Drawbacks of a Modular Structure for IT Multisourcing

During the last decade, the modus operandi of IT outsourcing has undergone a major transformation. While earlier outsourcing deals were primarily executed with a single vendor, more recent deals often involve multiple vendors. When a firm contracts with multiple vendors for IT projects and services, this is called IT multisourcing. Numerous global companies, such as ABN AMRO, BP, Chevron, General Motors and Royal Dutch Shell, have adopted IT multisourcing strategies to reap the potential benefits this approach has to offer. Compared to traditional single-sourcing arrangements, key benefits include lower IT costs resulting from vendor competition and best-of-breed services, higher IT service quality and lower vendor dependency. Table 1 summarizes major benefits (and risks) of IT multisourcing.

The predominant approach to structuring IT multisourcing arrangements is based on the concept of vendor modularity. This approach follows the same logic as single-sourcing models: activities given to a vendor have to be “separable” from the activities performed by the client and other vendors, respectively. As a consequence, after the initial bidding phase at the latest, client firms tend to assign exclusive work areas to their multiple vendors. For example, in 2005, Dutch bank ABN AMRO signed an IT multisourcing contract worth $2.2 billion over five years...
with IBM for handling the IT infrastructure, with Accenture for application development and with a consortium of three Indian vendors (Infosys, Patni Computer Systems and Tata Consultancy Services) for application support and maintenance. Similarly, in 2008, Royal Dutch Shell entered into a five-year, $4 billion multisourcing deal with AT&T for network and telecommunications, T-Systems for hosting and storage and EDS for end-user computing and infrastructure services.

By assigning dedicated work areas (“modules”) to each vendor, IT multisourcing clients employ a traditional way to deal with complexity in organizations and to limit coordination costs. They break down large sets of IT activities into modules to make them more manageable. Each module’s internal activities can be treated as a “black box” and thus can be optimized without considering other modules’ activities. Moreover, each module produces an outcome that is basically independent of the client’s other activities. In other words, each module has few overlaps (if any) with other activities of the firm, and any links that do exist are easy to identify. Furthermore, each outsourced module communicates with other modules through a limited set of well-defined interfaces.

The positive relationship between modularity and outsourcing has been observed in a variety of contexts, for example in car manufacturing and microcomputer production and pharmaceutical R&D. Similarly in information systems, the modular nature of IT activities has been shown to facilitate outsourcing. Put differently, when establishing IT outsourcing arrangements, and IT multisourcing arrangements in particular, clients aim to maximize vendor modularity (i.e., reduce vendor overlaps) to decrease coordination efforts on their part and clarify vendor accountabilities.

However, there may be a possible downside in assuming that single-sourcing strategies can always be successfully applied to IT multisourcing scenarios. In particular, can the modularity strategy that works so well in single-sourcing arrangements be generalized to multisourcing? A possible problem with modularity in IT

Table 1: IT Multisourcing Benefits and Risks

<table>
<thead>
<tr>
<th>Benefits</th>
<th>Risks</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Increased vendor competition in terms of price, quality, reliability, innovativeness, etc.</td>
<td>• Decreased incentive for vendors to make client-specific investments (relationship building, knowledge, technology, etc.)</td>
</tr>
<tr>
<td>• Best-of-breed services</td>
<td>• Decreased incentive for client to make vendor-specific investments (see above)</td>
</tr>
<tr>
<td>• Reduced operational and strategic risk (lower vendor dependency)</td>
<td>• Increased management overhead/transaction costs (vendor contracting, coordination, etc.)</td>
</tr>
<tr>
<td>• Increased ability to find the best-fitting vendor (in terms of cost, quality, innovativeness, etc.)</td>
<td></td>
</tr>
</tbody>
</table>

multisourcing arrangements is that it can limit the level of ongoing competition among vendors—a frequently cited key benefit of IT multisourcing. In other words, with modularity, the client runs the risk of creating multiple vendor work silos with limited or no competition within each silo. Furthermore, modularity makes it very difficult to modify the overall architecture since each module has to remain compatible with the other modules, and no party has control over all the components.

Modularity could also increase the client’s dependency on a vendor because the vendor responsible for a module may come to “own” it. If the module’s activities are really managed as a black box, it may be difficult for the client to assess them properly.

These downsides of a modular approach raise the question of how an IT multisourcing arrangement can be structured to tap the full potential of multisourcing, including intense vendor competition, greater client flexibility and reduced vendor dependency. In existing modular IT multisourcing models employed by global companies such as ABN AMRO and Royal Dutch Shell, vendor competition is largely limited to the initial bidding phase.

In contrast to these more partnership-oriented modular approaches, our case study of the adidas Group (see Appendix for research methodology) describes a novel and arguably more “aggressive” IT multisourcing approach, which embraces overlaps in vendor skills and work areas. This approach enabled adidas Global IT to achieve high levels of both ongoing vendor competition and cooperation among its vendors, thereby leveraging the benefits of IT multisourcing while also minimizing many of the risks and challenges associated with such a sourcing strategy. The case of adidas thus provides a unique window for assessing the use of vendor overlaps in IT multisourcing.

