*“Outsourcing may also result into the possible loss of flexibility in reacting to changing business conditions, lack of internal and external customer focus and sharing cost savings.”* [30]

- Undesirable result and lack of communication

This is a common thing which can happen to any company. Usually it occurs when hiring a third-party company for mass production. If final result does not meet quality standards, company is forced to hire another vendor. [30]

## 1.5 Potential risks of outsourcing

As it was said earlier, outsourcing has some advantages, disadvantages and of course, it carries some potential risks. Some of the potential risks that company should be aware of:

- Long dependency
- Safety risks
- Little knowledge of provider
- Contract is not set well
- Underestimation of process and organization rules of cooperation [7]

## 1.6 Common outsourcing mistakes

While realizing outsourcing projects, companies can make some mistakes:

- Unrealistic results are expected
- Submitter of the project has unrealistic ideas about the amount of work that has to be done by supplier
- Wrong expectations about saved amount of money caused by displaced service
- Underestimation of preparation phase of outsourcing project

- Critical factors are not specified (sufficiency of resources, knowledge, project management skills...)
- Bad extent of outsourced services
- Poor management
- Ill-structured contract or missing contract [17]

### 1.7 Outsourcing myths

1. Outsourcing will solve the problems

It does not have to be always true that outsourcing will solve all the company's problems. Sometimes it is better to look for other options. It can be enough just to hire more people than to move a problem from one place to another.

2. Specialized outsourcing companies will do it better

Also specialized companies which deal with outsourcing want to make a profit. That might be their primal goal and that can have an effect on their effort.

3. Outsourcing will save money

This might not to be true because eventually the cost of an outsourcing project can go unexpectedly high than was estimated. Companies should first take into account also sudden costs and also be careful when signing a contract with provider. [5]

### 1.8 Outsourcing & Offshoring

Offshoring is frequently mistaken with outsourcing. Even though these two terms have many similarities, there are certain differences and we should consider these terms as different. As was stated above, outsourcing is a term to describe an activity which is displaced to a third party. Offshoring, as the name implies, means moving the business or activities to someone away from the company's shore. Simply, this means moving the company to different country. [13] *“Many developing countries are attracting business organization from developed countries because developing countries are providing quality services at economically cheap price in comparison to developed countries. Various issues affect the decision of a client regarding offshore outsourcing. Factors like manpower cost, manpower quality, and infrastructure facilities in a nation decide the attractiveness of that country as an offshore outsourcing resource location. Legal and business environment in the service provider's country plays a major role in the development of offshore outsourcing.”* [13]

The motive power of offshoring is costing costs, mainly taking advantage of tax and salary gap between developed and developing countries. Companies from developed countries can cut their costs up to sixty percent when using offshoring. Even though the moving to different country carries lot of extra expenses like construction of new buildings or training, it will be compensated by salary savings. The difference is quite obvious if we compare the salaries of different occupations in the US and in India.

<b>Hourly wages for selected occupations US and India, 2002-03</b>		
<b>Occupation</b>	<b>US Wage</b>	<b>India Wage</b>
Telephone operator	\$12.57	Under \$1.00
Health record technologist/ Medical transcriptionist	\$13.17	\$1.50-2.00
Payroll clerk	\$15.17	\$1.50-2.00
Legal assistant/ paralegal	\$17.86	\$6.00-8.00
Accountant	\$23.35	\$6.00-15.00
Financial researcher/ Analyst	\$33.00	\$6.00-15.00
<i>Source: US wages are from US Bureau of Labor Statistics, National Compensation Survey, July 2002; India wages are from interviews, business literature search and review of employment want ads by the authors.</i>		

*Table 1: Hourly wages in the US and India*

Offshoring can have also different ways of cutting costs. For example, company can save lot of money by buying new components or devices for the production in the “new country”. Company can save money also by hiring local people for creating software and generally by using any of local services. [32]

## 2 OUTSOURCING PROCESS

Outsourcing as a process is realized by certain project. Outsourcing project is dependent on up to now solutions, on a type of contracting and ownership relationship of submitter and provider. Its process is usually very specific.

With regards to the strategic importance of decisions about outsourcing, it is suitable for a company to deal with procedure and detailed project by itself. On the other hand, it is common that when dealing with a project, company can share a project with a specialized consultancy company.

We can separate the process of outsourcing into six different phases:

- Strategic analysis of function fields.
- Specification of function fields which are going to be displaced
- Definition of a boundary line between “company- provider” and a definition of requirements for provider
- The selection of providers
- Transformation
- Relationship management
- Outsourcing contract [4]

### 2.1 Strategic analysis of function fields

Strategic analysis is a part of a global company strategy and its role is to clearly define the core business of a company. The principle of this analysis should be an effort to understand company’s basic abilities, strong and weak points and capability to face the competition.

By function field, we mean strategically important field, which is basic for competitiveness of a company, also known as core business.

This phase is critical for the success of the whole outsourcing process and it requires participation of top management for the whole time. The result could be long and throwaway decision which could possibly change the core business of a company and its organization structure.

