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On the Edge

Everything elastic

By Kishore S. Swaminathan

Chief Scientist
Accenture

What if your business processes and capabilities—your IT, workforce, R&D—were in essence elastic, able to stretch, change and expand at will and weather just about any global economic storm? Now imagine the impact this could have on your company's performance.

• Consulting • Technology • Outsourcing

Traditionally, organizations have been isolated islands, with fixed sets of business capabilities determined by what they can do on their own, within their own organizational boundaries. Expansion typically meant significant capital outlays for building new factories, entering new businesses or geographies, upgrading and expanding IT.

Such organizations are inherently reactive. Less demand? Factories reduce shifts, workers are furloughed and expensive capital equipment goes underutilized. A spurt in demand is often met by a shortage of products, disruption of services, unhappy customers, frantic hiring and impulsive capacity building. In fact, one could argue that any successful business today is by definition less than efficient, because its success is predicated on overcapacity to meet peak demand, which also means underutilization of resources—particularly capital—most of the rest of the time.

The invisible hand

Slowly but surely, the invisible hand of information technology has been blurring the boundaries between organizations to the point that business capabilities have now started to spill across organizational boundaries. To be sure, the phenomenon itself is not new. In the past, companies have shared business capabilities through various special arrangements such as alliances, trading agreements and industry consortia.

What's new is that IT is now making it possible for business capabilities to cross organizational boundaries at an *industrial scale*. This has enormous consequences for companies and indeed for the very fundamentals that govern the economics of business.

When organizations can effectively and efficiently share business capabilities, a series of things begin to happen. First, companies need

to plan only for average demand and can offload excess demand to a third-party provider on an as-needed basis, with the hope and promise that the provider can gracefully and seamlessly augment the company's capabilities. Second, much of the unpredictable or variable demand moves from a fixed or capital cost to a variable or operational cost on the balance sheet.

Third, this industrial-strength sharing of capabilities enables companies to enter new businesses and markets with relatively little risk. If the new product or market turns out to be a dog, a company can wind down operations with little or no sunk costs. Alternatively, if the adventure is wildly successful, the company can rapidly scale up to meet demand.

Put another way, when business capabilities can be sourced effectively and efficiently, companies can pass on significant business risks to a provider.

So what's in this for the third-party providers? First, as more clients seek their services, they begin to specialize, and as the process becomes cost effective, they gain price advantage. This, in turn, enables them to provide the same service to multiple clients at lower cost and thereby achieve scale. Once they have scale—particularly across multiple clients from different industries and different business cycles—providers are in a position to load-balance across all of their clients, taking advantage of the clients' staggered business needs.

When the providers achieve enough scale, they can plan for average (as opposed to peak) demand and achieve high utilization rates by constantly repurposing capacity from one client to another. This enables them to hedge against the risks that are passed on to them by their clients.

When scale happens, elasticity follows.

Enter the Internet

IT and business process outsourcing are early examples of elasticity—sourcing people and certain simple business processes from outside the organization, with the provider taking some of the demand and utilization risks. The phenomenon began to gain momentum in 2001. Many observers attribute this to cost reduction necessitated by that year's recession. Others point to cost arbitrage between developed and emerging economies. Still others attribute the rise of outsourcing to the need for companies to focus on their "core competence."

But cost arbitrage, the need to focus on core competence and the pressure to reduce costs have all existed for years. So what changed? The surprisingly simple answer is "the Internet."

By around 2000, the Internet had evolved to the point that it could support inter-enterprise communication—email, instant messaging, Voice over IP—and provide access to applications and data across organizational and geographic boundaries. Although outsourcing was practiced well before the Internet, the dramatic increase in various forms of outsourcing was made possible by the cheap, *industrial-scale* communication that was enabled by the Internet.

Today, the operating goal of every outsourcing provider is to go from a "your-mess-for-less" model (operating a business process for a client per the client's specifications) to a "many-to-one" model (offering a menu of standardized business processes per the provider's specifications). Why? Because only with scale can providers offer standardized processes to multiple clients so that the same process, people and other resources can be repur-

posed across clients to cater to their changing business needs.

