

Is outsourcing an option for startups and SMEs?

Why is outsourcing important?

The economic integration and the growing competition between well-established organizations and startups in the global and local markets are some of the factors that are forcing companies to vertically disintegrate some of the activities that previously would have been done in-house in order to stay competitive.

Among the main challenges that companies face in the current context, we can mention:

- Pressure to reduce costs
- Changes in consumer demand
- Tighter regulation of markets
- Fusions and acquisitions
- Business consolidations
- Disappearance of competitors
- Sales of business areas
- Influence of competitors

Consequently, the business processes that can generate greater value (or greater risk) for a company must be oriented towards the support of its strategy, in order to keep its products and services technologically valid, so that they provide the maximum quality and service to a company at a lower cost.

The majority of the startup community agrees that outsourcing the right jobs can mean the difference between breaking the bank or maintaining the budget. Outsourcing can save you 60% on overhead costs and the successful companies use this to their advantage.

Current technologies, as well as a world economy based on services, offer innumerable opportunities for startups and SMEs to increase profits while keeping operational costs down through an adequate outsourcing strategy.

Definition of outsourcing

Outsourcing can be defined as:

Systematic acquisition, total or partial, and through external suppliers, of certain goods or services necessary for the operation of a company and are goods or services linked to your activity.

The proposed definition explains outsourcing as a management technique, which involves the transfer to third parties of certain complementary processes that are not part of the main activities of the company or business, allowing the concentration of efforts on essential tasks in order to obtain competitiveness and focus on results.

Outsourcing always refers to functions, activities, tasks or processes, given that, even if the decision is related to buying goods instead of manufacturing them in our own plant, what is actually being outsourced is the activity or process of acquiring something, rather than the thing itself.

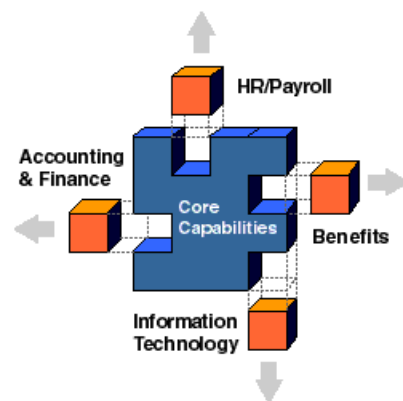
The importance of outsourcing is that it concentrates the company's efforts on the main activities of the business. In this way it is intended to provide greater added value for customers and products, while reducing processing times and even, in most cases, reducing costs and the amount of staff needed to operate. At the same time, this also potentializes individuals' talents.

What should and should not be outsourced

Areas or activities that benefit from outsourcing

There is now a concrete and obvious global trend in favor of outsourcing. Outsourcing can be applied to most areas of the company. These are the ten more commonly outsourced activities:

1. Financial systems;
2. Accounting systems;
3. Marketing activities;
4. Human Resources;
5. Administrative systems (IT management);
6. Outsourcing of secondary activities, including surveillance, cleaning, stationery supply, storage, and event organization, among others;
7. Production activities;
8. Transportation;
9. Sales and Distribution related activities;
10. Procurement process.



Outsourcing of the activities mentioned above can be total or partial:

- **Total outsourcing:** Involves the transfer of equipment, personnel, networks, operations and administrative responsibilities to the contractor.

- **Partial outsourcing:** Only some elements of the listed activities are transferred out of the company.

Areas or activities that should not be outsourced

The following are activities that should not be subcontracted under any circumstance:

- Strategic planning and management;
- Treasury;
- Control of suppliers (including those who provide outsourced services);
- Quality Management;
- Sales strategy.

Pros and cons of outsourcing

As with any other strategic decision an organization can make, outsourcing has its pros and cons. All of these should be taken into account when analyzing how to structure the new or existing company:

Pros

- **Cost reduction:** outsourcing usually means a reduction in total costs for the company. While this is usually easily quantifiable, supervision and coordination costs should be taken into account when working on the business plan.
- **Cost variability:** when outsourcing, many fixed costs are transformed into variable costs, as large structures are no longer supported and now costs are only proportional to the services or goods that are received from external suppliers.
- **Reduction of the administrative structure and its operational problems:** the benefits, in this case, come from having a smaller number of people to manage, which usually allows concentrating on motivating and training the key staff, with the purpose of obtaining satisfactory and lasting results.
- **Capital release:** when capital is released for other activities or profitable projects in line with the company's strategic objectives.
- **Improvements in quality:** when finding specialists, substantial improvements in the quality of the services and products obtained are usually obtained. This improves the company's position in the market.
- **Access to more and better technology:** outsourcing to a specialized supplier allows the company to possess the best of technology without the need to purchase it while making sure it is kept up to date.

