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Teaching case

Crafting and executing an offshore IT sourcing strategy: GlobShop's experience

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Abstract
This teaching case discusses the decisions facing GlobShop, a global travel-retail company, in its efforts to offshore a significant portion of its information technology (IT) work. In response to the business challenges that arose due to the September 11, 2001 terrorist attacks, the company decided to outsource many of its IT activities to an Indian vendor. This case traces the key decisions made by the CIO and the challenges that were encountered during the planning and execution of the company's offshore sourcing strategy. These decisions pertain to the choice of tasks to be offshored, decisions about the vendor and the nature of sourcing arrangement, managing the vendor relationship and change management issues induced by offshoring. As GlobShop nears the completion of its 3-year agreement with the offshore vendor, the CIO is faced with decisions regarding continuing offshore outsourcing, extending the contract and related implications for the future of IT organization at GlobShop.
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Introduction

In November 2005, Roger Deen, the CIO of GlobShop, and his team of information technology (IT) Directors sat in a conference room at the company's headquarters in Boston to discuss the imperatives facing them. GlobShop was a five billion dollar firm that operated over 200 duty-free and general merchandise shops in airports, hotel lobbies and downtown locations across Asia, Australia, North America and Europe.[1] Being a niche player in the travel-retail industry, the company's performance swayed with changes in air travel, tourist traffic and related economic events. Since the events of September 11, 2001, GlobShop has been engaged in a series of cost-reduction efforts, including offshoring a significant portion of its IT work.

Roger was contemplating moving more IT work offshore. GlobShop has been working with an Indian vendor, Indo-Systems Solutions (ISS), to take care of application development, support and maintenance of merchandising and retail systems, and technical support for the company's IT infrastructure. These initiatives have helped reduce IT expenses by over 35%. The business leadership has demanded additional cost reductions and has suggested that Roger examine the possibility of pushing more projects offshore.

Within the next few weeks, Roger will have to decide whether GlobShop should extend and renew its outsourcing agreement with ISS. To reduce the risk of becoming 'over-dependent' on ISS, the company has been mulling over using multiple offshore vendors rather than exclusively relying on ISS.

Another issue that needed Roger's attention was the future role of the internal IT function at GlobShop. If the company decides to move more IT activities offshore, it should carefully assess its implications for the internal IT group. GlobShop had reduced its IT workforce by over 50% and additional cuts could simply decimate the IT function. With over 60% of the IT spending concentrated on offshore activities, Roger wondered about the future steps.

Background

'Duty' is a generic term used to describe a variety of taxes imposed on goods. Duty-free shopping enables international travelers to purchase foreign goods at lower prices. Merchandise such as liquor, perfume, tobacco products that are subject to high taxes and duties are hot products in duty-free stores. Duty-free shops are typically located in international airports, selected hotels, tourist attractions and other areas that are designated as 'foreign trade zones.'

Founded in the 1950s, GlobShop sold foreign cars and liquor in US military bases abroad. As the idea of duty-free shopping picked up in Europe, the company opened stores in selected European and Asian airports in the 1960s. Spurred by the growth in international travel in the 1970s and 1980s, GlobShop expanded its presence to airports in Australia, New Zealand, USA and UK. Soon, the company became a profitable player in the small but growing travel-retail market. Despite the entry of several global competitors, GlobShop remained one of the leading players in this niche segment. The company expanded into several countries by acquiring smaller players. In the late 1980s, the company opened large, duty-free specialty stores in a few major cities in USA and Europe. These stores were multi-department luxury retail outlets that carried a range of items including tobacco products, wines, liquor, confectionary, perfumes, jewelry, silverware, gift items, souvenirs, memorabilia, travel goods and other products.

The Gulf War in 1991 severely affected international tourism. Since airport retail formed a major portion of GlobShop's revenues, its sales slumped by over 15%. To compensate for the losses, GlobShop closed a few specialty stores and halted its expansion plans. As the business picked up, GlobShop acquired some smaller players as a means to enter additional countries. Soon, the company was organized into 10 regional business units as a decentralized set-up. However, acquisitions and expansion left considerable diversity in business processes, managerial practices, supply chain structures and systems across the company. Dan Cwik, Vice President of Retail Operations, elaborated:

> Our organization was very diverse in terms of business processes and practices. Different countries had different ways to handle duty-free shopping. In some nations, a customer could take duty-free products straight out of the store. In some other countries, they had to buy it in-store and get it delivered on the flight or at their destination. Some countries supported the concept of duty-free as well as duty-paid products. We had to deal with different supply chain structures and retail processes.

In the 1990s, Asian tourists, who had been targeted as the focused customer segment by the company, represented a high potential market. GlobShop was successful in attracting and establishing its name among Asian travelers. While this worked well initially, the changes in the global economy in the late 1990s caused considerable hurdles to GlobShop. In particular, the East-Asian economic crisis in 1997 created ripple effects in several Asian nations affecting stock markets, currencies and exchange rates, subsequently leading to economic recession. Triggered by these events, international travel and tourist spending declined, creating a snowball effect on GlobShop's revenues.

Corporate restructuring

In 2000, a leading luxury retailer (Lux) bought a majority stake in GlobShop. Lux owned several brands in wines and spirits, perfumes, cosmetics, watches, jewelry, fashion and leather goods. Through this acquisition, GlobShop gained access to famous brands and premier luxury items. GlobShop also had a new executive team. A troika of CEO, CFO and CIO took over the management of GlobShop. Their immediate task was to address the decline in corporate performance. An obvious challenge was to reduce costs drastically as well as improve profitability.

