

# Winning in the Digital Economy

**W**hat in the world is going on in business these days? If you're confused about all this talk of supply chain management (SCM), application service providers (ASPs) and outsourcing, rest assured — you're not alone. Steve Case, chairman of AOL, recently said "There is probably going to be more confusion in the business world in the next decade than there has been in any decade in history." As you try to sort out all this confusion, you've probably heard that you need to outsource your non-core competence functions and focus on the key



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attributes of your business strategy. Ed Yardeni, chief economist at New York-based Deutsche Bank believes that "outsourcing is the basis for all prosperity." But wait, there's more to it than just trying to follow the lead of organizations like Cisco and outsourcing all your superfluous departments like human resources, procurement, and accounting.

With the rapid introduction, adoption and use of the Internet and e-com-

merce throughout the enterprise infrastructure, effective supply chain management (SCM) has received a renewed examination. The shape and future of your SCM process has been changed forever with the Internet. In this age of increasing technological globalization and maturity, the road to market leadership is paved with operating excellence and effectiveness. Establishing a superior electronic or e-SCM process — the making, buying, moving and selling of your products or services — can help your company achieve the competitive advantage necessary to become an



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industry leader. What was once a theoretical exercise and often perceived as a non-strategic business activity two decades ago is now one of the hottest competitive weapons and differentiator. E-SCM is clearly becoming the next battleground for corporations worldwide.

To thrive in this fast-paced e-commerce world, your organization needs to structurally transform your internal IT and SCM foundation just to survive, let alone to be effective. You need to re-examine your internal processes, applications and infrastructure, and realign

your inter-enterprise strategies, supply chain management, and business operations with the new business rules of e-commerce. In short, you need to start getting ready now for an organizational model that will be virtually unrecognizable in the future. Management guru Peter Drucker believes that “the corporation as we know it, which is now 120 years old, is not likely to survive the next 25 years. Legally and financially, yes, but not structurally and economically.”

### What does it take?

So, what does it take for companies to

thrive given the emerging trend of outsourcing e-commerce and supply chain management? Let's start by examining the combination of outsourcing, technical infrastructure and strategy, and the role that they co-operatively play in maximizing the management of today's IT solution. Whether you choose to keep the process in-house or move to an outsource provider, identifying your key technological and business process components and a solid understanding of your key business requirements is essential in determining the right strategy for execution.

Too many organizations find themselves caught up in the excitement of the Internet and believe that by “Web-enabling” their SCM applications, that they have magically met this new requirement of e-commerce or e-business. Others seek to use electronic messaging or limited data-sharing across the Internet — also believing that they have met the Internet challenge. However, only those organizations that have recognized that by moving the tools, systems, and business processes outside of their organizations are truly recognizing the power and capability of the Internet and outsourced activities.

### What's your strategy position?

One of the first things you must do is decide where your organization is with your overall SCM strategy. Because outsourcing the supply chain means something different to different organizations, your SCM outsourcing strategy must be in concert with your suppliers and customers. Historically, larger enterprises looked to outsourcing as a niche activity with a high degree of integration, or the justification for developing an internal hosting environment. In short, they see the smaller-sized organizations as a part of the procurement side of their supply chain.

Additionally, these same smaller sized organizations looked to outsourcing as a way to enjoy the levels of service and technology capabilities that larger organizations enjoy. In general, smaller-sized organizations see the larger enterprises as a part of the customer side

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of their supply chain process. Hence, your organization needs to examine its existing SCM strategy (on both the procurement and the customer side) to be able to focus your IT outsourcing strategies accordingly.

### Deciding factors

When considering outsourcing, there are three major components of any service level decision. They include:

- the ability to access remotely-hosted applications as services are delivered over a wide area network;
- contractual services to deploy, host, manage, or rent access to an application, or secure a business service from an external centrally-managed facility or organization; and
- the enabling technologies that will pull together your trading partners and information into an open, collaborative environment.

Companies are aligning themselves with business partners to carry out services that can be performed more efficiently outside the four walls of their organization. These relationships enable an organization to focus its core competencies on the fundamental drivers of its business, such as product, brand and customer.

Companies are no longer just procuring IT products; they are buying services and that means it's critical that your IT specialists understand how to successfully choose and manage the partners that will ultimately drive growth, value and profit. When identifying the service level of your outsourcing partner, you'll need to differentiate between the core services that are offered, the managed services that are offered, and the extended services that are available from outsourcing providers.

### When should you outsource?

Outsourcing may be an appealing option for an organization that is looking for a way to get ahead. One of the benefits of outsourcing SCM systems and processes is the ability to capitalize on the expertise and the best-practice experiences of the outsource provider. To be successful, an outsourcer must have a core competence in its specialty areas and those areas must align with your business model. Powerful synergies can be achieved by combining these skills with your company's own core competencies. Your organization can capitalize on the outsource provider's knowledge to enter new businesses, enhance operational effectiveness or gain additional value from existing assets.