However, allowing overlaps in vendor work areas increases the number of interfaces and the overall level of complexity and therefore requires considerable coordination. Overlapping vendor activities may also increase the difficulty in clarifying responsibilities, which makes vendor monitoring more difficult as well.

adidas Business and IT Background

The adidas Group is a major player in the global sporting goods industry. With more than 50,000 employees worldwide and annual revenues of about 15 billion euros (US$16.6 billion), adidas is currently the second biggest sporting goods company, behind the market leader, Nike. Its product line includes 20,000 diverse items and is updated twice yearly to respond to the highly competitive environment.

Globalized markets and increased competitive pressure in the sporting goods industry forced industry players to work to tight profit margins and be very conscious of cost. To save on costs, adidas (like its main competitors, such as Nike) relied heavily on outsourcing for product manufacturing. For example, since 1993, the bulk of adidas’ production has been outsourced to suppliers in Asia. Against this backdrop, it is not surprising that corporate strategists at adidas also saw the value of IT outsourcing, including IT offshoring, as a viable cost-cutting tool.

Since the late 1990s, the strategic focus of the adidas Group has shifted from being a pure wholesaler to engaging in direct interactions with end consumers around the globe. As a pure wholesaler, adidas sold containers of sporting goods to major retailing partners, but entered the retail business in the late 1990s by opening its own retail stores and launching its own e-commerce platforms. In 2010, adidas operated more than 1,350 retail concept stores worldwide.

The strategic shift from wholesaling to retailing significantly increased the demand for more flexible, more innovative and consumer-oriented IT solutions. As a consequence, IT was no longer regarded only as a mere operational tool, but also as an important contributor to competitive differentiation and value creation. This change is also reflected in the new mission statement of adidas Global IT, the internal IT organization of the adidas Group: “Building a

17 Euro/dollar conversion rate as of early July 2016.
digital ecosystem for the enthusiastic consumer and the empowered employee.”

adidas Global IT currently employs about 1,050 IT experts worldwide. It is structured in eight vertical units, called “Centers of Excellence” (CoEs), which largely mirror the organizational structure of the business (e.g., sales and retail, ecommerce, operations and marketing) (see Figure 1). As indicated above, adidas' IT organization has a long history of outsourcing and offshoring. As early as 1998, adidas had started to outsource IT projects and services to an Indian Tier-1 vendor, referred to as India1 in the following. In 2007, adidas Global IT set up a captive offshore service center with this vendor in Hyderabad, India. Over time, however, adidas felt that India1 was becoming more and more complacent and that the quality of IT resources and services it provided had decreased. When India1 declined to renegotiate cost rates, adidas Global IT realized how dependent it had become over the years on this single vendor (see also Figure 1). The company therefore embarked in its IT multisourcing journey.

**adidas’ Multisourcing Journey**

adidas’ multisourcing journey had two phases. In Phase 1, IT work was outsourced on a CoE basis, with each CoE having to use at least two vendors within its area. This led to many vendor overlaps and interfaces. Following a restructure of adidas Global IT into “horizontal” cross-CoE IT functions, there were fewer but larger vendor overlaps in Phase 2 of the journey.

**Phase 1: Introducing IT Multisourcing (2011-2013)**

In 2009, around the time that adidas Global IT realized that India1’s performance was declining, a new CIO joined the adidas Group. To create a highly competitive vendor environment, he introduced a new IT multisourcing strategy in 2011. This strategy runs contrary to well-established industry practices because it embraces vendor overlaps (as opposed to vendor modularity). Specifically, the CIO and his senior management team decided to contract with two additional offshore Tier-2 vendors. One, which we call India2, is a medium-sized, Indian company certified as Level 5 of the Capability Maturity Model Integration (CMMI) model and is “hungry” for work and willing to offer highly competitive pricing. The second, which we call Belarus, is a medium-sized, CMMI Level 4 company from Eastern Europe. Its culture is similar to that at adidas’ German headquarters. The vendor selection process was orchestrated carefully to ensure that India2 and Belarus have skillsets that overlap significantly with the former single vendor, India1. This ensured that each vendor

![Figure 1: Single Vendor Outsourcing at adidas](image-url)
was able to take on virtually any project or service in adidas’ entire IT portfolio.

The wide overlaps in vendor skillsets meant that adidas Global IT could assign IT projects and services to the three vendors in a way that was characterized by vendor overlaps. Most importantly, each vertical unit (CoE) in adidas Global IT had to work with at least two of the three vendors. Moreover, within a vertical, two vendors often had to work together to provide support services for a single software application. For example, one vendor might be responsible for first- and second-level support, while another was responsible for third-level support. And sometimes, all three vendors had to work together on one project:

“There are projects where we have seen all companies working on the same project.”
Regional Director, India2

adidas’ CIO emphasized that vendor overlaps were created intentionally in the IT multisourcing arrangement:

“… It was absolutely intentional that there is a significant overlap, and, in fact, we push some of [the vendors] to increase the overlap. So, ideally, for every single [task], in any area of my organization, I have all three of them bidding.” CIO, adidas

By embracing significant overlaps among vendor skills and tasks, adidas Global IT ensured that each vendor was simultaneously competing and cooperating with the other two vendors.