Instead of relying solely on airport stores, the management sought to actively expand into sea-travel retail. GlobShop acquired a cruiseline firm that operated port stores as well as on-board ferry shops. However, revenues from sea-travel retail formed only a small proportion of overall revenues. Therefore, the executive team began to aggressively pursue cost-reduction efforts. Proliferation of retail operations at different regions highlighted the growing need for more effective coordination of diverse operations. The senior leadership at GlobShop heavily debated on the merits and demerits of a centralized *vs* decentralized business set-up. Roger explained:

> Our airport retail is essentially a concession-driven business. In such a business, one must re-win the business every five years or whenever Government (or an airport authority) commences a RFP process for retail space. Decentralized operations allow all costs to be added or eliminated with each win or loss. A centralized structure has fixed costs associated with operations that cannot be reduced 100% when business is lost. Therefore, in a volatile environment, decentralized organization gives us the flexibility to add or reduce our operations and scale it according to business fluctuations.

A decentralized set-up also implied duplication of efforts and lack of standard processes that ultimately increase the operational costs. The leadership sensed significant savings by centralizing a number of activities. As a result, the management announced a reorganization by which GlobShop would streamline its business processes and reduce redundancies by adopting a major restructuring. This meant redefining a number of operational and management processes and centralizing them at the corporate level. Dan Cwik, Vice President of Retail Operations, noted: 'We had duplication of systems, people and processes throughout. We figured that we could consolidate a number of these and do them in a common way. So, we decided to take the costs out by standardizing and centralizing a number of our processes. And it was clear that information technology was the best route to achieve this.'

IT organization at GlobShop

IT operation at GlobShop was highly decentralized (Figure 1). Each region had its own IT division that catered to the local needs. A corporate IT group served the needs of the global headquarters in USA, in addition to providing shared IT services like email. Each of the 10 regional IT divisions functioned independent of each other and was

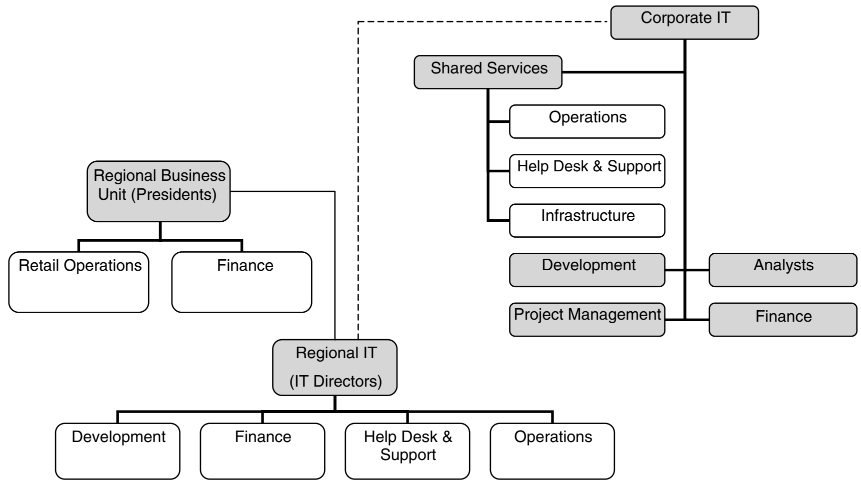

Figure 1 Decentralized IT organization.

headed by a regional IT Director who reported to the President of the regional business unit, with a dotted relationship to the corporate CIO. Each regional unit funded local IT projects and operated under a distinct IT budget. A natural outcome of such a decentralized set-up was duplication of applications, services and technology resources. Neal Parker, Director of IT, observed: 'We had several legacy applications that ran in different regions that were expensive to maintain and couldn't communicate with each other. We had multiple versions of the same application. Despite a corporate IT, the regional IT units functioned independently. This resulted in many redundant resources – infrastructure, software, hardware and people. All these added to our IT overhead costs.'

GlobShop had several legacy merchandising systems in the 10 regions. Each region also had a data center storing unit-level sales information. Further, GlobShop had SAP financials and Peoplesoft HR systems. For retail processes, the company had two different point-of-sales applications across the stores worldwide. GlobShop had a resource pool of over 300 IT employees across the 10 regions.

Centralizing IT management

In 2000, in order to facilitate the corporate restructuring effort, Roger was entrusted with the responsibility of consolidating the IT organization. Roger's mandate was to spearhead the realignment of GlobShop's regional IT set-up into a global unit, along with associated changes in business processes. A major IT reorganization would not only facilitate streamlining diverse business processes and systems worldwide, but also pave the way for significant cost savings. Roger's background was also particularly suited for the reorganization initiative: he knew the company's retail business well and had seen how an integrated operation could achieve efficiencies; he also had an international background with significant work experience in Asia-Pacific and North American regions.

Roger and his team embarked on an extensive study of regional IT units. Detailed information on the IT resources, applications and spending was gathered. Neal elaborated, 'It was an eye-opener for us. We had over 250 internally developed applications across the ten regions. These applications had over 15000 objects such as programs, databases etc and had over 5 million lines of code. We dissected our IT dollars and precisely knew how much each of the IT services cost us. We were spending much more than what we ought to be.' The analysis revealed that GlobShop was spending over 60 million dollars annually on IT. Reorganization would help them save more than one-third of these costs.

Roger had extensive discussions with IT Directors and business unit leaders at each of the 10 regions. Further, Roger convened planning retreats and brainstorming workshops that helped discover a number of issues. The presidents of the business units were concerned that the consolidation would distance the regional users from the IT group. Moreover, centralization also implied a significant loss of control over IT. Neal remarked: 'There was a lot of reluctance and resistance to give up local IT resources to a global pool. They felt they won't be any longer able to walk to a programmer's desk, make a request and get it fulfilled on-demand. There was concern that this was going to impede their ability to do what they have been doing and also take away their control. There was a tremendous amount of resistance.' Roger highlighted another issue: 'We were largely running our IT departments simply by managing-by-wandering-around model. Adopting a global delivery model with a centralized set-up required a very different set of competencies.' However, the high pressure to prune costs and the clear mandate from the top helped GlobShop move forward with its IT reorganization.

