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Sustainability practices in global IT outsourcing

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Sustainability Practices in Global IT Outsourcing

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Abstract

Buyers and providers of global IT outsourcing increasingly strive for sustainability. Lessons from global leaders can give strategic and responsive direction to the IT outsourcing industry and to buyers of outsourcing services.

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Sustainability Practices in Global IT Outsourcing

Buyers and providers of global IT outsourcing increasingly strive for sustainability. Lessons from global leaders can give strategic and responsive direction to the IT outsourcing industry and to buyers of outsourcing services.

By Ron Babin and Brian Nicholson

Until recently sustainability was the domain of social and environmental activists. Today, it is a priority item on the agenda of almost every business organization. In parallel, global IT outsourcing continues to grow unabated, and – not surprisingly – leading providers have embraced sustainability. Buyers and providers of global IT outsourcing expect short term and strategic value from sustainability. Buyers increasingly expect providers to deliver sustainability capability as both parties are reacting to government regulations and employee expectations to reduce energy costs while creating a smaller carbon footprint.

More strategically, providers are embracing sustainability as part of the integrated relationship with buyers and strengthening their brand. In many cases, leading providers are finding that sustainability related services provide a new source of revenue.

Sustainability encompasses both social and environmental issues, often referred to as ‘people and planet’ responsibilities. The first dimension concerns the social responsibility of buyers and providers. Government and non-government organization (NGO) guidelines, standards, reporting frameworks and regulations create a set of public expectations. For example, Socially Responsible Outsourcing (SRO) is an outsourcing model that creates social benefits by employing workers from a disadvantaged population in a profitable outsourcing business. The environmental issues are related to eWaste, increasing power consumption and related green house gas emissions.

The Rise of Sustainability in IT Outsourcing Sustainability has become an unavoidable issue in global IT outsourcing and for the leaders represents a strategic opportunity.

In our interviews and surveys of leading buyers and providers (see “About this research”), buyers revealed distinct criteria for evaluating providers sustainability capability. A recent industry survey from the International Association of Outsourcing Professionals (IAOP) on social responsibility in outsourcing found that “[Sustainability] is an important and growing issue for outsourcing customers and providers – 71 percent say that [sustainability] will become more important or much more important in future outsourcing contracts.” Outsourcing buyers and providers rated the importance of sustainability in their business strategy, the response was 3.9 on a 5 point scale (1 is somewhat important, 5 is crucial).

Respondents to the IAOP survey rated people issues as more important than planet issues. The top three sustainability issues that outsourcing buyers look for are labor practices, fair operating
practices and human rights. Environmental issues were rated fifth most important, after consumer issues.

Our research examined the reasons that outsourcing providers, especially leading global firms such as Accenture, IBM, HP, Infosys, Tata Consulting Services and Wipro and many others, have begun to invest heavily in sustainability.

The findings point to multiple roles and rationale for sustainability divided into categories of Responsive and Strategic\(^2\). The Responsive category has two elements; i) acting as a good corporate citizen, attuned to the evolving social expectations and needs of stakeholders, and ii) mitigating existing or adverse effects from business activities. The Strategic perspective involves initiatives where social and business benefits are distinctive and provide long term competitive advantage.

Many of the sustainability initiatives in global IT outsourcing are responsive but some are strategic. The leading firms demonstrate how strategic advantage through sustainability in outsourcing relationships can be gained leading to significant benefits.

About this research
Our research began in 2008, with participation from researchers at the University of Manchester Business School and Ryerson University in Toronto. We interviewed executives and senior managers at 18 significant outsourcing buyers, providers and advisors. The organizations in the sample were all large global providers and buyers of outsourcing services. The interview findings were summarized and discussed in a focus group session conducted at the main author’s University. Three case studies have been developed, with detailed interviews at both the client and provider sites, including offshore locations in India. A total of 31 executives participated in the structured interviews and case studies. In addition we met with industry representatives from NASSCOM in India, IAOP in the United States, the National Outsourcing Association (NOA) in the UK and the Centre for Outsourcing Research and Education (CORE) in Canada. Finally, data have been collected and analyzed through surveys sponsored by IAOP and CORE, with approximately 220 responses. About 60% of responses came from North America, 13% from Europe and the rest from all other regions.