The resulting vendor overlaps were numerous but often small when considering the size of each work component awarded through a request for proposal (RfP). More specifically, although the infrastructure teams were shared among the various CoEs, the vendors’ development, testing, integration and support teams were embedded into each vertical unit. Thus, the vendor overlaps were created at a very granular level (see Figure 2). This does not mean, however, that vendors performed exactly the same type of activities, which could have led to management challenges when responsibility for the work needed to be determined. Rather, vendors were assigned to different but interfacing areas of work. For example, in one project:

“[India1] was more focused on the functional aspect of the delivery, and [Belarus] was more on the technical aspect of the delivery. So, there is no mix in the same sort of a role, but it’s a mixed team delivering the project. So, from that perspective, … adidas has been successful in keeping two parties where we are not stepping on one another.”
Group Project Manager, India1

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**Figure 2: Vendor Overlaps and Interfaces in Phase 1**

![Vendor Overlaps and Interfaces in Phase 1](image-url)
Ultimately, though, it was adidas management that was responsible for coordinating the vendors, ensuring coherence and integrating the project results and program management levels.

Furthermore, by dividing the work for each CoE into small “chunks,” adidas Global IT was able to easily create “room” for the two new vendors without taking away significant business from India1 all at once. This approach also removed the risk associated with assigning major work areas (e.g., software development) to a new vendor that is not familiar with the client’s business context and IT landscape. Additionally, the small chunks meant that adidas issued many RfPs per month, which provided the new vendors with numerous opportunities to build up a significant business volume with adidas, while at the same time promoting competition among the vendors.

Moreover, because of the vertical CoEs, the vendor work packages were closely aligned with the requirements of the respective CoEs, as highlighted by adidas Global IT’s Senior Vice President: “The multisourcing structure was highly successful in terms of driving business alignment and business satisfaction.”

The significant overlaps between the vendors’ areas of work could have led to haggling and conflicts among the vendors. However, in part because the vendors had significant business with adidas, relationships among vendors remained constructive, and they collaborated to find solutions to problems:

“In the end, you will have a couple of software developers from two different companies that need to find a solution for whatever problem they have ... very, very few times [did] I have an escalation from one of my guys, working on the account, where they felt that [they were] being treated unfairly by another vendor.”
Account Manager, Belarus

Even when a new vendor took business away from the original vendor, the relationship between the two remained professional:

“There are some cases where we need to transition out services. ... So, in those cases, we have gone as far as inviting [India1] people to [India2] to [help with the] transition. ... Surprisingly, it was not very hostile ... it's a very friendly environment.”
Regional Director, India2

Using multiple and overlapping vendors was especially favorable to the two new vendors, and ultimately to adidas Global IT. Because of the overlaps, India2 and Belarus were able to learn from India1 and get up to speed on the various work areas at adidas in a relatively short period of time. This enabled them to compete with the former single vendor as equals, to develop new competencies (that they could also market to other clients) and to make innovative suggestions on how to improve IT operations at adidas.18

Nevertheless, the collaborative vendor environment did not mean that there was no pressure applied by adidas on the vendors. Even some of the joint meetings, required to coordinate the vendor overlaps, were used to apply subtle pressure on vendors:

“Weekly, I have so-called technical architects meetings where I am sitting together with my guys, and I invite [India1] and [Belarus]. ... [When] you have [them] sitting at the same table ... everyone tries to present himself or herself in the best manner, tries to present his or her company in a good light.”
Senior Manager Wholesale ERP, adidas

In summary, by introducing IT multisourcing and by deliberately implementing a multisourcing structure that embraced vendor overlaps, adidas Global IT significantly increased vendor competition and decreased its dependency on any of the vendors. Although the vendor overlaps led to intense competition, they also created an environment that fostered vendor collaboration and learning.

However, adidas’ multisourcing structure also had some drawbacks. For example, the high level of decentralization led to required skills, such as Java developers, being replicated in each CoE. This replication limited greatly the vendors’ ability to exploit economies of scale and scope, making the work for adidas less attractive for the vendors.

In addition, by creating a high number of vendor interfaces that had to be managed, the structure led to increased transaction costs for both adidas and the vendors. These costs arose in three ways. First, even when the vendors had different work streams within an IT project or for an IT service (e.g., development vs. testing, first- or second-level support vs. third-level support), each vendor had to coordinate its work stream with the work stream(s) of the other vendor(s). Usually, this coordination also involved adidas managers, creating yet another interface. Second, the various projects and services also had to be coordinated with each other, to ensure coherence in the portfolio of each CoE. Third, each CoE had to coordinate with the other CoEs to ensure coherence at a corporate level.

Transaction costs were also increased by the frequent issuing of RfPs, often for very small projects. Another drawback of the Phase 1 multisourcing structure was that adidas retained the final responsibility for resolving problems in a project staffed with multiple vendors:

“So, who takes the responsibility if the project goes wrong? Who takes the responsibility of ensuring responsibility that the timelines are met? Who takes the responsibility of mitigating risks in a project? The answer is adidas.” Regional Director, India2

Phase 2: Leveraging IT Multisourcing (2013-2015)

Two years after the introduction of the new IT multisourcing strategy, adidas’ CIO and his senior management team were generally satisfied with the outcomes. India2 and Belarus had reached a critical threshold of business volume and were able to enter into intense competition with India1. adidas Global IT’s management thus felt that the time had come to address the drawbacks of the existing structure, which was designed to successfully onboard the two new vendors. The overarching idea in Phase 2 was to implement what the CIO labeled an “industrialization of the IT organization.” To do so, adidas Global IT built horizontal IT functions across all of its CoEs for development, testing, integration and support activities. This structural change was not fundamentally linked with outsourcing. It was an organizational change that shifted the view of IT activities from a CoE-centric view to a process-centric view. Figure 3 illustrates the changed structure.