All the function fields which do not belong to the core business could be considered for outsourcing. [4]

## 2.2 Specification of function fields which are going to be displaced

After closing the strategic analysis, it comes to determination of the function fields which are going to be displaced. The key questions for this process are:

- Which fields would be appropriate for displacement?
- Is better to displace the whole field or just a part of it?
- What advantages and risks could be expected?
- Displacement of which part would bring the biggest contribution?
- Is it preferable to move fields to one provider or more?

It is important what fields will company displace. By no manner of means should company displace something what is not exactly defined. Any uncertainty could cause lot of damage. It is very important to make an analysis of potential risks, costs and benefits. The problem of costs is represented mostly by hidden costs. [4]

The company should closely explore whether they should displace the whole field or just a part of it and whether it will be more beneficial to outsource with one or more providers.

In this phase, company should see some vision about the range of outsourcing contracts.

Here we can see three main relationships between the company and outsourcing provider:

1. short-term and occasional contracts, strictly defined assignment during a short period;
2. long-term contracts, usually for five to ten years;
3. joint ventures, when two sides share costs and risks together. For example, one company wants to be engaged in industrial surveys and other wants to use information systems of other.
4. Definition of a boundary line between “company- provider” and a definition of requirements for provider [4]

## 2.3 Definition of a boundary line between “company- provider”

In this phase, it comes to concretizing the required service between company and provider. It is important to determine mutual relationship in exact terms to avoid any disagreement and extra costs. Definition of a boundary line between company and provider should include:

- Types of products and services
- Information
- Technology

- Maximum time in which will provider react
- Prices
- Competencies of both sides [4]

It is also required to define specifications from the side of a provider. It is possible to structure them in different ways and displace the most critical ones. Although the fact the provider owns some means of operation, e.g. computers, they can have limited options for using them. The requirements for provider can include size of a provider, qualifying requirements, resources ownership confirmation or acceptance of commitment. [4]

## **2.4 The selection of providers**

Company should be very careful about the choice of the future outsourcing provider. This choice can carry much potential risk considering that both sides do not share the same profit motives. From experience of other companies, we can put down three main warning signals against the potential failure considering the choice of a provider:

1. Finances, law or provider dominate in the contract process
2. Reference and reputation are not taken into consideration
3. The short- term advantages dominate when making decisions [4]

## **2.5 Transformation**

Generally, this part of a process is critical mostly from the point of human resources. It should be recommended to inform all the employees, who could be affected by outsourcing to avoid any misunderstanding.

If the company is displacing a field, which has already been managed in the company, the problem could be what to do with all the actives (technologies, licenses, machines, staff...). The most acceptable option would be to displace the whole field with all its actives. In this case, provider usually buys them for their accounting value. [4]

## **2.6 Outsourcing contract**

Negotiating an outsourcing contract is an integral and inevitable part of the whole outsourcing process. It is important for a company to realize that by making a contract they assign to a provider for long time (usually between three years up to ten years). This contract has to be advantageous for both sides so the business partnership is successful.

[17]

### 2.6.1 Forms of outsourcing contract

Czech system of law has two main kinds of using of contracts. Named and unnamed. Among named contracts, which can be used for closing outsourcing deals, belong:

- Fixed job contract- the problem with this kind of a contract is that “fixed job” is time limited and finished operation. But we cannot understand outsourcing in this sense, because it is an always developing process. That is why this kind of contract works for example for one time development of information system with specific result.
- Lease- the problem with a lease is that it is applicable only for a “thing” not for people, information system or software. Its usage is exploitable for the lease of hardware for example.

More appropriate for outsourcing contracts is usage of unnamed contracts. [17]

### 2.6.2 Outsourcing contract contents

In every contract there should be certain points so the contract is safe, has minimum risks and is advantageous for both sides.

The most important points that should be mentioned in the contract:

- Definition of contacting parties- client of the outsourcing service and supplier
- Subject of the contract- the gist is to determine services which are going to be displaced. The best method is to describe outputs of given process; specify requirements for partnership and general responsibilities of service supplier.
- Pricing- the price should be set in a way that would correspond to performance also in longer cooperation. It is suitable to include also anti-inflationary measures.
- Confidence clause of provided information- the contract should have provision of security because many times an order party gives confidential information to the supplier.
- Responsibilities of client, supplier and transformation of liabilities
- Penalty clause, extra bonuses etc
- Life of the agreement
- The way of changing the contract
- The ways of termination of the contract

These are the main points which should be included but there are usually more. Company can mention points concerning technologies and devices, the way of communication, possibilities of control and others. [17]



### 3 TYPES OF OUTSOURCING

„One challenge every business enterprise faces nowadays is to find niches that generate the most income. Several companies are wary to venture on additional expenditures that do not promise considerable yield. This is the main reason why companies resort to outsourcing activities.” [25] It would be possible to divide outsourcing into many categories, but to be clearer we can use three main types:

1. technology services outsourcing
2. business process outsourcing
3. knowledge process outsourcing [25]

#### 3.1 Technology services outsourcing

„Companies that utilize technology require sophisticated, quick-responding computer systems and software that are flexible enough to respond to the increasing capabilities of technology and the rapid changes in business models. Selecting the right technology partner is an integral part of many successful ventures. Following are the specific types of technology services.