When selecting an outsourcing partner to pursue new opportunities, the emphasis should be on obtaining essential skills. Some examples of when to pursue such an outsourcing opportunity include:

- **Gaining expertise for a new business process or technology.** An organization may desire to enter a new business market or implement a new technology but may also lack the in-house expertise to do the job effectively. For example, a "brick and mortar" company may have plenty of expertise with their back-office systems, but it may need different supply chain expertise to launch an e-business operation. Competitive time pressures can preclude your ability to grow the expertise internally and eliminate any luxury of learning through mistakes. By bringing in an outsourcer to share its expertise with you, rather than learning new methods and techniques from scratch, your organization may be able to launch its e-business SCM processes sooner and more effectively.
- **Enhancing integration.** Many organizations have disparate pieces of business activities, processes, and technologies that have evolved independently over time. Rather than selecting an outsourcer to simply maintain a disparate, existing environment, your company could choose an integrator with the experience to merge multiple systems and technologies to provide the greater overall value to your organization. As part of any engagement, an outsourcer must be able to consolidate and rationalize multiple sources of your organization's information.
- **Making better use of existing assets.** Outsourcers can have an inventory of best practices from working with many different types of organizations. Combining these best practices with a fresh, outside point of view can enable the outsourcer to leverage your existing assets in ways that would otherwise be missed. For example, a company may have a robust procurement application whose life could be extended and the value enhanced by being Web-enabled or made available to your employees via your corporate intranet. Another possibility is to use your outsourcer as a change agent to identify and license a promising internal technology to the other members of your supply chain.
- **Improving efficiency or lowering costs.** Improving efficiency and lowering costs are two of the most valuable reasons why any organization should consider outsourcing. Your outsourcer, through their efficiencies of scale and replicable best practices, could improve your efficiency, save money, or do both by getting things done sooner, for less money, or getting more work done for the same cost. In the right situations, some outsourcers can even guarantee specific levels of savings. A classic example of improving efficiency and lowering costs is the outsourcing of data-processing operations. Hardware

outsourcers reap considerable economies of scale and could provide your organization access to technologies you could otherwise not afford.

### When outsourcing doesn't make sense

There are a number of situations in which outsourcing makes sense and can be an attractive option for your organization. However, before you assume that outsourcing is the ultimate solution or alternative, the following are some specific circumstances that can severely restrict or even eliminate the benefits your company might receive from an outsource provider:

- **A very troubled IT organization.** An IT organization may have a level of systemic problems that might be beyond any outsourcing organization's capability to repair. Although it is tempting to hand off your entire problem to an outsourcer, doing so is bound to bring failure. No competent outsourcer would voluntarily step into that situation, recognizing that it cannot possibly resolve such a large-scale problem. An unsophisticated outsourcer might take on the challenge, but most likely would fail to turn around those IT problems in your organization. Also, an IT organization that does not have a handle on its own operations cannot hope to successfully negotiate a fair outsourcing contract, set the appropriate service levels, or co-ordinate all of the transition activities that are required successfully with the selected outsourcer. For all of these reasons, very troubled IT organizations will need to make improvements before any outsourcing is possible. In some cases, a service provider might be willing to assist your organization in making those changes and then provide some outsourcing services after appropriate controls are put in place.
- **A situation that limits the outsourcer's ability to apply improvements.** To apply available improvements and make the total outsourcing engagement profitable and successful for your organization, an outsourcer must have control over certain aspects of the service being provided. For instance, an outsourcer will have its own processes and best practices that it uses to achieve certain productivity and quality targets. By placing certain limitations on the outsourcer, you will prohibit the enhancement of these processes, which can make the engagement economically unfeasible for both the outsourcer and your organization.

- **The inability to define good measures.** Essential to any outsourcing contract is the definition of service levels requirements. An outsourcer should commit to providing a set of service levels to your organization, and the outsourcer's performance should be measured by its ability to achieve these targets. Service levels will be set and should be based on the actual measures and rates currently in place, and being met, by your existing IT organization. If your IT organization is unable to quantify and identify these crucial measures before or during the negotiation process, then the service levels specified in the outsourcing contract will be inherently unreliable, leading to mismatched expectations and an ineffective outsourcing agreement.

### Selecting the right outsourcing entity

Every organization has operational functions and business processes that could potentially benefit from the use of outsourcing. Selecting the right service provider is one of the most important challenges facing an organization that is considering outsourcing. The choice of a candidate and the type of outsourcing selected are highly interrelated. For example, a candidate well suited for a supply chain engagement may be significantly less attractive when considered for another type of outsourcing. Further, the most obvious candidate may not be the most successful nor provide the highest benefits. Selection of the wrong candidate can doom an engagement before it starts. Even the best outsourcer cannot make a winner out of a losing project, and organizations tend to blame outsourcing (and the service provider) for that failure, rather than the inappropriateness of their own selection process.

The characteristics of your ideal candidate are largely defined by the overall goals of the outsourcing effort. Determining the appropriate candidate is usually accomplished through "degrees of fulfillment" rather than the simple "yes or no" decision of functionality support. The lower the average degree of fulfillment across the selected process, the more tightly coupled the outsourcer must be with your company's operations. Your outsourced SCM solution must go beyond the traditional application-hosting concept to create a new value premise for your organization's new e-business models.

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