With this new structure for adidas Global IT, there were still overlaps between the three offshore vendors, but the pattern of overlaps had changed. The original “vertical” overlaps were very granular. In contrast, the new structure, which was based on four basic IT functions, emphasized “horizontal” overlaps that were fewer in number but bigger in size than the previous overlaps. The goal was to “bundle” vendor business volumes by limiting the number of RfPs within each function to one per type of technology (e.g., Java) or business domain. Issuing RfPs in this way helped to regroup related tasks across the CoEs. This also meant that IT projects and services were no longer the specific responsibility of the adidas CoE managers.

Interestingly, each horizontal IT function was organized differently. For example, the development function was structured around development technologies, whereas the testing function was structured by domains (which are closer to the CoEs). Two vendors were assigned to each horizontal function, and projects involving two or more functions had to be carried out by different vendors for each function. Thus, for example, the development group of one vendor had to interface with the testing group of another vendor. This arrangement enabled adidas to sustain high levels of vendor competition and made sure that the vendor environment did not get “too collaborative:"

“[it is] not the objective to make them ‘one.’ … they should stay alert, they should stay competitors. It’s like a football match … you absolutely want to win that game.” CIO, adidas

When looking at the overlaps in the new structure, the number of interfaces was drastically reduced compared to Phase 1. Vendors within one horizontal (for example Java development) now coordinated at most with two vendors, one for upstream and one for downstream activities (also organized by horizontal). Thus, there were fewer overlaps between vendors, but they were larger in size (see Figure 4).
Overall, the Phase 2 multisourcing structure was positive for adidas because it continued to limit vendor modularity. No vendor could work in isolation from the others because they had to interact closely, although in more concentrated ways. This resulted in much larger blocks of outsourced work, which enabled the vendors to better leverage economies of scale and scope, and reduced adidas’ coordination costs. To further reduce coordination costs, adidas Global IT introduced a new vendor management team. This team was primarily concerned with increasing the level of standardization in terms of contracts (in particular, the development of templates for the statements of work for individual IT projects and services), vendor rate cards and key performance indicators that were used for steering the three vendors.

The vendors also perceived the new structure as positive because it facilitated skills development, as is typical with such functionally oriented structures. Moreover, the vendors found that the new structure, and the better-defined vendor interfaces in particular, made vendor collaboration less onerous because (in the words of an India2 Regional Director) “responsibilities are [now] very, very clearly demarcated.” This had been a key drawback of the earlier structure because the fine granularity of the tasks made responsibilities for the larger body of work difficult to pinpoint.

Moreover, the interface used in the new structure was easier for the vendors to understand and implement. The old separation of activities, along the verticals, had been a good fit with adidas’ IT organizational structure. However, the structure based around horizontal IT functions seemed to be a good fit with how IT people tend to think of and separate IT activities. This could explain why it was well received by the vendors. Additionally, the new structure put pressure on the vendors to improve their performance:

“Everybody’s measuring the efficiency of every horizontal, and every vendor in that horizontal is required [to perform] on a very competitive basis. So there is competition between the horizontals and also within the horizontals.” Regional Director, India2

Summary of adidas’ Multisourcing Journey

Prior to adopting a multisourcing strategy, adidas Global IT had been in a long-term relationship with India1 that could probably...
be considered a co-operative partnership.\textsuperscript{19} adidas not only gave a major portion of its IT outsourcing budget to India, but it also established a captive center with this long-term vendor, which would suggest the existence of complementary goals. However, as is often the case in such co-operative partnerships, especially those that are focused on creating internal efficiencies, the power balance shifted in favor of the vendor, and the once-stable partnership began to deteriorate.\textsuperscript{20} To redress the balance between adidas and its outsourcing vendor, adidas Global IT adopted a multisourcing strategy (Phase 1 of its IT multisourcing journey) and fine-tuned this strategy in Phase 2.

The changes that adidas’ IT organization made during its multisourcing journey can be summarized under three headings: organizational structure, contract structure and the consequences of each phase (see Table 2). Phase 2 coincided with a changed organizational structure for adidas Global IT. The initial move toward multisourcing (Phase 1) had retained the correspondence between IT projects and the CoEs. However, the change to horizontal cross-CoE IT functions meant that, in Phase 2, outsourcing the development of new systems, as well as their testing, integration and support, took the same form as infrastructure management. From this point in time, the bidding process and the boundaries of RfPs changed. They now matched the horizontal layers (IT functions) instead of the vertical silos (business functions).