- *Electronic Commerce ("eCommerce")*
- *Infrastructure ("Networks")*
- *Software ("Applications")*
- *Telecommunications*
- *Website Development & Hosting” [24]*

#### 3.2 Business process outsourcing

„BPO is distinct from information technology (IT) outsourcing, which focuses on hiring a third-party company or service provider to do IT-related activities, such as application management and application development, data center operations, or testing and quality assurance.

*In the early days, BPO usually consisted of outsourcing processes such as payroll. Then it grew to include employee benefits management. Now it encompasses a number of functions that are considered "non-core" to the primary business strategy. “[2]*

- Customer Contact (Customer Relations Management)
- Equipment
- Finance / Accounting
- Human Resources
- Logistics
- Procurement / Supply Chain Management
- Security [24]

### 3.3 Knowledge process outsourcing

*“A more sophisticated level of outsourcing relative to BPO is knowledge process outsourcing (KPO). This involves advanced research, analytical, and technical skills which means that providers are expected to work independently. It is also important to note that in BPO, all processes are still laid out by the client whereas KPO specialists are given managerial control. Examples of KPO include:*

- *pharmaceutical research and development*
- *intellectual property research*
- *content writing*
- *database development services*

*Among the three types, knowledge process outsourcing is the oldest form of outsourcing and usually involves short-term and peripheral projects. BPO, however, is considered as the most popular among the three types especially if one is to consider that most companies outsource business processes to offshore locations such as the Philippines.”*  
[25]

Common critical factors of all the outsourcing variants for success are:

- Proper definition and content of service, its customization and integration
- Precise capacity of the service
- Adequate quality of services
- Reasonable price
- Stable and responsible supplier

- Appropriate usage of resources in the company- sources should be used in processes which have higher effectiveness of using the resources than displaces process. [29]

Henceforward, I will deal with Technology services outsourcing in my bachelor thesis.

### **3.4 Outsourcing variants according to the subject of outsourcing**

Informative processes and resources have to be integrated in providing all informative services. The key question is which of the necessary processes and resources should be provided by external subject and which should be owned.

By this we can come to the different variants of outsourcing. The basic criteria for separating of outsourcing variants is the key subject, that means which responsibilities and which related activities convert to external supplier. [29]

From the previous division of technology services outsourcing we can have a look at specifications of IS/IT area from outsourcing point of view. We can consider as outsourcing of IS/IT also a situation 10 years ago or even more, when it was inaccessible in Czech Republic for most companies to process data internally and when this or other IS/IT services were provided specialized company. Outsourcing of IS/IT was considered as disadvantage and later with the development of cheaper mainframe computers and primarily with development with affordable computers, many companies crossed to internal IS/IT service securing.

Investments to IS/IT are specific mostly by extremely fast development of technologies, mainly in the areas of hardware, software and communication standards. Development of these areas is linked and dependant. It is necessary for the new way of information integration with surrounding always to have new software and this kind runs only on new computers. That is why this relatively cheap equipment costs lot of money because of its need for continuous innovation. The usual lifespan of hardware is two to three years, the basic software five to six years and application software six to ten years. In the previous years IT expenses for companies have even enlarged because of the massive growth of the Internet and the need for the connectivity.

Keeping up with the high level of information systems is technologically difficult because of constant following the world trends, it is demanding to investments for innovations and costs for unexpected ups and downs of the world IS/IT development. If we add other usual

costs, we will find out that operating of information system is very expensive and demanding for experts and technologies. [29]

Because of these reasons, companies tend to use outsourcing of IS/IT.

From the view of suppliers, it is clear that it is simpler to sell goods than selling services. One reason is because of the high responsibility and also because of lesser demandingness for resources and system control. But IS/IT market is saturating. Suppliers who cannot sell their goods on saturated market are naturally turning into their current customers offering them new services. With growing level of these services, there is also growing space for outsourcing.

From the point of IS/IT we can distinguish three main divisions:

1. Outsourcing of complex IS/ICT
2. Partial outsourcing of IS/ICT
3. Development outsourcing of IS/ICT [29]

#### **3.4.1 Outsourcing of complex IS/ICT**

In this case, provider moves operation and development of all the information services and related processes with information sources to the supplier. In contrast to BPO, company does not move also business processes to external supplier. For example, company will displace whole IS/IT area including accounting application, but the accountancy process of itself will stay in the company. With these processes, supplier receives also all the responsibilities for displaced applications. That means big advantage for the clients, because they will get rid of all the concerns connected to IS/IT. [29]

#### **3.4.2 Partial outsourcing of IS/ICT**

Parts that can be moved to the supplier:

- Specific information services- a good example can be outsourcing of electronic mail operation and others.
- Selected information processes- including sources which are needed for their displacement.
- Selected information sources- typical activities connected with each source are: purchase/ development, maintenance/ upgrade, customization, integration with other sources, operation, selling and liquidation. The main advantage of this variant is that it enables detailed planning and control in informatics. That means, company

can outsource only information services or processes which have wide representation on the market and they are able to look for better price. [29]

### 3.4.3 Development outsourcing of IS/IT

This type of IS/IT outsourcing moves only development of some IS/IT sources to the supplier, which will be operated later by submitter. The most typical example of this type of outsourcing is development of application software. Included can be also training of personnel because actually it is development of one of the information resources-information personnel. [29]