We examined public information available on websites for the top 19 global outsourcers to gain a better understanding of their sustainability profiles. We examined company annual reports and sustainability reports where available. For each company we looked for participation in global sustainability standards, which included the Global Reporting Initiative (GRI), the Carbon Disclosure Project (CDP), the UN Global Compact, ISO 14001 and 26000. For those companies that are listed on public stock exchanges we examined if the stock was included in a socially responsible investment (SRI) index such as the Dow Jones Sustainability Index. From this content analysis we prepared a hierarchy of sustainable outsourcers, which allowed us to identify attributes of the leaders and propose lessons to the rest.

In the sections below we describe six examples of Responsive and three examples of Strategic sustainability practices. In the Responsive category, outsourcing providers react to expectations of three stakeholder groups: customers, governments and employees. Employees have specific social and personal needs such as education and health that sustainability can address. Buyers and providers seek to protect their corporate brand through Responsive sustainability. Finally,
cost reduction through Green outsourcing (Green-sourcing) is a Responsive action. On the Strategic side, building relationship trust and new value-added services are two distinct practices adopted by the leading providers.

**Responsive Sustainability in Global IT Outsourcing**

Many sustainability actions in outsourcing appear to be reactionary and tactical, such as responding to a client sustainability requirement in a request for proposal (RFP) or complying with a government regulation. These actions are classified as Responsive where outsourcing providers act as good corporate citizens, attuned to the evolving social concerns of their stakeholders.

We can identify three sets of outsourcing stakeholders: buyers, employees and regulators. Below we explore the sustainability expectations of each stakeholder group.

1. **Buyer sustainability expectations** We initially expected that buyer requirements would drive outsourcing provider sustainability capabilities. This was confirmed with evidence from buyers such as an RFP requirement for a global mining company for “suppliers [with] appropriate health and environmental objectives and the management systems in place to deliver on those requirements” and a stated need for the importance of cultural fit and shared sustainability values when evaluating an outsourcing provider. Buyers expect outsourcing providers to bring a sustainability capability that will not diminish the buyer’s reputation. As one buyer explained “Our own environmental responsibility builds our brand and trust. This reputation brings and retains our customers.” “When we look at the outsourcer’s [sustainability profile] we must balance cost [benefits] with the impact to our brand”. In other words, the buyer seeks lower operating costs through outsourcing, but not if outsourcing reduces their reputation for sustainability.

The IAOP survey found that 30 percent of buyers always or often consider the sustainability capability of the provider when making an outsourcing decision. An additional 34 percent of buyers sometimes consider sustainability in an outsourcing decision. 71 percent of the respondents expect sustainability to be more important or much more important in future outsourcing contracts. The IAOP clearly sees this as an important issue for the outsourcing industry, largely driven by buyer expectations.

2. **Government environmental sustainability expectations** Domestic policy makers and world leaders are concerned about the emission of Green House Gasses (GHGs) that contribute to global warming. It’s only a matter of time before environmentally unaware companies will face steep fines. The production of electricity often requires the burning of fossil fuels, such as natural gas or coal, which produces GHGs. In the last decade the general public has become aware and very concerned about global warming. Governments in many countries are now adopting laws and regulations to curb or diminish the consumption of electrical power and the burning of fossil fuels. For example, the UK government implemented the Carbon Reduction Commitment requiring an estimated 5,000 UK organizations to reduce electrical power consumption through a set of incentives and penalties. In October 2008 the European Union published a code of Conduct for Data Centres Efficiency, which establishes best practices to “ensure the carbon emissions and other impacts ... associated with increases in energy consumption are mitigated”


In response to these regulations, the National Outsourcing Association established a Green Committee and published an initial white paper with the intent “to advise relevant officials and regulatory bodies on how best to approach the issue of carbon reduction and the green agenda, with specific focus on the outsourcing space.” Similarly, in the US the International Association of Outsourcing Professionals has begun discussions with leading providers on how to embed sustainability requirements in certification of outsourcing practitioners.

While governments implement regulations to curb GHG production, a set of global sustainability standards has grown to become an accepted business requirement for leading providers of IT outsourcing. We examined the public sustainability profile of the top 19 global outsourcing firms and found that the leading six firms had all adopted and conformed to a ‘defacto’ set of sustainability standards. The set of standards include the Global Reporting Initiative (GRI), the Carbon Disclosure Project (CDP), ISO 14000 and the UN Global Compact.