The contract structure evolved through each phase, shifting from one extreme to the other. In the single-sourcing era, contracts were large, awarded infrequently and, because there was a single vendor, did not overlap in terms of skills and areas. In Phase 1 of the multisourcing journey, the nature of vendor contracts was transformed drastically. Rather small contracts were awarded very frequently, facilitated by extensive skill and numerous work overlaps. This created the need for many interfaces between the vendors to coordinate interdependencies across work processes and outputs. In Phase 2, the introduction of the horizontal IT functions reduced the bidding frequency to a more manageable level, with the larger size of each RfP being more attractive to the vendors. This change was accompanied by an increasing focus on standardization (e.g., harmonization of vendor rate cards and introduction of contract


\textsuperscript{20} Ibid.
templates), which enabled adidas to handle bidding processes and the ensuing contracts more consistently and smoothly. Overlaps in vendor skills and areas were retained in Phase 2, with two vendors participating in each group of activities. However, the number of interfaces reduced to a more manageable level.

In terms of consequences, the level of both vendor competition and cooperation remained high after adidas’ switch to IT multisourcing. adidas no longer depends on a single vendor for any given activity. Although the initial Phase 1 multisourcing structure removed the incumbent vendor’s monopoly status and successfully onboarded two new vendors, it still resulted in high coordination costs. It can thus be argued that Phase 1 was an interim multisourcing strategy that allowed adidas to “unfreeze” the status quo. The Phase 2 structure, built around the horizontal IT functions, helped to reduce the coordination costs associated with the multisourcing strategy. Moreover, this change led to an increase in vendor accountability and enabled the vendors to achieve economies of scale and scope.

Table 2: Summary of Main Characteristics and Consequences of Single Sourcing and Multisourcing Phases

<table>
<thead>
<tr>
<th></th>
<th>Single Sourcing</th>
<th>Phase 1: Introducing Multisourcing</th>
<th>Phase 2: Leveraging Multisourcing</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of IT vendors</td>
<td>1</td>
<td>3</td>
<td>3</td>
</tr>
</tbody>
</table>

**Organizational Structure Characteristics**

<table>
<thead>
<tr>
<th></th>
<th>Business-centric (verticals)</th>
<th>Business-centric (verticals)</th>
<th>Process-centric (horizontals)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dominant IT structure</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Control of sourcing process</td>
<td>Individual CoE</td>
<td>Individual CoE</td>
<td>IT organization</td>
</tr>
</tbody>
</table>

**Contract Structure Characteristics**

<table>
<thead>
<tr>
<th></th>
<th>Large</th>
<th>Very small</th>
<th>Medium</th>
</tr>
</thead>
<tbody>
<tr>
<td>RfP size</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bidding frequency</td>
<td>Low</td>
<td>High</td>
<td>Medium</td>
</tr>
<tr>
<td>Overlaps in vendor skills</td>
<td>None</td>
<td>High</td>
<td>Medium to high</td>
</tr>
<tr>
<td>Overlaps in vendor areas</td>
<td>None</td>
<td>Task level (many overlaps)</td>
<td>Function level (fewer overlaps)</td>
</tr>
<tr>
<td>Number of interfaces between parties</td>
<td>Low</td>
<td>High</td>
<td>Medium</td>
</tr>
<tr>
<td>Level of standardization</td>
<td>Medium</td>
<td>Medium</td>
<td>High</td>
</tr>
</tbody>
</table>

**Consequences**

<table>
<thead>
<tr>
<th></th>
<th>Low (to none)</th>
<th>High</th>
<th>Medium to high</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vendor competition</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Vendor cooperation</td>
<td>Low (to none)</td>
<td>High</td>
<td>Medium to high</td>
</tr>
<tr>
<td>Transaction costs (coordination, etc.)</td>
<td>Low to medium</td>
<td>High</td>
<td>Medium</td>
</tr>
<tr>
<td>Client dependency on vendors</td>
<td>High</td>
<td>Low</td>
<td>Low</td>
</tr>
<tr>
<td>Vendor economies of scale and scope</td>
<td>High</td>
<td>Low</td>
<td>Medium to high</td>
</tr>
</tbody>
</table>
Benefits Realized from adidas’ Multisourcing Journey

adidas benefited in several ways from how it introduced (Phase 1) and leveraged (Phase 2) its IT multisourcing strategy. On average, IT service costs per activity have dropped by more than 20%, and the average number of defects per lines of code has halved. adidas and its vendor partners expect the structural organizational change—the introduction of the four horizontal IT functions—to maintain these cost and quality benefits:

“By ‘horizontalizing’ these functions, ... they’ll be able to better leverage process tools and also ... bring in a lot of synergies, which might help them in [further] reducing the cost and increasing the quality.” Account Manager, India1

Another efficiency that was gained by adidas (and its vendors) was in the issuing and processing of RFPs. Having access to three knowledgeable and skilled vendors—all of whom were familiar with the context, infrastructure and processes in virtually any area of adidas’ IT portfolio—significantly simplified the RFP process. In addition, harmonizing the vendor rate cards and introducing standard templates for project and service contracts speeded up the process for evaluating bids and contracting with vendors. In particular, standardization helped reduce the amount of information required for processing an RFP.21 Furthermore, by having three competent vendors knowledgeable about its operations, adidas Global IT had constant cost and quality benchmarks, which contributed to a further increase in vendor competition.