Cons

- **Instability in supply:** While a written contract is used when hiring suppliers, breaches of the deadlines for the provision of services or delivery of goods, quality deficiencies, and changes in prices in the short term might be some of the challenges the company might face.
- **Data protection and confidentiality:** confidentiality may be lost if data is not well handled by service providers, which can cause major disruptions to the company and its reputation.
- **Idleness and demotivation of the staff:** if the company is already operational and decides to move forward with implementing an outsourcing strategy, there will be staff with reduced or canceled tasks, which will cause demotivation and discouragement, which can be transferred to the rest of the staff.
- **Greater dependence on third parties and possible losses of control:** the results are controlled, but not the processes of external companies, which is a negative element for the final efficiency and for the independence of the organization that outsources because it is tied to the provider and begins to depend on it.
- **Competence:** when learning and having knowledge of the product in question, there is a possibility that the supplier will use it to start their own industry and become a competitor of the company.
- **High replacement cost:** the cost of changing a supplier in case the selected one is not satisfactory can be high if there are not many options available in the market. In addition, a company cannot always change providers immediately, which increases costs even more.

Flexibility of Outsourcing

Other often overlooked benefits of Outsourcing are related to the capacity of the suppliers to adapt to the rapid changes in demand and constant technological advances. Some of these benefits are:

- Permanent adaptation to the client's requirements;
- Staying tuned for technological changes;
- Adaptation to legal changes;
- Creation and maintenance of contingency plans and risk mitigation;
- Permanent training of staff;
- Ability to modify the service or goods provided, according to the needs of the company.

Strategies for Outsourcing

When a company decides to carry out an outsourcing process, it must define a strategy that guides the whole process. There are two basic types of outsourcing strategies:

1. **The peripheral strategy:** when the company acquires activities of little strategic relevance from external suppliers.
2. **The central strategy:** when companies contract activities considered of great importance to their long-term success.

The chosen strategy must be clearly defined in order to ensure that the process is governed by the company's outsourcing guidelines. The employees must be aware of and involved in this process and supported by senior management.

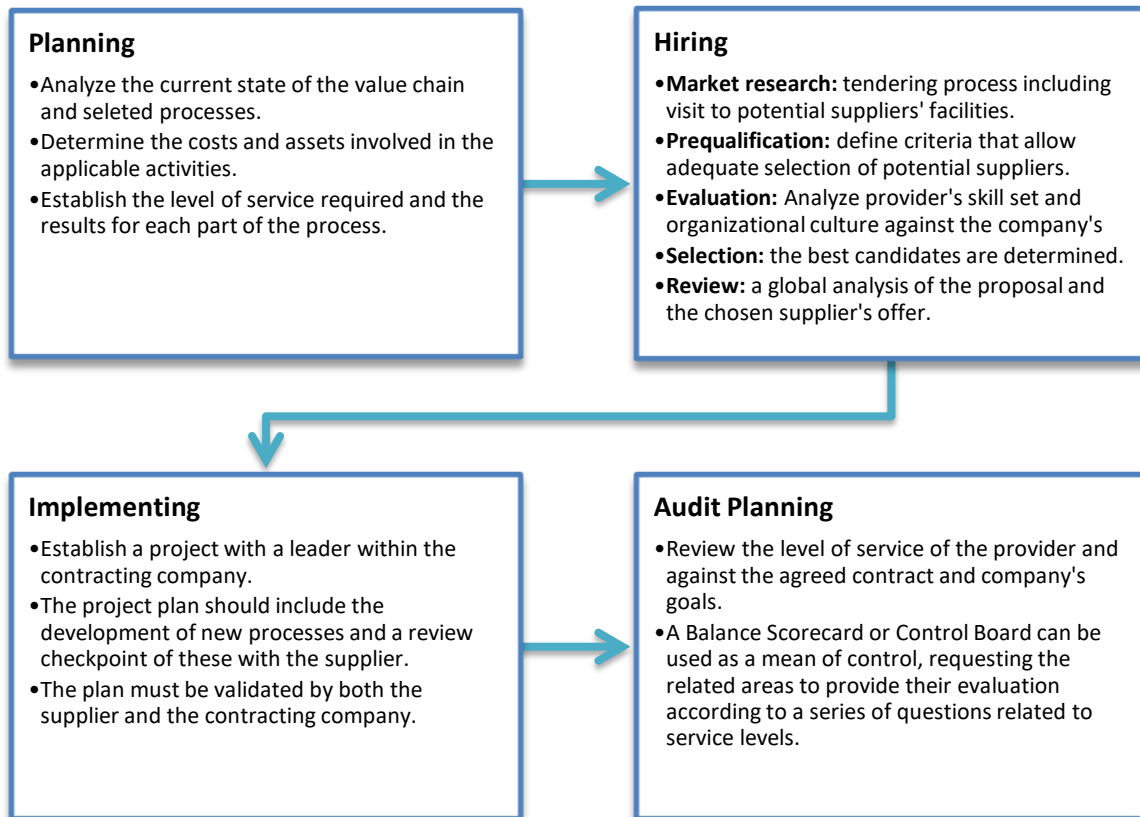
Another aspect to be defined is the type of relationship between the company that contracts and the supplier.

