Chapter VII

Outsourcing Decisions: Using Porter’s Model

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ABSTRACT

It is no longer questioned that the management of information systems (MIS) is an important variable when studying organizational effectiveness and competitiveness. There have been numerous studies on how information systems (IS) can be used by organizations for strategic purposes, yet actual experiences of an organization’s use of IS have often been less than satisfactory. Problems with cost, quality, and IS performance, as well as unfavorable end-user—IS relations are frequently reported. Partially because of these problems, the outsourcing of IS functions has become increasingly common. Outsourcing IS functions provides advantages to an organization but it may also create a new set of problems if the impact of the outsourcing decision to the organization as a whole is not fully considered. This chapter reviews the strategic use of IS in organizations, discusses the growing popularity of outsourcing IS functions, and uses Porter’s model of five competitive forces to provide a different viewpoint on the decision to outsource.

INTRODUCTION

In the last dozen years, the use of information systems (IS) in organizations has expanded exponentially. IS has gone from a supportive role in organizations to becoming an integral part of corporate strategy. In the mid 1980s, academic journals published numerous articles about the growing relevance of IS as a strategic weapon. Several of these articles built on Porter’s (1980) descriptions of five competitive forces and three generic strategies used by organizations. By the late 1980s, researchers were acknowledging that IS could be used for strategic and competitive reasons and were turning their focus to how to select and implement an IS strategy that would align with the corporate strategy.

In the 1990s, questions about the sustainability of IS competitiveness dominated IS strategy literature. Outsourcing became one strategy organizations used to deal with difficulties in sustaining competitive advantage over rivals. Outsourcing...
can be defined as a "make-versus-buy" decision facing an organization. Some or all aspects of the IS area can be outsourced including, but not limited to, hardware, software application development, and management functions (Loh and Venkatraman, 1992). Simply stated, outsourcing has become increasingly popular in both small and large firms as competition and other external pressures increase.

Porter (1980) stated that all organizations had strategic plans, whether explicit or implicit. He emphasized the importance of explicit strategic planning for all organizations. He created a framework to "help a firm analyze its industry as a whole and predict the industry's future evolution, to understand its competitors and its own position, and to translate this analysis into a competitive strategy for a particular business" (Porter, 1980, p. xiv). The basis of the framework is the analysis of five competitive forces (rivals, new entrants, suppliers, buyers, and substitute products) and their impact and strategic implications on the organization and the industry as a whole. Porter defined three generic strategies implemented by organizations: low-cost, differentiation, and niche, and discussed how the five forces affect the chosen strategy. Porter acknowledged that all five forces may not be crucial to a particular organization and that managers should use the framework to determine which factors are crucial and how they can be analyzed.

The goal of this chapter is to illustrate how Porter's five forces model can be used to determine when an organization is most likely to successfully outsource IS functions and whether certain forces are more important than others in the decision. Outsourcing's reported advantages of cost cutting and higher system quality have been questioned by researchers and practitioners as more data becomes available to study the long-term effects of IS outsourcing. This chapter suggests the use of Porter's framework when formulating strategic IS plans to determine whether an organization should outsource IS functions or keep them in-house for optimal success and satisfaction.

The chapter is divided into four further sections. The second section reviews IS literature and the history of the strategic use of IS within an organization. The next section defines outsourcing, reviews management information systems (MIS) literature on outsourcing, and describes advantages and disadvantages commonly associated with outsourcing. Next, Porter's framework is reviewed in more detail, outsourcing questions are fit into Porter's framework, and suggestions/proposals are given for organizations making an outsourcing decision. The final section applies theory to practice and reinforces the usefulness of the strategic alignment model of business and information technology.

IS AS A STRATEGIC WEAPON

In the early 1980s, academic articles began promoting IS as a competitive weapon that could enhance an organization's corporate strategy. Several frameworks were developed to assist managers in developing their organization's IS into a strategic advantage. Earl (1987) summarized and compared the early frameworks, categorizing them into awareness, opportunity, and positioning frameworks. Awareness frameworks helped executives determine where strategic opportunities for IS applications existed and answered such questions as 'How do I
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