After studying the problems and issues, Roger proposed a three-pronged approach for the reorganization. The central idea was to consolidate the 10 regional IT units into one global IT unit, with all of the IT operations dispersed in two centers, one in Asia and another one in USA. The new IT vision was to have 'one global team without boundaries, delivering acknowledged value and exceeding customer expectations.' The highlights of the new reorganization were:

- *Centralized global IT budget*: Under the new arrangement, the funding for IT would be centralized. The regional IT units would no longer pay for the IT services directly but through corporate allocation and a charge-back system.

- *Streamlined IT governance*: Neal Parker, Director of IT, commented: 'We planned a new set of centralized, formalized processes in place about how we were going to manage our IT. Any major application development or IT-related service request had to be centrally submitted. It would be assessed, prioritized and resource allocation be made accordingly.' This implied serious changes in the way different functional and regional units interacted with IT. Further, all the IT initiatives would be classified into three categories: capital initiatives, expense initiatives and support related. While capital initiatives were to be decided and driven by business, expense and support initiatives would be handled by the IT unit.
- *Consolidation and standardization*: IT operations at the 10 regional centers were to be consolidated into two hubs, one in USA and one in Asia-Pacific. Twenty AS 400 systems operated at the regional centers would be consolidated into the two hubs. Multiple instances of the applications would be minimized and information stored in a centralized data repository.

As a part of the reorganization, GlobShop decided to cut its IT costs by outsourcing a part of application support and maintenance. In November 2000, GlobShop hired an Indian vendor, Indo-Systems Solutions (ISS), for on-site maintenance and enhancements of the merchandising system. The vendor's responsibilities included documenting the system, deploying its staff on-site in USA for technical support and undertaking minor enhancements.

The journey offshore – formulating an offshore sourcing strategy

Impetus for offshoring

The events of September 11, 2001 in New York severely affected the air-travel sector. There was a sharp decline in passenger traffic as several airlines cut back their flight schedules. Movement of international tourists reduced drastically (Figures 2 and 3). All the major airport retailers, including GlobShop, were hit hard by the drop in passenger traffic. This made cost cutting that much more imperative for GlobShop. The company suffered a severe setback when it was still implementing its reorganization. Dan Cwik said: '9/11 created havoc. Fewer passengers meant fewer dollars, cash flow crunch, store closures, halting expansion. We had to cut costs drastically. We realized we had to make some radical changes.' These provided the trigger for offshoring IT tasks and realizing significant savings. Roger explained: 'After 9/11, we looked down the barrel of having to transform the way we run our business. We looked at offshoring as a means to do that.'

Finding the partner

Roger and his team began by looking at potential offshore locations and vendors. They assessed Canada, Eastern Europe, China and India. Roger recounted: 'I looked at different geographies and at that time Eastern Europe was a bit unstable. China was emerging but I had concerns about IT protection and intellectual property issues. India was the most matured segment with lots of players and a good legal system in place.' The team visited a few vendors in India, including tier-1 vendors like Infosys, Wipro, other smaller vendors, and decided to work with ISS. Explaining the choice of ISS, Roger said: 'At that time, ISS was a medium-sized, yet growing company. I didn't want to work

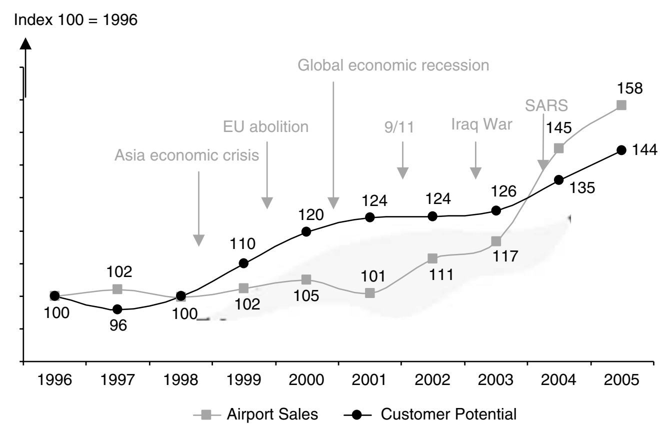

Figure 2 Major economic events and airport retail sales.
Source: Generation Group, Sweden.

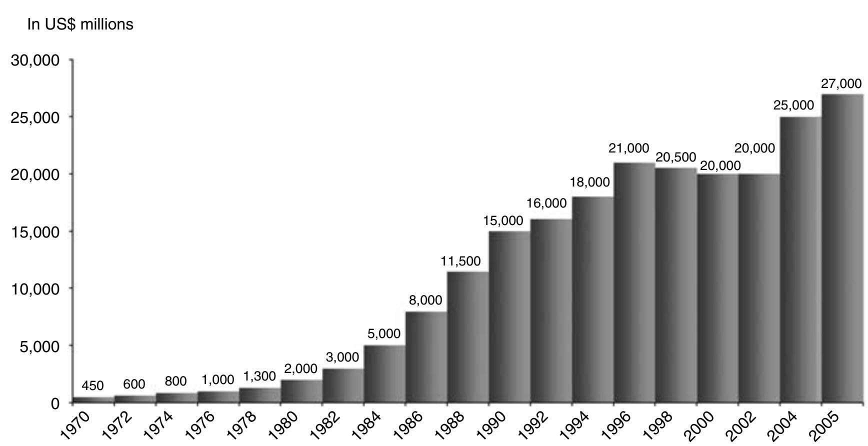

Figure 3 Global duty-free and travel retail sales.
Source: Generation Group, Sweden.

with any tier-1 Indian vendors because I didn't want to be so small that I was insignificant to them. I wanted to be a meaningful client to the partner so that I could get the attention I needed. Moreover, we were only starting out on offshoring so I had to have the flexibility to change or pull out when needed.' Another factor that weighed in favor of ISS was that it was a 'hybrid' offshore firm with presence in both USA and India.