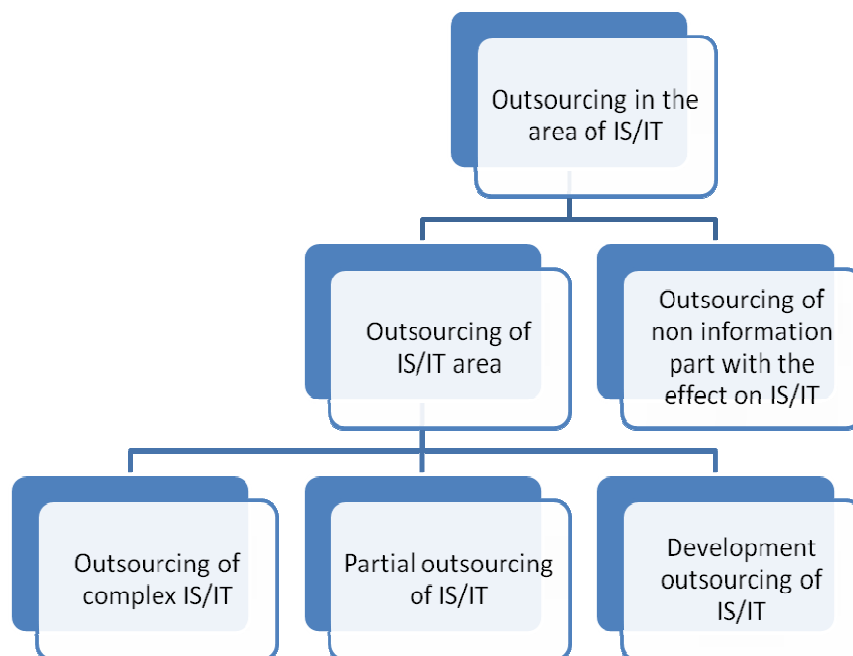


Figure 4: Area division of IS/IT outsourcing [29]

### 3.4.4 Independently detachable IS/IT parts

According to previous divisions, we have made a picture about outsourcing variants and we can see that it has many ways. Here we can see some of the most common IS/IT situations which are outsourced.

- Body shop outsourcing. The easiest way of outsourcing is displacing of human resources. In case of need any programmers, analysts or different specialist, company can hire them from specialized companies. Providing of human resources is the cheapest way of outsourcing service. Outsourcing of human resources can

also mean hiring of tradesmen instead of regular employees so the company can avoid some inconvenient aspects which happen in business.

- Outsourcing of data centers. In data centers, customers have stored and processed their data which they use by remote access. It is interfirm distribution of data, suitable for architecture of client- server type. Provider guarantees security and protection of data. It is possible to penalize the provider for breaking the guaranty and also for incurred loss. Also provider has to guarantee the response time of data process and data accessibility. Outsourcing of data centers solves mainly investment demandingness of establishing own data center. It is possible to modify on the side of the provider capacity needs, as hardware or data system, in disregard of the ways of application implementation of customers.
- ASW outsourcing. Application software is mainly subject of the outsourcing development. If it is owned or maintained externally, usually the provider is the supplier of ASW development and mainly within displaced integral IS/IT.
- Outsourcing of local networks and their functions. Except of remote network management, backup maintenance (backup and disaster recovery) can be outsourced. It does not have to be accessible for a company to manage internal plan of data recovery (due to natural disaster, for example). Provider can responsibly oblige that data that have been made a backup by a customer can be in specific time restored.
- Outsourcing of WAN, telecommunications, WWW servers and EDI. Global telecommunications give the great space for outsourcing; even some companies are forced for this. Costs for the creation of private global communication network are very high. It is natural that there are only few companies with infrastructure of private global communication network which have pushed through. Global telecommunications involve also www web pages, which many companies acquire nowadays for marketing and sale purposes. EDI (Electronic Data Interchange) can be outsourced. Provider can supply and operate hardware, software and related services necessary for conversion of business data to separate formats. It is used mainly for information exchange among business partners (purchase orders, invoice, payment order...)

- Transformation outsourcing. It is a onetime transformation of information system of the company, which works on mainframe computers. The transformation is usually for cheaper client- server.
- Different separately displaced IS/IT parts. Another usually displaced IS/IT parts can be help desk, trainings, PC support. [4]

## 4 OUTSOURCING AS A SERVICE

Nowadays many companies are service focused and we can say that providing services has become the huge trend. Especially in IT field. Through the last several decades, leading-edge firms, as well as many business scholars and consultants, started to refocus on substantial firm activity or transforming the entire firm orientation from producing output, primarily manufactured goods, to a concern with services. These initiatives can be found in both business-to-business (e.g., IBM, GE) or also in business to-consumer enterprises (e.g. Lowe's, Kodak, Apple) and in some cases of entire industries (e.g., software-as-a-service). This is based on an idea that most of the companies are based on producing and exchanging more services than goods, thus the services require more attention. [26] This implies that we can say that outsourcing is a service and service is a trend by itself and is replacing goods market.