The latest technology trends—Internet computing; mobile computing; the convergence of communication, collaboration, communities and content—seem poised to create even more business elasticity.

Today, Internet computing—a.k.a. cloud computing—makes it possible to buy processing power, storage, software, even simple business processes on the fly, pay for what you use and scale up or down as needed. Internet computing provides elasticity to IT itself. Companies no longer need to commit to expensive (and often underutilized) capital equipment or software in their data centers, but can simply rent them when needed. A few Fortune 500 companies have started using cloud computing for core business functions, including drug development, CRM, ERP and procurement.

Perhaps more important, Internet computing also brings elasticity to business processes, enabling them to change or scale horizontally and vertically depending on business conditions.

How? Software as a service, software markets and integration standards provide companies with many more sourcing options and standard means of integrating hardware, software and process components. Business processes, therefore, need no longer be cookie-cutter affairs provided by large monolithic software packages but instead can be assembled and reassembled from a large set of third-party software suites.

And since the hardware and software are sourced from outside the enterprise firewall, it becomes much easier to integrate processes with those of providers (to expand business capacity horizontally) or those of industry partners (to expand

business capabilities vertically). Moreover, the integration takes on an industrial scale: no more proprietary arrangements, lawyers or small-print documents.

If something as simple as email and VoIP could give rise to workforce elasticity in the form of business process outsourcing, recent developments in collaboration and mobile technologies may well call into question many of the assumptions underpinning today's global mega enterprises.

Companies and individuals today have access to an astonishing range of options for communication and collaboration, from IM, VoIP, blogs and wikis to 3G and 4G wireless networks to location-awareness and near-field technology. Add to this the so-called Millennials or Generation Y (including my lovely teenager), for whom mobile phones, IM, podcasting, Facebook and Twitter are like air and gravity. As these young people begin to enter the workforce in large numbers over the next five years, companies will not only have to revisit their different technological options; they will also need to rethink their workforce and workplace practices. (For more, see "Does your company have an IT generation gap?" *Outlook*, January 2009.)

For example, how can a company reduce the wear and tear on employees caused by travel and time zone differences and the time wasted in daily commutes? Better utilize or even eliminate office space? Or avoid the enormous stress on management and workers caused by large-scale hiring and layoffs in times of business volatility?

How does a company effectively deploy an expert across multiple projects and augment R&D with experts from the outside? Or use crowd-sourcing techniques internally as well as with customers to increase innovation?

Indeed, how does a company manage an elastic workforce that may consist of a core set of employees and a large number of free agents working for themselves or for other organizations?

Technology is already available that enables companies to source people on demand to solve a problem or aid a computer in solving a problem that requires human intelligence. To be sure, there's nothing new about engaging contractors for work. But what is new is that collaboration and mobile communication technologies are taking it to a new level: global sourcing of human expertise at scale and on the fly.

New frontier

Innovation elasticity is a particularly interesting new frontier. For example, today there are "open-innovation marketplaces" such as InnoCentive, where companies can pose complex scientific or business problems to a community of more than 100,000 researchers from various fields and pay only if a suitable solution is proposed. Procter & Gamble reports positive results through InnoCentive and is now actively experimenting with an R&D model called Connect + Develop. P&G's goal is to derive 50 percent of its innovation from outside the company in the future.

At the other end of the spectrum, companies such as Starbucks and Dell have developed web-based models for large-scale inclusion of their customers as an integral part of their innovation processes. As of March of this year, customers have contributed more than 60,000 ideas to mystarbucksidea.com (for example, "a free drink on your birthday") and 11,000 ideas to Dell's Ideastream ("Add the decibel level of your computer to the specifications," suggested one customer).

The relentless march of information technology is slowly carving out a new reality. Elastic processes. Elastic workforce. Elastic IT. Elastic innovation. And complimentary latte on your birthday. Is your company ready?

Kishore S. Swaminathan is based in Chicago.

k.s.swaminathan@accenture.com

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