Testing the offshore waters

Initially, GlobShop outsourced only a small piece of production support, in order to minimize risks and assess the benefits from offshoring. After the events following 9/11, GlobShop decided to extend its relationship with ISS to hand over all of its production support for its merchandising system and few retail applications. The basic idea was to achieve a complete 'follow the sun' model for production support where ISS began taking requests from data centers and business users from around the geographical regions. GlobShop entered into short-term agreements with ISS on fixed-price terms as it learned about the vendor and experimented with the best ways of making offshoring work. There were some initial kinks that had to be worked out. Neal remarked: 'We found that the on-site resources were not as effective working with our business partners as we had hoped. So we sat down with ISS and talked to them about that, and two things happened. They changed some of the people and their process. And, we took more responsibility for the relationship and adapted the onshore/offshore model to work better in our environment.' ISS deputed Rahul Sharma as the on-site manager to coordinate and oversee the projects at GlobShop. Rahul brought two more managers from ISS to work on-site. These managers acted as the liaison between GlobShop's managers and the offshore staff. These measures improved the working arrangements between the two companies.

Satisfied with ISS's performance in providing production support, Roger decided to further experiment by focusing on more value-added projects. GlobShop engaged ISS to architect a data warehouse that would enable faster reporting and provide business leaders with a view of enterprise-level data. This project was very successful and it helped win the confidence of business leaders. Roger said: 'When we offshored production support, it brought visibility and credibility from end users. When people saw the results from data warehousing, we had the buy-in from senior business stakeholders.' He further elaborated: 'When you try a new offshore sourcing strategy, the project needs to be visible and to be meaningful to the stakeholders. However, the project cannot be so important that you are betting your entire business on it. That is very risky. What we achieved through data warehousing resonated throughout the organization and set the stage for me to do a whole lot with offshoring.'

Laying the ground rules

Before completely embracing offshoring, GlobShop had to have some basic tenets in place. Roger explained: 'As we started thinking about offshoring, it became clear to me that we could do a lot with global offshoring that was strategic in nature and not merely cost-oriented, like 24×7 productivity, costs moving from fixed to variable and the notion of variable skills etc. We wanted to capitalize on the strategic side of offshoring… therefore, we adopted an "*and*" philosophy. That is, we had to reduce costs *and* improve productivity, quality, speed and agility.' He further cautioned: 'Outsourcing does not mean transferring the accountability of IT to a third party. Always, the global IT will be responsible and accountable for the IT outcomes.'

Roger developed an additional set of principles for offshoring. The focus was to be on the business outcomes of the projects rather than on the specific activity offshored. Rather than enforce competitive bidding for every project, GlobShop would adopt a partnership approach to work with a single vendor over a long term. Justifying this approach, Roger remarked: 'If costs were the only focus, one can go with a bidding race among vendors. But if offshoring needs to be strategic, then a partnership approach is more appropriate. Partnership means treating vendors as colleagues than as contractors.'

Designing the agreement

GlobShop and ISS had separate 90-day agreements for the initial support and data warehousing activities. GlobShop preferred these agreements to be on a fixed-price basis. Neal explained: 'We opted for a fixed-price model as the requirements were specific and very straight-forward. Payments to our partner were tied to specific milestones and deliverables. We did not want any cost overruns or unanticipated surprises.' In November 2002, GlobShop entered into a 3-year global offshoring agreement through which ISS became responsible for selected new application development and support. The companies entered into a master services agreement (MSA) that enabled creation of separate work orders or statement-of-work (SOW) for each new project or extensions of ongoing projects (see Figure 4). ISS's responsibilities included analysis, documentation, knowledge transfer, guided support and stand-alone support. Neal elaborated: 'The standard business and legal terms that do not change over time were taken care of by the MSA. Under the MSA, we did SOWs for each individual project. The logic was that the typical legal stuff got negotiated once under MSA; however the CIO had the authority to sign off on the SOWs – he could use different staffing models, rate structures and service levels in each SOW.'

One of the hallmarks of the GlobShop–ISS agreement was the implicit gain-sharing incentives for the vendor. Rather than sharing a proportion of the savings on a one-time basis, GlobShop agreed to reinvest the savings from offshoring back into IT, which could translate into continued revenue generation for ISS. Given GlobShop's difficulties in expanding the IT budget or making substantial IT investments, the strategy was to channel the cost savings realized from IT offshoring back into newer value-added IT initiatives. Roger remarked: 'As ISS helps us reduce our costs, we redeploy those dollars into other IT projects. We are going to go back to ISS first to get those projects done. This was a win-win situation for both of us.'