In addition, by creating vendor overlaps instead of using a modular multisourcing structure, adidas avoided the reduction of flexibility that can be associated with modular multisourcing. As mentioned by one respondent:

“[The IT multisourcing strategy made] the whole agility and flexibility of adidas IT better.” Senior Manager Group Procurement IT, adidas

In this context, an important element is that adidas was able to restructure its IT delivery processes, which in itself demonstrates the advantage of the low level of modularity in its IT multisourcing approach. Prior research indicates that outsourcing modular activities leads to rigidity in the IT architecture. Although a modular approach makes it easy to optimize each component, it becomes very difficult to modify the overall architecture. A modular configuration would have limited adidas’ ability to change its overall IT configuration without having to renegotiate relationships with its vendors (which can be costly). Because its multisourcing strategy was built around vendor overlaps, adidas was able to transition from a CoE-centric organization to a process-centric organization without any contractual difficulties. The changes were introduced by gradually adjusting the allocation of tasks among the vendors and by adjusting the pattern of the tasks included in the RFPs. By outsourcing in a non-modular way, adidas had the flexibility to modify the IT group structure and was thus able to introduce significant organizational changes without contractual hurdles (while also maintaining the vendor overlaps).

The three vendors also benefited from adidas’ IT multisourcing strategy. By challenging India1 (the incumbent vendor), two new vendors (India2 and Belarus) spurred the incumbent to increase staff motivation and to further professionalize its internal processes. As a consequence, India1 became more responsive to adidas’ needs and improved its service quality while lowering its prices. India2 and Belarus were also providing creative and competent services and were able to compete with India1 at the same level. By 2015, both India2 and Belarus had reached business volumes of 10 million euros ($11.1 million), twice the critical threshold of 5 million euros that adidas originally defined for the new vendors. At the same time, India1’s revenues from adidas grew from 19 million euros ($21 million) in 2010, the year before the two new vendors were onboarded, to 40 million euros ($44.4 million) in 2015. This growth in vendor business volumes was enabled by an increase in adidas’ IT budget (which is set as a fixed percentage of group revenues) and reallocating

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Lessons Learned from the adidas Case

We believe that many lessons derived from adidas’ multisourcing journey can be applied in other organizations. We highlight six lessons about how to structure and manage IT multisourcing arrangements. The first three relate to the use of vendor overlaps, which were introduced in Phase 1 of adidas’ multisourcing journey. The other three stem mainly from Phase 2 of the journey. In Phase 2, adidas was able to alleviate some disadvantages of its initial multisourcing approach through the adoption of a new IT organizational structure and a matching sourcing structure.

Lesson 1. Embracing Vendor Overlaps Promotes Ongoing and Healthy Vendor Competition

Padula and Dagnino posit that competition requires “inter-firm interdependencies.” Embracing vendor overlaps in multisourcing arrangements thus means that competition (and cooperation) is always present in any area of work that is awarded to a vendor. This was the case at adidas, which recognized that simply having more than one vendor was not sufficient to create real competition:

“In every field of services, we have always a minimum of two [vendor] options and sometimes even three options.” Director, Corporate Marketing CoE, adidas

In contrast, by using a modular structure for multisourcing in which the client assigns exclusive work areas to each vendor (see Figure 5), client firms, according to adidas’ CIO, “[virtually] create a monopolist in every area.”

Modular IT multisourcing arrangements are more partnership-oriented and cooperation-dominant approaches to multisourcing. Cooperation might be promoted by remuneration systems such as BP’s system of risk-based rewards, which were distributed among its three service partners, or other contractual mechanisms, such as gain sharing, which are designed to incentivize service providers.

Such cooperation-dominant IT multisourcing arrangements may promote a longer-term view of the relationships among the vendors, as well as the client. They may also promote more stability, especially compared to Phase 1 of adidas’ IT multisourcing journey, where frequent structural adjustments had to be made to balance the need for competition with the heavy cooperation requirements. This suggests that the initial structure used by adidas is legitimate only as an interim multisourcing strategy and will likely not be the best long-term structure.

In addition, embracing vendor overlaps means that clients need to accept an increase in (internal) coordination costs, at least in the beginning. Coordination is needed to ensure that production costs are minimized through vendor competition. The implication is that clients must take on the responsibility for managing the vendor overlaps rather than spreading the responsibility across the vendors.

Lesson 2. High Granularity in Vendor Overlaps Reduces Vendor Onboarding Risk and Accelerates Vendor Learning

Dividing outsourced activities into very granular ones facilitates the introduction of new vendors into the multisourcing mix. Outsourcing a major chunk of work to a new vendor could be high risk both for the client and the vendor. The client might lack prior knowledge of the vendor, and the vendor might have no prior knowledge of the client and limited knowledge of the domain in which the client operates. This lack of knowledge, combined with the new collaboration mode, would make the new venture very risky. With the granular approach, the use of smaller RFPs enables new vendors to familiarize and gain experience and knowledge with the client as well as with the other vendors, thereby limiting the risk to the client.