Currently, organizations seek more formal and long-term relationships where the internal team assumes a strategic partner role, which allows a better understanding of the development of the supplier's strategy.

The advantage of this type of relationship is that it allows both parties to become familiar with the staff and the operating style of the other company and helps the supplier to meet the contractor's expectations more effectively in terms of communication and frequency in the reports.

Stages of outsourcing

The methodology described below is applicable to all outsourcing processes. The company needs to consider its needs, sector, and environment when creating preparing the different activities within these stages.



Success factors for any outsourcing project

While the previously mentioned steps are the minimum requirements needed to plan and execute an outsourcing strategy, there are some general rules which can be used as a guide while creating and implementing the company's outsourcing project.

Clear goals	The client must have very defined goals
	The supplier's performance must be measured against these goals.
Realistic expectations	It is important to set the border within the limits of what is possible.
	The hiring company should look references within its industry to understand what the similar organizations are doing.
Commitment from the client	Outsourcing requires highly qualified resources from the client, who can exploit their potential benefits through proper management and supervision functions.
Detailed info of included services	The client must ask the supplier for a clear and precise definition of all the services included in the contract to avoid surprises later on when the actual services are delivered
Clear service levels	Each service must have associated parameters for measurement of its performance.
	Progress can be monitored by a battery of indicators, to take preventive or corrective measures as necessary
Financial flexibility	Any agreement must be able to adapt to conditions that may affect the total cost of the commercial relationship between both parties.
Supplier's staff capacity	The supplier must commit to avoid both excessive staff turnover and to use the client's long-term contract as a school for their staff.
	A guarantee of continuity and minimum staff quality on the part of the provider needs to be agreed.
Management team's commitment	The success of any long-term project depends to a large extent on the continuity of the management team responsible for it.
	Leaders from both parties must be fully involved in the contractual negotiations. This is guarantees a long-term relationship.
Technology flexibility	To avoid technological obsolescence, the agreement must incorporate definitions and procedures for technological updating.
Operational flexibility	It is very important that the original agreement incorporates sufficient flexibility to change the operative terms or, even, the definition of the services provided, without resorting to tortuous renegotiations of the contract.

Is outsourcing good for a startup or SME?

There is no doubt that a world of scarce resources is dictating a reduction in managerial and operational staff. In fact, the morality of society itself has already signaled the end of waste

and inefficiency, particularly those affecting the natural environment. In this aspect, an outsourcing strategy embedded within the business plan is particularly interesting for startups and SMEs.

New companies should adopt one or more methodologies to implement outsourcing at some scale as part of their daily operations.

Several recent studies reveal that outsourcing is growing, while service providers are expanding their range of offers. This means startups and SMEs concentrating on their competitive advantages and their core business needs while keeping a healthy cost structure.

Organizations that are starting operations are able to think about the best way to produce, market and distribute products or services, and the best ways to do it, including whether they really need to have all the processes within their companies.

Summarizing, startups and SMEs are in the best shape to evaluate the possibility an outsourcing strategy may create since they can incorporate it from the very beginning of their business planning process.

New companies will adopt outsourcing more easily than traditional organization since they have the opportunity to design their business processes properly, from scratch, to be the most efficient, and not simply copy others in the industry.