Another noteworthy part of the relationship was the flexibility to plug-and-play IT resources according to the

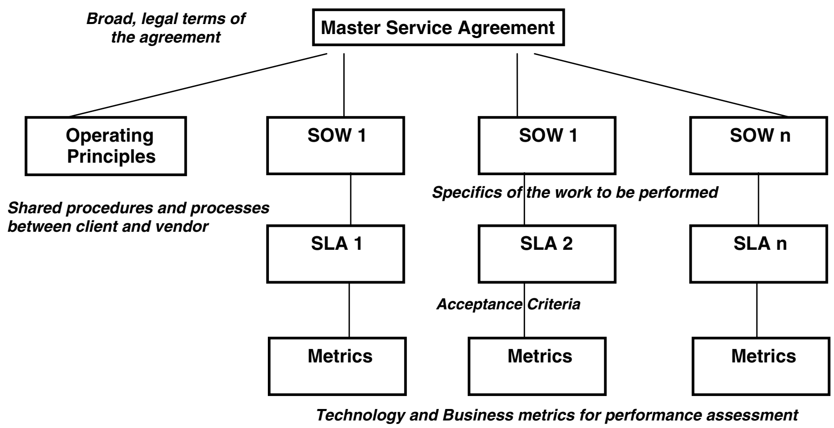

Figure 4 Structure of agreement.

needs of IT initiatives. Under the global offshoring agreement, ISS committed to maintain a talented pool of offshore staff with retail and Globshop-specific knowledge. Depending on the specific project requirements, the company would have just-in-time IT resources. Neal commented: 'We get a well-educated, knowledgeable and scalable IT team using a just-in-time global sourcing philosophy where we get the best talent, as needed, quickly. We don't mind paying more for this kind of flexibility. We are using fewer hours of the best available skills and experience, rather than employing moderately skilled talent full time and using only a portion of the available capacity.'

Under the 3-year deal, several IT tasks were offshored to ISS. Apart from consolidation, maintenance and ongoing support for core merchandising system, projects that were given to ISS included support for the ERP modules and point-of-sales systems, development of intranet site and content management processes.

Executing offshoring – managing the change process

Within GlobShop, the offshoring effort was to be implemented as a part of its overall IT reorganization. The business impacts of the September 11 event forced the company to adopt a more aggressive strategy and accelerate its reorganization efforts. Senior management demanded a faster reorganization and quicker results. The IT leadership had to not only accelerate cost reductions but also cope with increased demands from corporate management to improve the speed and quality of IT offerings. Roger said: 'When we came up with our strategy for global IT re-organization, we anticipated a 36-month period for the complete re-organization. However within weeks after 9/11, business mandated drastic cuts across entire enterprise. Our goal was accelerated to 9 months.'

Handling workforce reductions

Reengineering the old structure and accelerating the consolidation was more difficult than initially anticipated. An aggressive offshore strategy implied reducing a significant portion of the IT workforce. Dave Blanks, an IT manager, recollected the mindset that prevailed: 'None of it was comfortable. GlobShop was a great organization to work for and we had people with over 25 years of experience in the company. The decision to layoff had very serious emotional impacts.' GlobShop had to determine how many people and whom to retrench, whether to carry out the workforce reduction in multiple phases, and how to communicate its intentions to the employees. The timing of the downsizing was critical because GlobShop had to work on transferring critical knowledge from affected workers to other staff and the vendor. Roger elaborated:

> A big issue that we faced was how to handle people changes. We had to worry about perceptions of internal staff, external stakeholders as well as the community. Some managers wanted to do the layoffs in phases, hoping that the business would turn around so that future cuts can be avoided. Others opposed the idea arguing that phased cuts will create lots of uncertainty among remaining employees. We also wrestled with 'telling-them-now' or 'tell them at the last minute'. There was staff who had to be cut but whose knowledge had to be transferred. We tussled with how to convince them to stay for a specific time period.

Quick retrenchment was problematic as GlobShop did not have a good documentation of its IT systems and applications. Knowledge transfer was a serious concern. Neal noted: 'There wasn't much documentation and a lot of knowledge was in people's heads, those who had been around for a long time.'

The initial hesitations not withstanding, the company communicated its intentions to accelerate offshoring and reduce a significant number of employees. Over a period of time, three out of four IT jobs were to move offshore. The senior management took charge of the process to ensure it did not turn out to be a very painful experience. Roger said: 'open communication is very important. We were open and honest with people about what we were doing.' Commending the senior management's role, Neal remarked: 'Our CEO played a very critical role in how well he reached out to the employees and communicated with them in this process.'

GlobShop's management worked out a package for employees affected by downsizing. A severance pay structure was put in place. Another key element was retention pay for the IT staff whose knowledge had to be extracted and transferred. Neal elaborated: 'We had to transfer the knowledge from people's heads to either another employee or to our offshore vendor. We significantly increased their bonuses if they stayed for a time period to productively transfer the knowledge they had.' In addition, GlobShop also offered career transition assistance through a third party by which the employees could identify and apply for appropriate positions in other organizations.

Reflecting on his actions, Roger believed that these measures greatly helped the transition process: 'I personally met with everyone who was going to leave our company. We told people well in advance that layoffs were coming. The employees, though discontent, were happy that we told them the truth. In addition, we gave them some runway and also provided significant support for them to find new jobs. That was key – to be honest and open, and offer additional support.'

Soon after the announcement of layoffs, a number of offshore-implementation issues demanded management attention. These issues concerned many elements of governance process between ISS and GlobShop and the day-to-day working arrangements.

Improving vendor relationship and governance process

When ISS was entrusted with the responsibility of production support for core merchandising systems, ISS sent its personnel to each region. These people spent several weeks on-site, learning and documenting the processes, systems and related issues. GlobShop's IT staff worked closely with ISS's personnel to enable easy knowledge transfer and transition. Rahul Sharma, project manager from ISS, commented: 'Tracing and documenting the entire set of systems was tedious and time consuming, but was necessary for us to take over the production support. GlobShop was very co-operative and offered full support.'