3. **Employee sustainability expectations** In North America, where the baby-boom retirement will create hundreds of thousands of job vacancies in the next ten years, the outsource providers will compete in a shrinking pool of qualified resources. A recent Sustainability Initiative survey demonstrates that sustainability has an impact on employee recruitment and retention. The survey found “of private companies 57% say they expect employee interest in sustainability to impact their organizations” and “37% [had] already highlighted sustainability initiatives in recruiting.” Sustainability policies and action supports the attraction and retention of young employees, the talent for the future.

4. **Employee sustainability needs** In the developing nations however, sustainability initiatives must address societal needs for education and health. Here, the sustainability emphasis is on people (society) more than planet (environment).

For example, India has a young and growing population, in contrast to the aging populations in Europe and North America. The vice-chair of NASSCOM in Bangalore commented that “we are intending to develop programs that leverage ICT to accelerate vocational skilling”. For example, one program will “target young teenage women from poor backgrounds … we will focus on teaching them computer arts and animation skills.” In discussing sustainability in India, the focus is on “addressing the people [issues] first.” Developing the skills of the general population increases the pool of potential employees.

In discussing sustainability in outsourcing at a global mining firm, the director of sustainable development described the importance of employee and family health. In areas where malaria is prevalent, worker absenteeism can be problematic, when workers care for their sick family member or are themselves ill. Efforts to prevent malaria are a reasonable sustainability investment to improve worker attendance.

The following two responsive sustainability issues are related to mitigating existing or anticipated adverse effects from business activities.

5. **Defend the corporate brand value**

How important is brand to buyers and providers of global IT outsourcing? The Interbrand Best Global Brands 2009 ranking places IBM as the second most valuable brand, with a brand value of $60 billion. Approximately 40% of IBM business is in outsourcing. HP, with an outsourcing
business at 30% of total revenue, is ranked 11\textsuperscript{th} with a brand value of over $24 billion. Accenture, with 42% of its business in outsourcing, ranks 45\textsuperscript{th} with a brand value of over $7 billion. These North American providers invest heavily in branding. An example illustrate the importance:

In late 2009 Accenture faced a brand challenge after Tiger Woods’ personal relationships became public knowledge. Working with Mr. Woods since 2001, Accenture had built a strong global brand after separating from accounting firm Arthur Andersen. After Mr. Woods’ announcements Accenture shares declined in market value by approximately $1 billion before recovering early in 2010.\footnote{7}

This example illustrates the importance and the value of a strong brand to global buyers and providers. Sustainability initiatives can be seen as brand insurance buyers. As another example, a North American energy company described how sustainability and its impact on corporate brand would soon be included as a significant metric in their corporate and personal balanced scorecard. Not surprisingly, an outsourcer to the energy company is committed to “co-embrace environmental issues”. The providers will develop sustainability initiatives with the client that “can be measured in a meaningful way” so that they can be included in a balanced score card.

6. Cost reduction through Green outsourcing Environmental responsibility in outsourcing, driven by increasing power costs, the threat of negative publicity and regulation on reduced carbon emissions suggests that Green Outsourcing will be a growing requirement. Most outsourcer providers are major consumers of electrical power. The increasing power consumption by IT, doubling from 2000 to 2005 according to U.S. Environmental Protection Agency, gives rise to two sustainability concerns related to global outsourcing. First, the rising cost of electrical power has an economic impact on outsourced operations. Second, global outsourcing providers, who rely on IT, consume increasing amounts of electrical power as their operations grow.

Several commentators predict a long-term trend of rising energy demand and costs.\footnote{8} Dramatic increases mean the cost of energy is now a major concern for most organizations. The 2009 Green Outsourcing Survey reported that 85% of the senior executives surveyed said that “the adoption of green technology is more likely the result of escalating energy costs than ecological altruism.”

