

Outsource only what you can afford to give up

Minneapolis Star Tribune

Robert W. MacDonald, June 21, 2004

Management rhetoric these days promises a magic bullet to reduce costs, increase productivity, achieve growth and increase profitability—all while freeing up time to concentrate on “important issues.”

Some call it “outsourcing.”

It is difficult enough to pick up a business magazine or attend a meeting and not have people talking about, proposing or implementing outsourcing, which has quickly become the Atkins diet of management reduction. There are those who would have us believe that if we hire “experts” (them) to do our job, then our job will be easier. Of course, any job is easier if we don’t have to do it. But the job of management is to manage.

WHY OUTSOURCE?

Managers are constantly reminded they are not in the computer-processing business and should therefore outsource that process to those who are. We are also told government regulations in personnel are so complicated that payroll and employee benefits are distractions from the “real job” of the company, so “human resources” should be outsourced.

Remember the last time this outsourcing mania reared its head, and recall there were even those who recommended totally outsourcing employees and “leasing” them from another company that specialized in employee relations.

Other areas perceived to benefit from being outsourced are customer service, product fulfillment, distribution, marketing, and manufacturing. If taken to the extreme, it would be possible to outsource every company activity so that executives would be left to do what many of them do best: nothing. But even that can be outsourced, by hiring management consultants to do the thinking and planning.

BEWARE ‘ANTI-SELECTION’

We should not accept one simple solution to management challenges. Outsourcing can be an effective tool, but it is hardly nirvana.

The management of a company must always control those functions that are critical to the company’s success or failure. We call this avoiding “anti-selection,” which means if you give someone else the power to “anti-select” against the best interests of your company, eventually they will.

A company’s future mandates that you never relinquish control of three critical functions: product development, distribution and customer service. It’s OK to outsource janitorial services, parking lot management and printing. If they go bad, you may be irritated, but you are not out of business. But if customer service or distribution go bad, you go down.

Information technology is a shining example of a company function that is tempting to outsource. Why? It is expensive, confusing, mystifying and frustrating. IT activities chew up an inordinate chunk of the operating budget, require large numbers of employees and have an insatiable appetite for continuing capital investment.

The temptation of the outsourcing pitch is always the same: “Let us relieve you of the IT (or whatever) function. We are the leading experts in the field. We can reduce your costs, improve output, manage the geeks and eliminate the need for capital investment. Best of all: You don’t even need to be involved.”

That can be persuasive. Since they specialize in IT processing, they have more expertise than you can afford. Since they have 10 clients instead of one, expenses can be lower. And the technology is always state of the art. But those advantages come with a different kind of cost. When you give up control of critical functions such as IT, you give up control of the oxygen system of the modern company. Your IT function may be expensive and difficult to manage, but it’s yours to manage. When you outsource IT, you may reduce short-term costs, but you lose control over a function that can make or break your company.

What happens if you outsource IT, get rid of all your machines and employees, and then the outsource company goes out of business, is sold, or simply does not perform as promised? Will you sue them while you go out of business?

When I was hired as CEO of a large company, I learned that management had violated the fundamental rule by outsourcing control of product, distribution, and administration. But they kept parking lot management, printing and IT in house.

At first management was able to reduce costs, increase production and appear to be profitable. However, when the products provided by the outsourcers turned bad, the distribution was diverted. And those providing customer service didn’t deliver.

The company nearly failed. By outsourcing activities critical to its success, management had effectively given up control of the company’s future.

By recapturing control of product development and distribution and recovering the ability to issue and administer its own business (a goal that was accomplished by acquiring the outsource firm), the company turned around and became a star performer.

The decision to outsource is very simple. The key is to look long term, not short-term, and then calculate the impact on the company if something goes wrong—because it will. If the function is not critical to the long-term success of the company and you can survive the worst that can happen with outsourcing, then it should be given strong consideration.

If that is not the case, then walk away.