Roger took specific steps to help overcome the cultural and social differences between the offshore staff and the global IT team. Specific training sessions were conducted to impart an understanding of multiple cultures and value systems and ways of addressing cultural differences. Workshops on diverse teams and teamwork were also organized (Figure 5 presents a snapshot of outcome from such a workshop). An analyst commented: 'We had diversity experts who taught us how cultures vary and how to recognize and work with such differences.'

The relationship between GlobShop and ISS expanded significantly. From a transactional mode, Roger wanted to forge a tighter partnership so that ISS could play a more proactive role in providing value-added services as well as in identifying newer IT opportunities. He created teams called the 'communities of practice' (COPs). The COPs consisted of core project participants drawn from the business, IT and the offshore vendor. Roger explained: 'Each COP is made of different entities with specific areas of focused expertise, and all COPs are integrated by the GlobShop IT management team, to contribute interdependently towards accomplishing overall business goals.' There were two fundamental objectives behind the formation of COPs: (1) To ensure that the offshore vendor is completely infused into GlobShop so that the vendor works as a mere extension of GlobShop's IT unit. This implied that the offshore vendor personnel were treated as internal colleagues rather than as external contractors. (2) To bring the technology, user and vendor personnel together.

Commenting upon his role in the COP, Rahul (Project Manager, ISS) said: 'Through the communities of practice, I got a seat at the table where GlobShop made key IT-business decisions. I felt I belonged to GlobShop.' When the COPs were initially set up, considerable concerns were expressed about the changed roles of the vendor. Rahul recollected: 'I was invited to top-level meetings and saw many people wonder what I am doing in that meeting. I sensed a silent uneasiness.' However, as GlobShop's executives started seeing some promising results, the idea of COPs gained quick and widespread acceptance. The COPs also helped change the mindset of the vendor. Rahul remarked: 'We had to re-orient ourselves and see what we could really do to improve the bottom line of their business. If we were on some sales-mode trying to simply sell our solutions or services, they'd have thrown us out.'

Onshore/offshore management structure

In the initial days of their relationship, working arrangements between GlobShop and ISS were largely informal. However, as ISS took over the maintenance of a significant portion of GlobShop's merchandising system, the two companies decided to develop a more formal structure for working together. The structure provided a more coordinated way for the business users, GlobShop's IT staff, ISS's on-site specialists and the offshore team to work together (Figure 6). The two companies also agreed on a common set of principles for onshore/on-site/offshore staffing. Neal explained:

> The ratio of onsite/offshore/onshore staff varies on each project as we progress through the different phases of the project lifecycle. The appropriate team ratio for a project is arrived by jointly taking into account the cost, services, project needs and effort. For any new work, we typically start with a larger on-site staff that slowly transitions offshore as the requirements of the project become more stable.

For most maintenance projects, ISS followed a typical sequence: analysis and documentation, knowledge transfer and service phase. While more on-site staff was required in the analysis phase, this staff was transitioned offshore as the knowledge transfer and learning improved. The offshore team became more independent in the service phase. For some of the early application support and maintenance projects, 30% of ISS's staff was dispersed on-site with 70% offshore. Gradually, most of the application support projects achieved on-site to offshore ratios of 10% to 90%. For application development projects, the on-site-offshore ratio varied from 60–40 to 30–70.

Initial results from offshoring

Within 18 months of the global sourcing arrangement, GlobShop reduced its IT expenses by 35%. As planned, the