Alongside rising energy costs, there is an unrelenting appetite for energy in data centers. Aggregate electricity for servers doubled over the period 2000 to 2005 both in the U.S. and worldwide and that almost all of this growth was the result of the increasing number of servers, with only a small part being attributable to increased power use per unit.\footnote{9} Forecasts that total electricity used by servers would continue to grow an additional 76% higher over the next five years. Other researchers have concluded that all computer-related equipment and internet usage is responsible for close to 6 percent of the U.S. electrical consumption.\footnote{10}

Sustainability initiatives in globally outsourced operations have the potential to reduce power consumption costs through more energy efficient data centers, better cooling technology and through technology virtualization and consolidation. One global outsourcer, Cognizant, quotes
a 35% reduction in servers procured in 2008, through technology virtualization, while continuing to grow by 32%.

Outsourcing provides a path for buyers to reduce escalating technology costs and the associated GHG emissions from increased power consumption. Saving money through Green outsourcing is a strong reactive sustainability opportunity for many organizations.

**Strategic Sustainability in Outsourcing**

Strategic sustainability “is about choosing a unique position—doing things differently from competitors in a way that lowers costs or better serves a particular set of customer needs.”1 According to Porter and Kramer, sustainability “unlocks shared value by investing in social aspects of context that strengthen company competitiveness.”

In our research we identified two strategic practices by which sustainability strengthens competitiveness. First, sustainability enhances the outsourcing relationship by building trust. Second, new and growing service lines and revenue opportunities are available to providers who deliver sustainability leadership and services to buyers.

1. **Enhance outsourcing relationship trust through shared sustainability activities** Sustainability provides a strategic reinforcement of trust. Alignment in social and environmental commitments between outsourcing buyer and provider creates foundation of mutual trust that enhances the relationship between the two partners.11 This trust extends well beyond the contractual commitments and RFP evaluations. Referring to a recent outsourcing RFP, one buyer told us “cultural fit, i.e. the values that we share, is becoming very important, especially when price difference [between providers] is marginal.” The need for trust and strong relationships is magnified in global outsourcing where differences in time zones, legal system, language and culture can make the establishment of a trusting professional relationship very difficult. Development of sustainability does not preclude the parties from building trust in other ways, such as reliable delivery of services, shared risk and reward, clear communication channels, etc., but it does provide a convenient and tangible mechanism for bringing the two parties closer together, through shared values and shared sustainability activities

Among our cases, global outsourcing provider (A) spoke of sustainability as a strategic competitive advantage. Working with a North American energy company, the provider described a carbon reduction goal and a joint client sustainability project. Provider A described how measurable sustainability will become a mark of “maturity in the client relationship”.

Another provider (B) described how the India office had coordinated with a European customer office in a shared “charity day” event. The provider spoke of sustainability as a “clearly articulated strategy” with a “clear plan with targets and goals”. The provider described sustainability activities as an “extension or bridge between the client and the outsourcer”. Recognizing that the geographic distance between provider and buyer is a “faceless” relationship, sustainability allows for a demonstration of shared values, allowing “teams to work seamlessly in a global company”, which “strengthens trust… working cross culture and cross geography”. Based on the success of the shared charity day, the provider stated that they are
now evaluating their client sustainability profiles to understand how the provider’s sustainability focus can be used to build stronger relationships with current and future clients.

A North American outsourcing buyer (C) described their relationship with an outsource provider in south-east Asia. When the 2004 tsunami hit that region, the client office staff responded with a fund raising initiative to help their colleagues in the provider firm. The “faceless” relationship had become all too tangible and the effort to help strengthened the relationship and trust between the individuals in the two organizations.

<table>
<thead>
<tr>
<th>Strategic Sustainability in Outsourcing - Examples</th>
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<tbody>
<tr>
<td>A. Global outsource provider</td>
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<td></td>
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<tr>
<td>B. Global outsource provider</td>
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<tr>
<td>C. North American outsourcing buyer</td>
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</table>

2. Value added services Many outsource providers are building a growing line of business in providing sustainability consulting services to outsource buyers. The new offerings may come from outsourcing providers who have developed expertise through developing their own sustainability capabilities, or may come from sustainability experts.

Two large outsource providers told us how they offer sustainability consulting services to buyers. One outsourcing executive told us of their sustainability consulting practice that had grown to employ 1000 people in under two years. Another large provider described helping a client to develop a balanced scorecard to focus on sustainability issues in the outsourcing relationship.

The large outsourcing providers publish sustainability white papers, articles and describe clients’ success stories. One large provider told us of a series of client case studies being prepared for publication. Another provider’s 2009 sustainability report cites numerous examples of businesses “optimizing their operations to minimize environmental impact … in a manner that maximizes performance”.