For example, in Phase 1, the fine-grained (vertical) vendor overlaps required adidas’ new vendors to work with its former single vendor, enabling them to learn from this vendor and facilitating knowledge transfer among the vendors. Moreover, the overlapping work areas also prompted the incumbent vendor, and enabled the new vendors, to question the status quo, promoting the development of innovative ideas on how to improve IT operations at adidas. The nature of the relationships among adidas’ existing and new vendors is consistent with the results of a study on “coopetitive” relationships in the semiconductor industry, which reports that interorganizational relationships characterized by both high competition and high cooperation are the most innovative ones. But because the competitive forces are so dynamic, such relationships tend to be tenuous, as a steady state is hard to achieve, and constant adjustment is needed. That could explain why there was so much flux during adidas’ IT multisourcing journey.

High granularity of vendor overlaps also means that new vendors start with a small portfolio that they can grow over time. Providing growth opportunities ensures that the vendors remain actively interested in additional business and continue to bid aggressively on subsequent RfPs, which lowers prices further. High granularity also ensures that a former single vendor does not lose a huge portion of its contracts all at once, which could adversely impact vendor morale. On the other hand, high granularity of vendor overlaps makes it difficult for vendors to exploit economies of scale and scope, and requires more coordination on the part of the client.

Lesson 3. Providing Vendors with Opportunities for Growth Helps Sustain Competition and Cooperation

Adopting an IT multisourcing strategy is challenging for both the client and the involved vendors, especially when the strategy embraces vendor overlaps. Each vendor is constantly competing with the other vendors and, at the same time, has to collaborate with them to ensure that activities are completed.

adidas’ three vendors found that the work was generally satisfying, and the collaboration climate was good. The vendor satisfaction was likely linked to adidas having acquired the management capabilities to carefully balance the vendor overlaps so that the vendors’ efforts were valued. adidas’ CIO ensured that the business volume of each vendor was growing. Even India1, which lost its “quasi-monopoly” status, doubled its revenues from adidas in five years. The growth in business ensured that the vendors continued both to treat adidas as a preferred client and to provide high-quality services.

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Overall, the benefits of the multisourcing strategy compensated for the additional efforts introduced by the multivendor constraints. However, it would probably be difficult to provide the same level of motivation if the vendors’ business with the client was declining. In the situation, transitioning activities from one vendor to another could become acrimonious.

**Lesson 4. Vendor Overlaps Create Both Short-Term and Long-Term Benefits**

In the case of adidas, the vendor overlaps created immediate benefits: a decrease of vendor dependency (and complacency), a reduction in IT project and service costs, and an increase in the quality of IT services received. These benefits were observed shortly after adidas had introduced its new multisourcing strategy and were thus a clear outcome of the competition created by vendor overlaps.

What was less visible at the time (Phase 1), but could be observed later on (Phase 2), was the flexibility that vendor overlaps provided to adidas. As mentioned earlier, most outsourcing arrangements are modular and create a rigid structure. Once modules are assigned to vendors, reshuffling the activities among vendors becomes very difficult because it requires a contractual adjustment with each of them.

The way in which IT activities were restructured at adidas was not linked primarily with IT multisourcing; rather the new structure was a different way to view the IT organization. Because of the numerous vendor overlaps created in the initial (Phase 1) IT multisourcing structure, adidas was able to shuffle the vendor activities over a relatively short time to match the new structure. This reshuffling was accomplished without having to renegotiate any vendor contracts (which can be very costly). The ability to quickly and easily reassign work among the vendors provided a significant long-term benefit. While adidas recognized that coordinating vendor overlaps can be costly, this ability provided a degree of multisourcing flexibility that is at least on a par with that observed in an internal organization.

**Lesson 5. Less Granular, Horizontal Vendor Overlaps Help Reduce Coordination Costs and Improve Accountability**

Horizontal vendor overlaps can be a valuable tool for managing IT multisourcing by ensuring vendor competition, while at the same time reducing the number of vendor interfaces. The creation of adidas’ horizontal IT structure that coincided with Phase 2 of its multisourcing journey increased the size of the work activities included in each RfP. Activities were separated according to the four horizontal IT functions: development, testing, integration and support. This separation corresponds to a traditional view of the IT production function and is readily understood by the client and its multisourcing vendors. In turn, the use of familiar interfaces enables easier coordination for the client by limiting the number of interactions among vendors, while still allowing for the presence of more than one vendor in each stream of activities. Moreover, separating activities along traditional IT functions increases vendor accountability for each set of activities. It also enables the creation of larger units of work, which helps the client to limit the administrative burden (e.g., the number of RfPs issued) and the vendors to generate economies of scale and scope.

**Lesson 6. Treating Multiple Vendors as an Ensemble Facilitates a High Performance Environment**

Multisourced activities should be viewed as an ensemble of interdependent activities—in terms of both vendor selection and task assignment. Much of the success of adidas’ IT multisourcing strategy is due to the ensemble of vendors that adidas selected. Had adidas selected two or more Tier-1 vendors, the level of competition may have been so high as to prevent cooperation. On the other hand, had adidas selected two additional Tier-3 vendors, they may not have been able to compete at “eye level” with adidas’ long-term Tier-1 partner (as India2 and Belarus were able to do successfully). Furthermore, the number of vendors in the ensemble is a crucial factor. The more vendors that are hired, the more difficult it is to control and coordinate vendor activities.