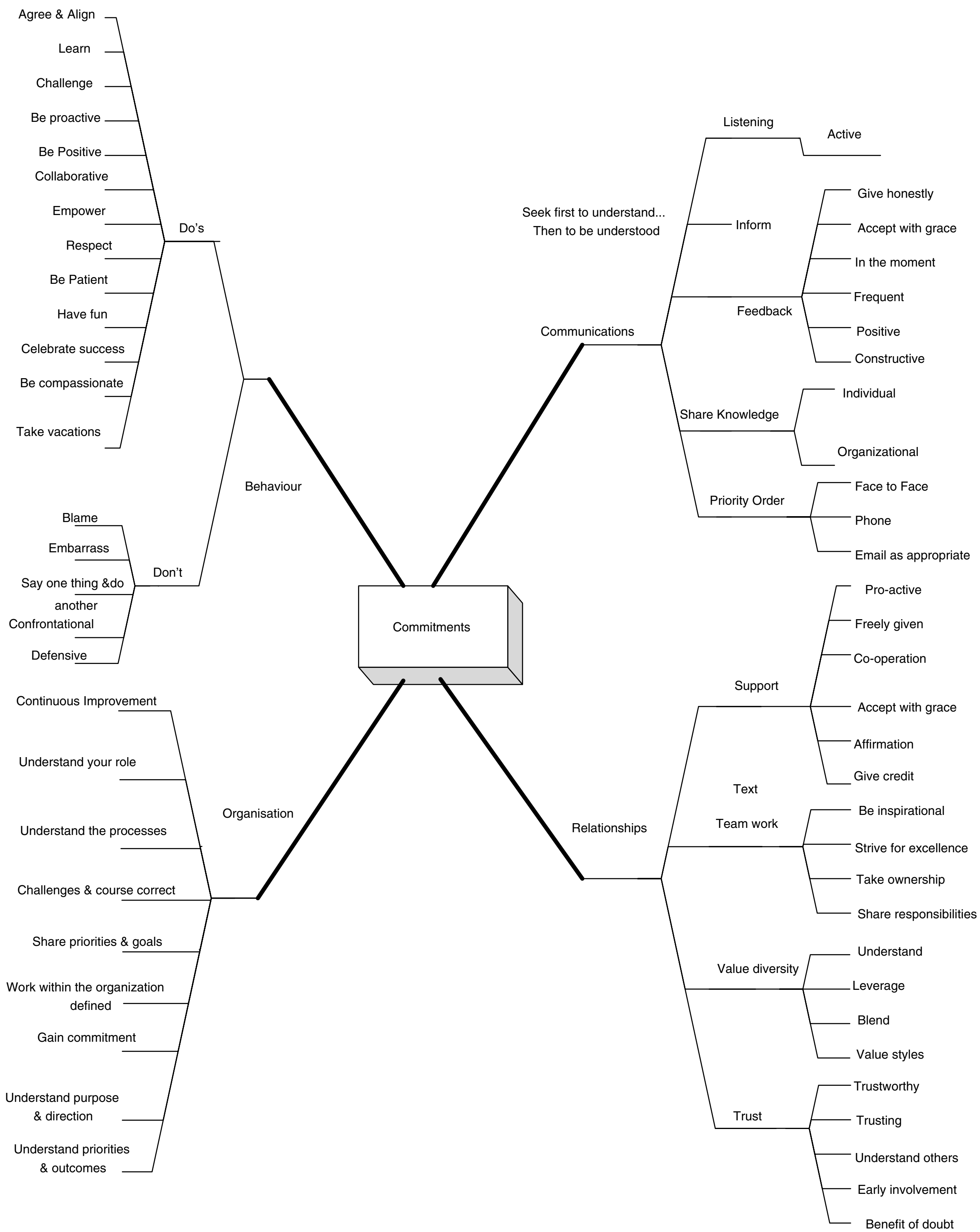

Figure 5 Enhancing global teamwork: snapshot of output from workshop.
Source: Internal company records.

IT organization at GlobShop was reorganized and consolidated in two locations – one in USA and one in Asia, with an extended offshore team located in India. The global IT staff shrank 43% in the first year, and 59% in the second year of MSA. The legacy applications that resided in over 24 AS400 machines in 10 regions were consolidated into one machine and the support work was moved offshore. GlobShop conducted a user satisfaction study that showed an improvement from 2 to 3.5 on a 5-point scale since they started offshoring.

Expanding the relationship

Enthused by these results, GlobShop decided to award additional projects to ISS under the broader MSA (Figure 7 presents the key IT responsibilities at GlobShop). ISS studied a number of IT opportunities and suggested new initiatives for GlobShop. Subsequently, ISS was asked to work on several projects – development of GlobShop's internal and external web sites, improving the technical architecture, site performance, navigation and content management processes and also performing infrastructure tasks. As a value-added service, ISS created a web-based knowledge management system about GlobShop's systems that was required for ongoing maintenance and support, and a web-based task management system to capture detailed project activity. The information captured from these two systems enabled GlobShop to better assess the offshore projects. The number of ISS staff who worked on GlobShop's projects also trebled.

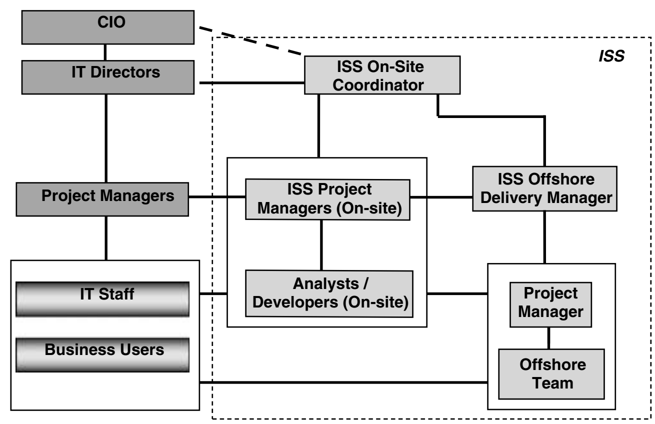

Figure 6 On-site/offshore management structure.

Taking stock and moving forward

As GlobShop neared the end of its 3-year sourcing agreement with ISS, Roger confronted several serious questions. Should GlobShop continue to move more value-added IT work offshore? Should it renew its agreement with ISS? The company had managed to weather economic storms and gained incremental revenue growth. The company had plans to streamline its global supply chain and implement some advanced EDI solutions. It also needed to work on migrating from legacy environment to more advanced platforms.

Pleased with the offshoring results thus far, the senior leadership at GlobShop was willing to move newer IT projects offshore. Dan Cwik, Vice President of Retail Operations, remarked: 'I am very impressed by our offshoring experience and I think it is a very good solution to have our IT work done in India. Offshore outsourcing helps us focus on exactly what our business is – global travel-retail. I don't believe doing this work internally is going to make us more competitive.' Sally Curry, Vice President of Finance, expressed similar sentiments: 'In the volatile environment in which we operate, our main task is to focus on improving our retail business. That means

