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TRAVELING A DIFFERENT ROAD

Middle-market companies have different attitudes than their larger and smaller peers



By Anthony Baldo

Like middle children, middle-market companies seem to think differently than their larger and smaller competitors...especially when it comes to outsourcing.

This is apparent from The Outsourcing Institute's Sixth Annual Index, a survey of 1,911 of its members.

At first blush, middle-market companies do what others do. Companies with more than 1,000 employees but fewer than 5,000 mostly outsource technology, administration and manufacturing, just like corporations with fewer than 1,000 workers and more than 5,000.

But there are differences in how companies of varied sizes think, and even within the middle tier itself. For example, while information technology is overall the most popular outsourcing choice, mid-market companies do less of it than firms with fewer than 1,000 workers (47%) and 5,000 to 9,999 (62%). Only 39% of the companies with between 2,500 and 4,999 workers outsource IT, and just 45% of those with 1,000 to 2,499 employees do.

View Charts

- Which stage are Mid-Size Companies at?
- What Mid-Size Companies are Currently Outsourcing
- What Mid-Size Companies are Considering Outsourcing
- Top 5 Reasons Mid-Size Companies Outsource

Then look at administration. At least 30% of the companies in each of the four segments of companies with fewer than 10,000 workers outsource it, but it's especially popular with the 1,000- to 2,499-worker crowd (48%).

That the figures tumbled out this way isn't surprising. One director of IT says a company loses much intellectual capital when it outsources IT, perhaps explaining middle-market

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companies' reluctance to make a deeper plunge.

They don't, however, face as much of a risk with administration outsourcing. "Administration is perceived as one of the less strategic components, with little loss associated with intellectual capital," says Tandy Gold, who founded and still coordinates the Offshore Interest Group, an organization of outsourcing executives from Fortune 100 companies that meet monthly by phone. "So you get pure-play savings with little perceived negative impact." Thus, administration outsourcing pays much bigger dividends for middle-market companies than they do for larger ones, she adds.

"Larger firms can more than likely create shared service departments that are cost efficient within their own company," says John Ruther, director of outsourced services for CHEMCENTRAL, the world's largest independent chemical distributor. "In order to obtain the same economies of scale, the middle-market firms have to outsource." At least 14% of the respondents in the four sectors with fewer than 10,000 workers outsource manufacturing, but the small and big ones (both 19%) do so the most.

Real estate and facilities management outsourcing was common (22%) within the 2,500- to 4,999-employee group, but that still paled to what smaller- and larger-sized companies are doing in that area. Data capture (23%)

was more typical among the 1,000- to 2,499-worker types and really didn't show up as a current outsourcing choice in other size sectors.

Naturally, anecdotal evidence shows that some middle-market companies are being creative with their outsourcing choices.

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Take Polo Ralph Lauren, for instance. Some 95% of its merchandise flows through its Greensboro, N.C., distribution facility, so the company can't suffer downtime. Backup generation is being outsourced to Duke Power, which provides a diesel generator and monitoring services.

Middle-market companies' aspirations for their outsourcing programs aren't as big as those of their small and large counterparts, either. Of course, IT tops everyone's wish list; half of the respondents with 1,000 to 2,499 workers are considering it, and 53% of the 2,500 to 4,999 bunch is. After that, firms in those two middle-market subsectors set their sights on administration (34% and 36%, respectively) and human resources (16% and 18%, respectively).

That's a far cry from the companies with fewer than 1,000 workers, who would make Santa blush with all the outsourcing projects on their Christmas lists. According to the survey, the outsourcing motivations of companies really don't differ all that much. Middle-market companies are more bent on outsourcing as a means of controlling operating costs; 61% of companies with 1,000 to 2,499 workers say that's the primary reason for outsourcing, while 63% of their 2,500- to 4,999-employee counterparts say so.

Smaller and larger companies were actually more motivated by the improved focus outsourcing provided them. It naturally follows, then, that price would be a driving force behind middle-market outsourcing choices, and it is. Some 71% of companies with between 1,000 and 2,499 workers cited price as the most important factor when picking an outsourcing vendor; 68% of their bigger middle-market brothers with 2,500 to 4,999 employees felt the same way. Compare that with firms with fewer than 1,000 staffers (57%).

"This may be more the politically correct answer than the truth," says Gold. "Relationship is not something individuals tend to respond to in a questionnaire. Actual decision-making

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shows that cost is just one of many factors, not the least of which is, can I establish a long-term, successful business relationship based upon mutual trust with this [outsourcing] firm?"

Cost can be a highly overrated factor. When Polo Ralph Lauren was experiencing continuous system outages in the Northeast four years ago, the menswear and fragrance company decided to outsource and get the expertise they needed. That was achieved. But besides not building enough growth in a five-year contract, costs were 2.5 times what they were before IT was outsourced, says Terry Land, the company's senior director of IT. Now, he notes, Polo Ralph Lauren is considering bringing IT back in house.

In fact, 52% of the companies with 1,000 to 2,499 workers say that finding the right expertise is a major problem they are experiencing with outsourcing. Cost containment doesn't seem to be a lingering issue. How can it be? CHEMCENTRAL's Ruther notes that it's extremely difficult to justify outsourcing a process in which the farmed-out service returns soft-dollar cost savings, such as error reduction or more time availability. "These typically will not reduce the workforce and show up as an additional expense line in the financial statements," he says. "Return on investment is quite difficult to prove."

Ruther says he asks outsourcing vendors to either guarantee hard-dollar savings or increased revenues. "Although price is a major factor, the vendor's financial strength and stability are keying partnering with us, says CHEMCENTRAL's Ruther. "Long-term relationships are important. This strategy worked well in the IT area during the early part of the decade when many service providers disappeared from the landscape."

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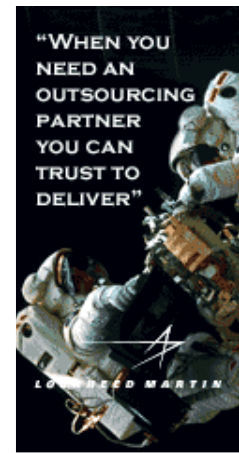
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