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The Innovative Organization: Creating Value Through Outsourcing

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Sprint versus IBM Global Services

- **2003:**

- Sprint requested IBM to handle a number of key software development and IT management tasks
- High hopes for the engagement, valued at \$400 million over five years
- Sprint CIO Michael Stout: sprint will "focus on areas of growth and innovation."
- Part of a plan to cut \$2 billion in operating costs over two years.

- **2006:**

- Stout is no longer CIO, Sprint has merged with Nextel
- Sprint accuses IBM in court of failing to achieve the promised productivity improvements and of concocting a scheme to "falsely bolster" its performance metrics.
- IBM and Sprint-Nextel reach a settlement (undisclosed)

- **Where did it go wrong?**

- Reports suggest that Sprint's internal accounting didn't properly value the work performed by the in-house IT staff

- **Other stories in the article (Sears, Chase, Diebold,...)**



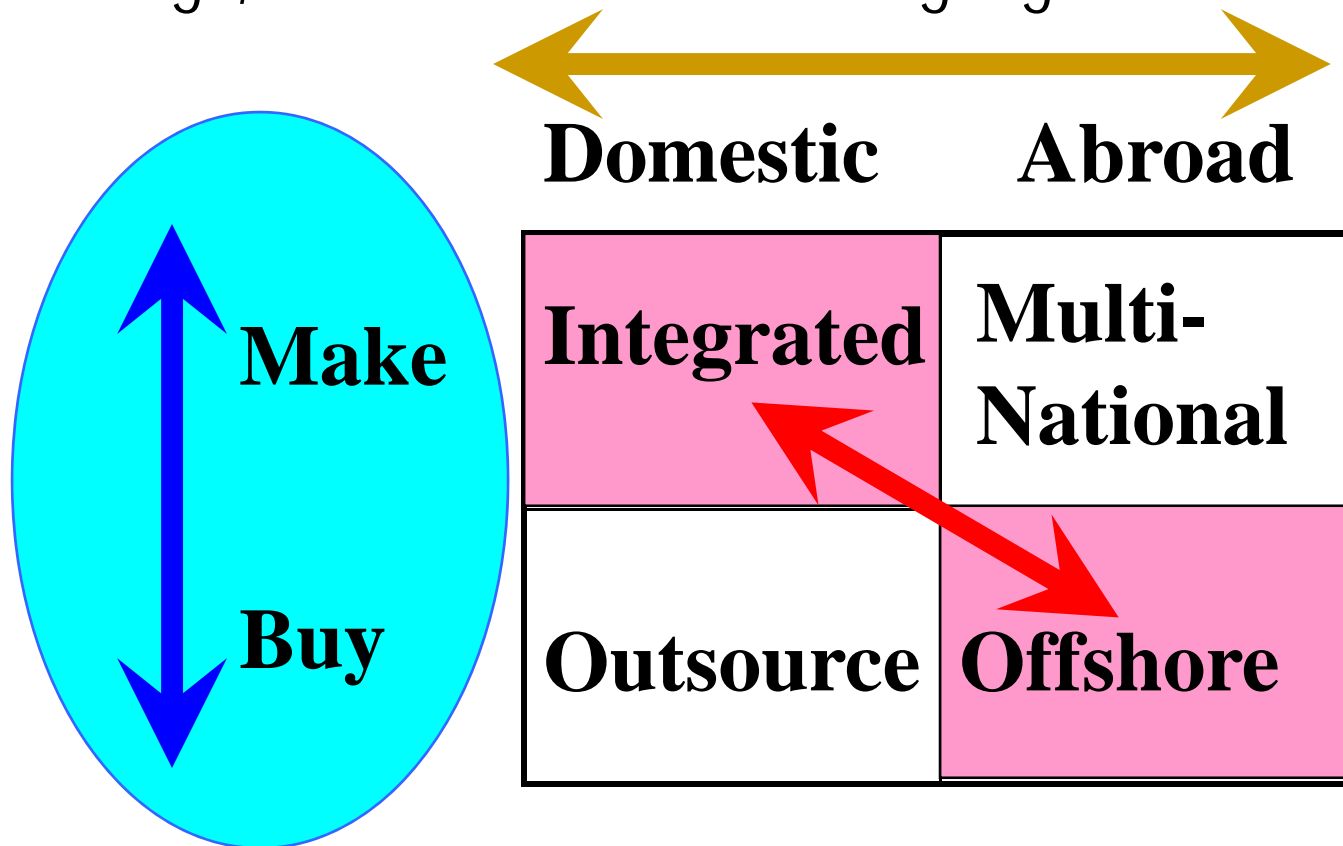
Is there a Trend?

- Deloitte Consulting surveyed 2005:
 - One-quarter of 25 large companies had brought functions back in-house after realizing they could do the work themselves more successfully and at lower costs.
 - 44% said outsourcing didn't save any money
 - Nearly half identified hidden costs as the most common problem when managing outsourcing projects.
 - Conclusion: companies embrace outsourcing to **cut costs, simplify projects**, and **tap expertise** not found in-house, but learn that unexpected complexity, **adds cost and friction**, requires **more senior management attention and skills**.
- InformationWeek's 2005 survey:
 - 45% blame failures on **poor service** and **lack of flexibility**
 - 39% point to **hidden costs**.