*„When a firm sees itself primarily as a manufacturer with an implied purpose of selling what it makes, it sees the key to making more money as selling more goods. There is little or no logic in selling fewer goods--why should Volkswagen want to sell fewer cars or Dow to sell fewer chemicals? In contrast, the service-dominant logic suggests that since these goods are actually mechanisms for service provision, the customer is always buying a service flow rather than a tangible thing, and thus the firm should focus on selling a flow of service. This would encourage it to determine the optimal configuration of goods, if any, for a level of service, the optimal organization or network configuration to maintain the service, and the optimal payment mechanism in exchange for providing the service. That is, the organization is encouraged to think about the service system.“* [28] This implies that we can say that outsourcing is a service and service is a trend by itself and is replacing goods market.

### 4.1 Goods dominant logic (GD)

As the name implies, goods dominant logic is a term centered on the good – or more recently, the “product”, to include both tangible (goods) and intangible (services) units of output – as typical units of exchange. [26] *“The roots of G-D logic are found in the work of Smith (1776) and took firmer, paradigmatic grasp in the context of the Industrial Revolution during the quest for a science of economics, at a time when “science” meant Newtonian mechanics, a paradigm for which the idea of goods embedded with value was*



*particularly amenable. Management and mainstream academic marketing, as well as society in general, inherited this logic from economics.*“ [26]

## 4.2 What is a service?

The main point of services in my bachelor thesis is that outsourcing is closely related with service which is a trend by itself. With expanding market of services we can see more and more opportunities for outsourcing process. That is why, we should define what service actually is.

*“A type of economic activity that is intangible, is not stored and does not result in ownership. A service is consumed at the point of sale. Services are one of the two key components of economics, the other being goods. Examples of services include the transfer of goods, such as the postal service delivering mail, and the use of expertise or experience, such as a person visiting a doctor.”* [18]

Service is oftentimes as something that does not belong to manufacturing or agricultural. From this point of view we say that services belong to the tertiary economic sector. By these definitions we can understand what service actually means.

Services can be distinguished by four major characteristics:

- Intangibility- service cannot be touched or view, that means that potential clients cannot be sure what they will get
- Perishability- unused service cannot be used or stored for the future. For example, unoccupied seats in the plane cannot be transferred to different plane or used in the future
- Variability- also referred as heterogeneity, means that same services can be performed in different ways
- Inseparability- service is usually produced at the same time as it is being received by a client. [20]

We can have a look at IBM, which is the world's biggest information technology company oriented on selling computer hardware and software and offers plenty of services. The company's prime services offers include information technology (IT) datacenters and business process outsourcing, application management services, consulting and systems integration, technology infrastructure and system maintenance, web hosting and the design and development of complex IT systems to a client's specifications

We can see on the picture six that IBM stated in 2009 annual report that ninety percent of their entire segment profit was from software, services and financing. [12]

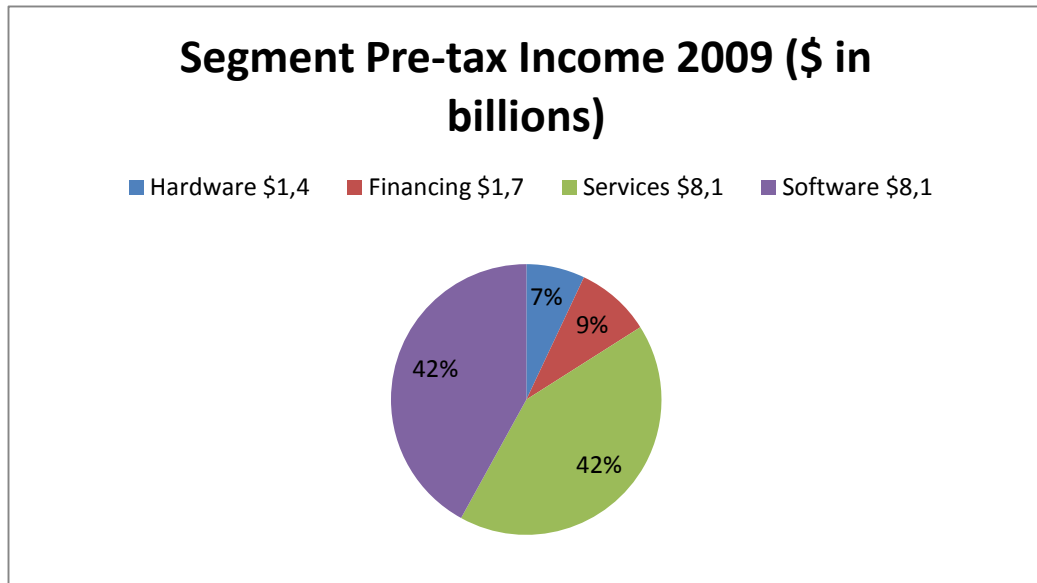


Figure 5: Segment Pre- tax Income 2009 [12]

Also, in this annual report we can find that total Global Services signings of IBM were \$57,094 million and decreased 0.2 percent .What is interesting is that outsourcing signings of \$33,014 million increased 8.8 percent. From this statement we can deduce that outsourcing and services are growing trend and are mutually connected.