In summary, Figure 1 below describes the different practices of responsive and strategic sustainability in global IT outsourcing.
Figure 1. Responsive and Strategic Sustainability in Global Outsourcing

<table>
<thead>
<tr>
<th>Responsive Sustainability</th>
<th>Comments and examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Respond to customer sustainability requirements in an RFP or in re-negotiation of existing contract</td>
<td>More customers are requiring providers to demonstrate capabilities in areas of social and environmental responsibility</td>
</tr>
<tr>
<td>2. Comply with government sustainability regulations or industry guidelines</td>
<td>This will vary by jurisdiction and issue. For example, the UK is focused on the Carbon Reduction Commitment</td>
</tr>
<tr>
<td>3. Build employee pride through sustainability initiatives and reputation</td>
<td>Attracting and retaining new staff with demonstrable actions in sustainability (social and environmental)</td>
</tr>
<tr>
<td>4. Develop employee capabilities</td>
<td>Build skills in poor communities. Promote good health for employees and their families</td>
</tr>
<tr>
<td>5. Defend the value of the brand with sustainability activities</td>
<td>Sustainability may be an insurance against negative public reaction to future events</td>
</tr>
<tr>
<td>6. Cost reduction through Green-sourcing</td>
<td>Large global outsourcing firms are better equipped to lower energy consumption and reduce the carbon footprint for ICT intensive operations</td>
</tr>
</tbody>
</table>

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<thead>
<tr>
<th>Strategic Sustainability</th>
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</thead>
<tbody>
<tr>
<td>1. Enhance outsourcing relationship trust through shared social and environmental activities</td>
<td>Customers required that the outsourcing provider has a shared set of values and will contribute to common social and environmental goals</td>
</tr>
<tr>
<td>2. Deliver new value added services in sustainability</td>
<td>Leading outsourcing firms are building strong sustainability advisory practices</td>
</tr>
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Implications for outsourcing buyers and providers

For outsourcing buyers. Opportunities to work cooperatively with providers on sustainability initiatives will grow. There will be continued uptake by providers of sustainability practices and buyers will need to determine their individual appetite for working collaboratively on sustainability projects. For example, outsourcing providers will seek to match a buyer’s sustainability profile in order to build a trusted outsourcing relationship. In addition to shared views on sustainability, buyers should expect sustainability leadership from their outsourcing providers. For example, a provider should be able to demonstrate reduced carbon emissions through power management that is more efficient than the buyer could achieve.

In our review of public profiles we found that the large global providers had mature sustainability, while the mid-tier or smaller outsourcer providers were still building their sustainability capability. We also found that buyers infrequently validate the provider sustainability profile. So a caution to outsource buyers: beware of unsubstantiated sustainability claims. Buyers will increasingly demand evidence of global sustainability standards such as the Carbon Disclosure Project (CDP), the Global Reporting Initiative, Carbon Disclosure Project and the UN Global Compact. Several independent consultancies are able to assist buyers with sustainability audits of potential outsourcing providers.
For outsourcing providers. Providers can expect to work with buyers to collaborate on sustainability initiatives. Data center providers must be able to demonstrate energy efficiency that exceeds the levels set by buyers and required by governments. Buyers will ask for both capability and knowledge in sustainability, so providers must continue to hire and develop expertise in this area. Increasing sustainability will require compliance with government and industry standards, and constant evolution and upgrading of skills. For example, providers must be aware and should participate in the Global Reporting Initiative, Carbon Disclosure Project and the UN Global Compact. Providers must understand and provide leadership to their buyers in areas of government sustainability regulations.

The global outsourcing market continues to grow at double digit rates. The need for sustainable business operations is becoming apparent at an even faster pace. The combination of these two trends will provide opportunities and challenges for buyers and providers of outsourcing services for quite some time.

Ron Babin is an assistant professor in the Ted Rogers School of IT Management at Ryerson University in Toronto and a doctoral candidate at the Manchester Business School. Brian Nicholson is a Senior Lecturer at Manchester Business School and has been involved in teaching, research and consultancy projects in the broad area of global outsourcing of software and other business processes since 1995.
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6 Harsh Manglik, interview with primary author, January 12, 2010.