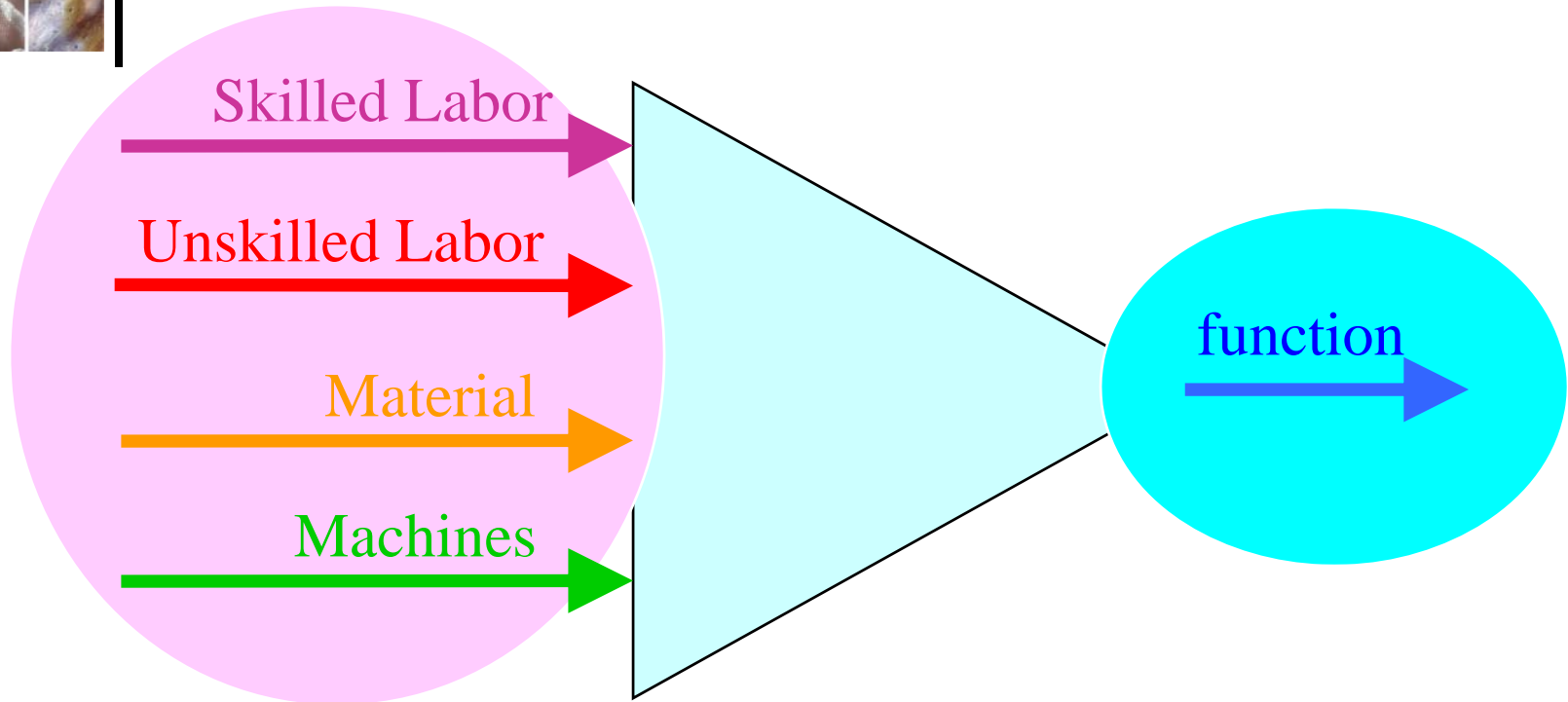
Some Terminology

- We tend to use “outsourcing” rather casually for many things, so here’s some finer language:



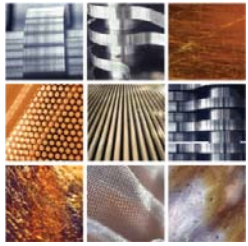


The Component: Make or Buy?



Alternative Question: **Buy or Buy?**

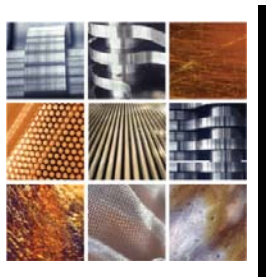
- **Buy:** Buy performance/function (FP)
- **Make:** Buy inputs and integration (C+)



Pros and Cons: Buy

Contracting for performance

Pros	Cons
Productive Efficiency: “What” not “how”	Describing and enforcing performance is costly
Spell out outcomes and define milestones	Changes require costly adaptations
Use market mechanism (RFPs)	Expose yourself to Opportunistic bidding
Focus on core business and increase efficiency	Lose expertise that may be valuable for future



The Innovative Organization

The leading questions:

- What are my **products** components?
- What **support functions** do we use?
- What are the **costs and benefits** of outsourcing?
 - contracting costs / need for flexibility
 - agency costs / opportunistic hazards
 - Strategic competencies / long run markets
- Learn the off-shoring risks before diving in!