Again, we can look at IBM annual report in the picture seven which shows us global technology and business services signings. [12]

For the year ended December 31	2009	2008
<b>Global Technology Services Signings</b>		
Outsourcing	\$25 507	\$24 446
ITS	\$9 196	\$10 247
Total	\$34 703	\$34 693
<b>Global Business Services Signings</b>		
Application Outsourcing	\$7 506	\$5 905
Consulting & System Integration	\$14 885	\$16 584
Total	\$22 391	\$22 488

Table 2: IBM global service Signings [12]

From this chart we can see the close connection of services and outsourcing. Outsourcing has the biggest share as far as Global Services Signings are concerned. [12]

With introducing service we come to different terms as service dominant logic and service science.

### 4.3 Service-Dominant logic (S-D logic)?

As was said in goods- dominant logic chapter, first, marketing inherited a model which had a dominant logic founded on the exchange of “goods”, which are manufactured output. This logic focused on tangible resources, embedded value and transactions. But after several decades, new ways of thinking were discovered which have modified logic focused on intangible resources, the cocreation of value and relationship. These new perspective have formed a new dominant logic for marketing where more important is position of services rather than goods. This logic is called service-dominant logic.

To understand this logic more, basic concepts should be clarified.

This relatively new approach was introduced in 2004 by Stephen Vargo and Robert Lusch in edition of Journal Marketing “Evolving to a New Dominant Logic for Marketing”. From this point, academics have accepted this idea with new marketing consequences.

S-D logic is based on ten basic foundational premises. Eight of them were set by Vargo and Lush and two others were added later in 2008. To understand more about S-D logic, we should specify these foundational premises (FP): [19]

*“FP1 Service is the fundamental basis of exchange. The application of operant resources (knowledge and skills), “service,” as defined in S-D logic, is the basis for all exchange. Service is exchanged for service.*

*FP2 Indirect exchange masks the fundamental basis of exchange. Because service is provided through complex combinations of goods, money, and institutions, the service basis of exchange is not always apparent.*

*FP3 Goods are a distribution mechanism for service provision. Goods (both durable and non-durable) derive their value through use – the service they provide.*

*FP4 Operant resources are the fundamental source of competitive advantage. The comparative ability to cause desired change drives competition.*

*FP5 All economies are service economies. Service (singular) is only now becoming more apparent with increased specialization and outsourcing.*

*FP6 The customer is always a cocreator of value. Implies value creation is interactional.*

*FP7 The enterprise cannot deliver value, but only offer value propositions. Enterprises can offer their applied resources for value creation and collaboratively (interactively) create value following acceptance of value propositions, but cannot create and/or deliver value independently.*

*FP8 A service-centered view is inherently customer oriented and relational Because service is defined in terms of customer-determined benefit and co-created it is inherently customer oriented and relational.*

*FP9 All social and economic actors are resource integrators. Implies the context of value creation is networks of networks (resource integrators).*

*FP10 Value is always uniquely and phenomenologically determined by the beneficiary Value is idiosyncratic, experiential, contextual, and meaning laden.” [19]*

#### **4.4 Service Science, Management and Engineering**

It took long time until services became dominant. As was said earlier, markets are starting to be more and more service based rather than based on goods but services were not examined. That carries the problem with specifications and descriptions of the terms.

Thereby that is why new discipline had to be established, started taught and researched at universities. And that is what service science is concerned about. This gives the market space for new studies as service design, development, marketing and delivery. [21]

Service Science, Management and Engineering is a term introduced by IBM to describe Service Science as a new way to approach to the study, design, and implementation of services systems. [20] They established the essential goals of this target:

- to become more systematic about innovation in services
- to complement product and process innovation methods
- to develop “a science of services”

The proposed areas should mainly deal with fields as computer systems, linguistic, social and economic systems. Also, we can distinguish three main parts of SSME and that is:

- science – to understand what services are and how to understand their evolution
- management- to deal with the investment to the services and their improvement
- engineering- to invent new technologies that would improve services systems

Application of SSME should help understand services more, their evolution and design. Also to make productivity, quality, attainability and innovation rates more predictable. [22]

## **II. ANALYSIS**

## 5 SWOT ANALYSIS OF OUTSOURCING

I have decided to make a SWOT analysis of outsourcing as a service in my bachelor thesis to understand and evaluate outsourcing more. SWOT analysis is based on analyzing internal factors (strengths, weaknesses) and external factors (opportunities, threats).

### 5.1 Internal factors

#### 1. Strengths

- Focus on core activities
- Cutting costs
- Getting work done more effectively and efficiently
- Sharing of risks
- Staffing flexibility
- Development of internal staff
- Variable capacity
- Access to innovation
- Improvement of business or customer focus
- Acceleration of projects
- Reengineering
- Releasing resources for different purposes
- Gaining competitive advantage
- Improvement in core business area
- Simplification of manager's work
- Saving on latest technology, software or infrastructure

#### 2. Weaknesses

- Loss of managerial control
- Hidden costs
- Loss of flexibility
- Undesirable result and lack of communication
- Not all processes are cost-effective to be outsourced
- Outsourcing can make possible redundancies to the company
- Lack of interest or lack of productivity by staff
- Bad publicity

## 5.2 External factors

1. Opportunities
  - Enlargement of markets for potential outsourcing
  - New trends
  
2. Threats
  - Loss of confidential information
  - Competition can take over potential suppliers
  - Loosing independence
  - Poor effort of the provider
  - In case, provider goes bankrupt, company can have problems
  - Employees getting their own job outsourced