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29 Hui, P. P. et al., op. cit., 2008; Aubert, B. A. et al., op. cit., 2012.
How adidas Realized Benefits from a Contrary IT Multisourcing Strategy

as well as to integrate their deliverables. adidas specifically chose to work with just three vendors—a number it deemed would create intense vendor competition but would be manageable in terms of control and coordination efforts.

As mentioned earlier, while competition among the vendors remained strong, they were able to work together harmoniously. At no point did our interviews with vendor representatives indicate a lack of respect for the skillset of competitors. In fact, by selecting a limited number of vendors with overlapping strengths and skillsets, adidas was able to realize the full benefits of IT multisourcing.

The overall structuring of task assignments should also be treated as an ensemble. CoE managers in adidas Global IT had typically selected the vendor that made the lowest bid or with whom they had worked before. As a consequence, some CoEs were not distributing the work as had been mandated and, at times, the adidas CIO overrode their selection to better balance the loads of the three vendors. This suggests that there needs to be some broader oversight and management capabilities to ensure that an IT multisourcing strategy is implemented successfully. For example, certain activities may be co-dependent, and keeping them together may improve scheduling and reduce production costs.

adidas may have realized this when it increased the granularity of the vendor overlaps as a consequence of introducing the horizontal IT functions. This suggests that grouping an ensemble of activities might be required to ensure coherence is retained. In these cases, overlaps in vendor responsibilities over a larger set of activities might be more efficient than excessive granularity resulting from breaking up activities among multiple vendors. Finally, the client needs to consider the extent to which it must integrate (or supervise the integration of) the deliverables produced by the various vendors so it can maintain the necessary levels of control and coordination.

Concluding Comments

The traditional approach to IT outsourcing has been to “isolate activities and outsource.” Outsourced activities are decoupled from other activities of the firm to minimize client coordination efforts and to ensure vendor accountability. The same logic has been used to determine the structure of IT multisourcing arrangements. However, a fundamental appeal of multisourcing is vendor competition, which can reduce clients’ IT costs and increase IT service quality. But a modular multisourcing structure, achieved by isolating activities, can create a quasi-monopoly that may be difficult to break free of once the contract is awarded to one vendor. Another drawback of a modular multisourcing structure is the rigidity it can introduce into the organization’s IT architecture and configuration. Overcoming this rigidity often requires costly renegotiation of the various vendor contracts.

adidas’ IT multisourcing strategy shows, however, that it is possible to avoid the downsides associated with modular multisourcing—providing that the client invests sufficient effort, shows intent and puts adequate care into selecting vendors. By nurturing vendor overlaps, adidas has been able to promote vendor competition and realize a range of benefits. Competition among adidas’ vendors is ongoing in every part of an IT project or service. It is not restricted to one-off exercises every few years once a contract has expired.

The adidas case also highlights the importance of organizational design for IT multisourcing success. After restructuring its IT organization, adidas was able to implement a new IT configuration within an existing outsourcing framework and thus retain its organizational flexibility.

The lessons from the adidas case show the benefits of adopting a contrary strategy for IT multisourcing strategy—one that embraces vendor overlaps rather than a modular structure. The guidelines derived from the lessons will help other organizations do the same. When defining an IT multisourcing strategy, many companies start from a situation where they are dealing with only one IT outsourcing vendor or where internal services control the bulk of the IT activities. By initially creating vendor overlaps at a fine-granular level, client firms can shape a highly competitive vendor ecosystem and generate an environment that is flexible. In today’s volatile business and IT environments, flexibility is a key

30 Kumar et al., op. cit., 2009.
ability for organizations, especially when they have to adapt their internal structures.

We recognize that adidas’ arguably “hard-hitting” IT multisourcing strategy can be seen as part of its business strategy, which relies on margin-conscious outsourcing to survive in the increasingly competitive global sporting goods industry. We also acknowledge that adidas’ multisourcing strategy is not a low-cost approach in terms of governance costs. However, as shown in this article, the benefits obtained from the increased vendor competition significantly offset the costs associated with vendor overlaps. We believe that adidas’ approach to IT multisourcing can encourage and inspire IT decision makers in other organizations to rethink the role of modular multisourcing structures and that the lessons learned from the adidas case will help them realize the full potential of their existing or future IT multisourcing strategies.

Appendix: Research Methodology

Data was gathered primarily from direct observations by two of the authors, a series of information meetings, two workshops with adidas managers and three rounds of semi-structured interviews. In total, 22 interviews were carried out over a period of almost three years (November 2012 to June 2015). Thirteen interviews were conducted with adidas IT managers, including the CIO and the Senior Vice President, as well as procurement managers and members of the sourcing team, who were responsible for the implementation and administration of the IT multisourcing strategy at the operational level. Nine interviews were conducted with key vendor employees who held job titles such as Account Manager, Group Project Manager and Regional Director. The interviews lasted between 45 minutes and three hours and were usually conducted by two researchers, with one running the interview and the other listening, taking notes and requesting clarification when necessary. Most interviews were recorded and transcribed immediately after the interview. The interview transcripts totaled 386 pages (220,144 words). Follow-up e-mails and phone calls were used to clarify any questions that arose during the interview transcription.

The research team also reviewed vendor contracts (all vendor master agreements as well as selected project/service agreements), steering board presentations, meeting minutes and other internal documents.

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