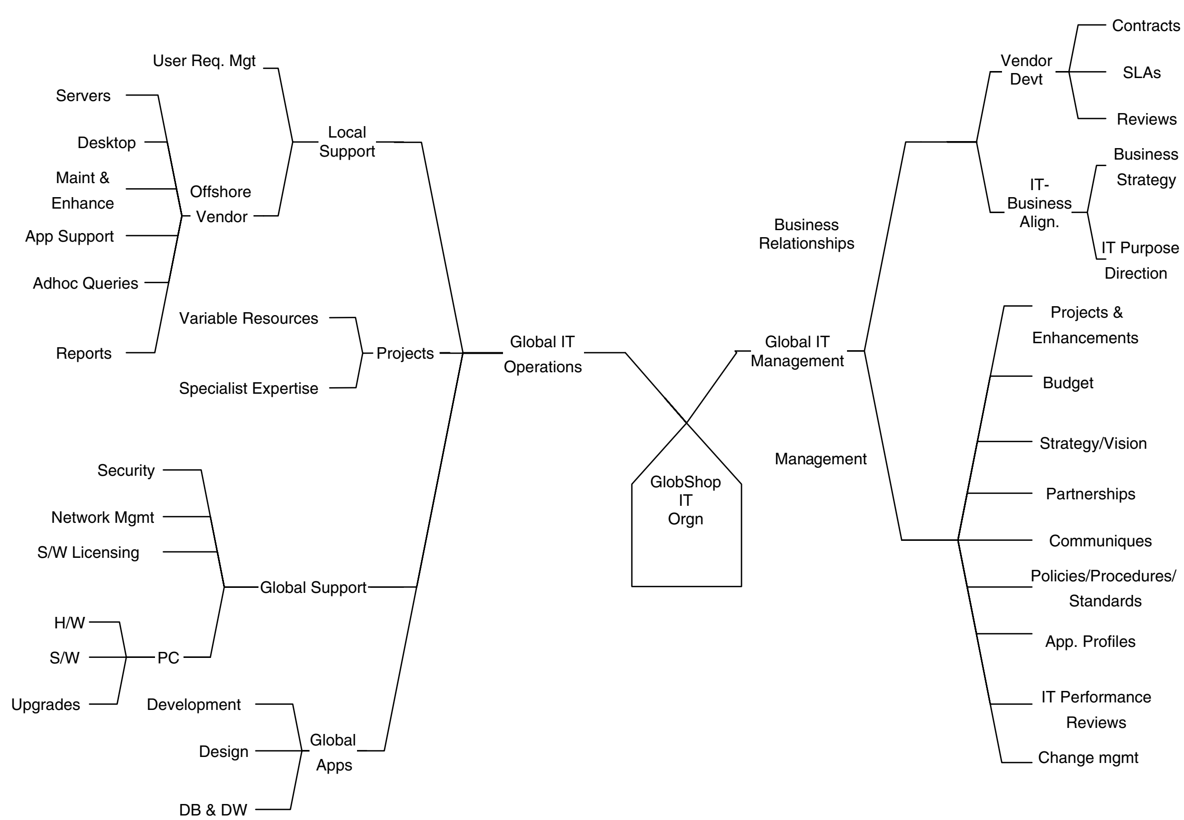

Figure 7 Key IT activities at GlobShop.

expanding geographically and into other travel-channels to buffer against economic events, improving efficiency in operations and streamlining supply chain. Information technology, while obviously an important part of our operations, can be handled well by our offshore partner. Each dollar that is saved from offshoring can be reinvested in our business.'

However, a section of executives believed that despite the success of offshore projects, entrusting the responsibility of critical projects like supply chain initiatives to an offshore vendor is 'too risky.' Roger noted: 'We have a few projects in our pipeline that are quite critical in nature, for example, advanced EDI linkages with vendors. Some business colleagues have expressed apprehensions about giving these projects entirely to our offshore partner. We are still debating what should be retained internally and what should be offshored.' Some of the IT managers wondered whether increased offshoring would simply erode their relevance in the company. Neal argued: 'This can be very risky. You're talking about more offshoring and that may place our mission critical tasks with the external vendor. This could also mean further layoffs and reduction of our IT group. So, what is our future?'

Over the past few years, ISS has grown to become one of the leading offshore vendors in India. Its clientele has expanded to include top retailers and several Fortune 1000 firms. In 2004, Rahul Sharma and two of ISS's on-site project managers were promoted and transferred to other ISS clients. Some of GlobShop's IT staff felt that ISS was diverting its 'star employees' and resources to more prestigious clients. Neal said: 'We had some new managers [from ISS] but I felt it wasn't like our old team. These new guys also had a steep learning curve. They were no match to the group we had earlier…. There was also an instance where we had to request them [ISS] to replace one of the [ISS] managers.' Dave Blanks added: 'These [Rahul and his team] people were very valuable. They knew our business, systems, formed good relationships with our managers and users. It cannot be replaced very easily.' Roger wondered if GlobShop would continue to receive the 'special treatment' it got from ISS.

Another issue that worried Roger was the extent of GlobShop's reliance on ISS. The company has become critically dependent on ISS for many of its IT operations. Some of the GlobShop managers felt it risky to work with a single offshore vendor and preferred to spread the work to multiple vendors. Larry Katz, Manager at the Global Data Center, argued:

> When we started working with ISS, we wanted to be able to pull out [of the relationship] anytime. We didn't want a situation where we became too dependant on them [ISS]. But now, I fear our dependence has reached a critical level. They [ISS] have grown big and can do without our account. For us, it may not be possible to live without them. I think it will be better to work with a few vendors so that we can spread the risks.

Neal was also concerned: 'We don't want all our eggs in one basket. The offshore market has grown. We can definitely shop around for other vendors. There are others who are competent as well as cheaper.'

The Vice President of Finance, Sally Curry, had an alternate viewpoint:

> I don't think working with multiple vendors will be cost-effective. It is going to drive our overheads up. We are happy with what we got from ISS – Why not just continue with them? It is going to be very expensive to find new partners, help them learn, transfer all the knowledge. We cannot afford that.

A larger issue that was looming in Roger's mind was the future of IT organization and its relevance in GlobShop. If GlobShop continued offshoring more value-added and core activities, what purpose would the internal IT unit serve in future? It might simply be a matter of time before the entire IT function was farmed out.

Note

1 The authors have prepared this case solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of the managerial situation. The authors have disguised the names and other identifying information to protect confidentiality.

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