SWOT ANALYSIS			
<b>Internal factors</b>	<table border="0" style="width: 100%;"> <tr> <td style="width: 50%; vertical-align: top;"> <p><b>S - Strengths</b></p> <ul style="list-style-type: none"> <li>Focus on core activities</li> <li>Cutting costs</li> <li>Getting work done more effectively and efficiently</li> <li>Sharing of risks</li> </ul> </td> <td style="width: 50%; vertical-align: top;"> <p><b>W – Weaknesses</b></p> <ul style="list-style-type: none"> <li>Loss of managerial control</li> <li>Hidden costs</li> <li>Loss of flexibility</li> <li>Undesirable result and lack of communication</li> </ul> </td> </tr> </table>	<p><b>S - Strengths</b></p> <ul style="list-style-type: none"> <li>Focus on core activities</li> <li>Cutting costs</li> <li>Getting work done more effectively and efficiently</li> <li>Sharing of risks</li> </ul>	<p><b>W – Weaknesses</b></p> <ul style="list-style-type: none"> <li>Loss of managerial control</li> <li>Hidden costs</li> <li>Loss of flexibility</li> <li>Undesirable result and lack of communication</li> </ul>
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<b>External factors</b>	<table border="0" style="width: 100%;"> <tr> <td style="width: 50%; vertical-align: top;"> <p><b>O– Opportunities</b></p> <ul style="list-style-type: none"> <li>Enlargement of markets for potential outsourcing</li> <li>New trends</li> </ul> </td> <td style="width: 50%; vertical-align: top;"> <p><b>T - Threats</b></p> <ul style="list-style-type: none"> <li>Loss of confidential information</li> <li>Competition can take over potential supplier</li> <li>Loosing independence</li> <li>Poor effort of the provider</li> </ul> </td> </tr> </table>	<p><b>O– Opportunities</b></p> <ul style="list-style-type: none"> <li>Enlargement of markets for potential outsourcing</li> <li>New trends</li> </ul>	<p><b>T - Threats</b></p> <ul style="list-style-type: none"> <li>Loss of confidential information</li> <li>Competition can take over potential supplier</li> <li>Loosing independence</li> <li>Poor effort of the provider</li> </ul>
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Table 3: SWOT analysis

## 6 CASE STUDIES

In my bachelor thesis, I have decided to bring out three case studies of one company which is focused on providing of outsourcing. Zeal Ltd is a Czech company which was established in 1994. It is a very strong and reliable supplier of information and communication technologies with years of experience. Their core business areas are specialized on ICT outsourcing, IP telecommunication systems, security of systems and networks, wireless communication and network management.

Zeal Ltd offers wide range of products and services for their customers. As examples of their core activities can be complex data administration and takeover of all ICT responsibilities, supply and maintenance of information systems, providing of the Internet connection and others.

Each case study contains descriptions of the various clients which have used Zeal's services, reason why these clients have chosen outsourcing, main requirements of the clients, products and services which were provided by Zeal Ltd and technical solutions. In conclusion I summarized obtained benefits for these companies and demonstrated on these three case studies that outsourcing is a frequently used option for companies.

### 6.1 Case study one

#### 1. Client description

Client is a travel agency with two branches which are from distant 25 and 90 kilometers from the central office. This company has twelve desktop computers (eight in the central office and four in the branch offices) plus six notebooks.

#### 2. Reasons for outsourcing

All the computers in the company have still the same software and still for the same purpose. This means, that having an IT administrator is waste of money and this worker would not have even enough work to be done to be employed. In this case, it is better to look for outsourcing service.

#### 3. Main requirements of the client

- Access to online booking system for clients
- Remote access for dislocated branches
- Reliable solution of data storage

#### 4. Products, services and solutions



- Creation of small local network and its administration including security, backup and connection to the Internet
  - File and email server, own domain, long distance access for remote branches
  - Hardware, software, expendable supplies, telephonic support
5. Technical solutions
- Working stations Triline, mail server Linux, file server HP Proliant
  - Backup by external disk array (NAS- raid 5), wireless connection to the Internet, antivirus and antispam ESET NOD 32

## 6.2 Case study two

### 1. Client description

Second case study which I am going to deal with in my bachelor thesis is a company which chose Zeal company for outsourcing service as well. This company makes and supplies pumping technology. They use in the company twelve desktop computers and three notebooks. There are heavy machine tools in the area which can be remote- operated by the computer.

### 1. Reasons for outsourcing

This company does not employ any qualified full time network administrator. That is why there is no one who could take care of such large system and its administration. Managing this kind of system would not be possible for one person anyway. The best solution was to think about outsourcing.

### 2. Main requirements of the client

- Integration of all computers and machines in the whole area into one network
- Responsible solution on the field of backup
- Fast and quality internet connection, connection to the central office in different country

### 3. Products, services and solutions

- Creation of middle-sized network and its administration including security, backup and connection to the Internet by using WiMax technology
- Administration of email and file servers, own domain
- Hardware, software and expendable supplies

- Technical support, distant administration, visits of an administrator according to the needs of client
- 4. Technical solutions
  - Triline working stations, HP Proliant server with Microsoft Windows Server 2003
  - Mail server Linux, implementation of optical fibers into network infrastructure
  - Information system ABRA, program for CAD documents replication
  - Data backup using disk array, VPN security Cisco, VPN tunnel site-to-site, Cisco router
  - Firewall Cisco pix, connection to the Internet by using WiMax technology, antivirus and antispam solutions

### 6.3 Case study three

#### 1. Client description

This client is an engineer's office specializing for production, construction work, supply of single purpose machines, automated assembly lines and other devices. Company has two offices which are 0.3 kilometers distant from each other. They prepare construction of factory building distant 1.3 kilometers. This company owns twenty desktop computers and seven notebooks.

#### 2. Reason for outsourcing

This company does not have and does not want its own network administrator. Ideal solution for them is outsourcing.

#### 3. Main requirements of the client

- High density and reliable connection of both offices
- High speed connection to the Internet
- Security and data storage
- Solution proposal and implementation of a mail server
- Possibility of network expansion in the future

#### 4. Products, services and solutions

- Creation of smaller network and its administration including backup and security
- Interconnection of the branches by optical fiber
- Connection to the Internet, administration of file and mail server, own domain
- Hardware, software and expendable supplies

- Telephonic support, distant administration and visits of an administrator according to the needs of client
5. Technical solutions
- Triline working stations, mail server Kerio Mail Server, file server HP Proliant
  - Data backup using disk array, router Cisco, VPN security Cisco, antivirus and antispam security, interconnection using optical fibers
  - Connection to the Internet using optical network

#### **6.4 Benefits from outsourcing**

By using outsourcing, many advantages have arisen to these clients. Mainly more effective usage of finances, companies will save lot of time and money. These savings can be put in different investments which are needed to be realized. For example, creation of new working places, training of staff or purchase of new equipment. What is more, handling of such a huge area as IT is not something easy and is not in the power of only person. By having their services outsourced, companies can use access to knowledge database of many professionals with different specializations. Another advantage can be displacement of responsibilities and certainty of security and immediate help if needed. Thanks to high speed connection to the Internet, it is possible to help with required problems and react quickly to any breakdown. [14]

#### **6.5 Summary**

From these three different case studies we can say that success of each outsourcing process depends on many factors and it cannot be said with any certainty that the project will or will not be successful. Important are all the stages of this process. From initialization to enclosure of the contract.

As we can see from theoretical part, outsourcing is frequently used option for many companies. It brings many advantages for companies but also certain risks. My aim was to prove that outsourcing used not only by big companies but also for smaller companies. These companies cannot afford to pay IT specialist or they can, but it would not be cost effective. Also, buying expensive software and different programs does not seem for companies as a good option if their core business is not in IT field. For companies as in these case studies, IT outsourcing seems to be the best option as to save money so the clients do not have to waste them on employees that would not be fully engaged, they do

not have to buy expensive IT products which is not really important for them, what is more they can invest saved money to different things which could bring them potential profit. By displacing the whole area and moving all the responsibilities, it is possible for the company to focus on the core activities and not to waste precious time on area which could be outsourced.

On the other hand, outsourcing seems to be one of the best options how to “get rid of” the secondary activities, however, clients should be always aware of the potential risks connected with outsourcing and also extra costs. Clients should always be very careful during the whole process of outsourcing. Firstly, they should realize if outsourcing will solve their problems, they should check if the chosen provider of outsourcing is reliable, be careful when arranging all the details of the contract and also organize in-house relations.

## CONCLUSION

By elaborating this bachelor thesis I can assume that usage of outsourcing will grow in the future especially in IT. Companies will still try to find opportunities how to cut costs, increase profit, maintain position with competition and keep pace with progress and new trends.

It might seem that in the future, companies will try to find other ways how to reduce costs or increase profits. Under pressure of competition, companies can be forced to outsource even their core competencies what might be a problem. That is why companies should carefully consider the option of outsourcing, whether it is the right way of managing for them and if it will bring them the needed benefits.

The aim of this bachelor thesis in theoretical part was to give a wide overview of outsourcing. It focused on advantages, disadvantages, outsourcing process, outsourcing contract and different aspects concerning outsourcing. What I wanted to specify closely were services. I think that this chapter was very beneficial for realizing what outsourcing really is. Outsourcing is a service and service nowadays is a trend by itself. This enlarging market gives space for outsourcing providers to spread.

Ultimately, in practical part, this thesis evaluated outsourcing according to SWOT analysis and from this analysis we can see clearly all aspects of outsourcing as strong and weak points, opportunities and threats. In the end I brought out three study case studies of one Czech company which provides IT outsourcing services. My aim was to demonstrate theory of outsourcing on these three study cases to see what advantages or disadvantages it can bring to various companies. We could make a rough picture of how outsourcing can look like in the practice. Now, we can connect theory with the real process, however to see this process more clearly we would have to know more information and to have wider details of the clients, their financial situation and other aspects which can lead to successful or unsuccessful outsourcing contract.

I consider as the main benefits of this bachelor thesis for me were realizing what outsourcing means, what benefits it can bring and I made a clear picture of the way outsourcing can work. Another contribution was learning from case studies that outsourcing is a complex process which success depends on many factors.

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