



# ***Practical Outsourcing What, Why and How.....***

## ***An Op2i Perspective***

***April 2008***

***“Outsource everything except your soul....” Tom Peters***



## *In this perspective*

- What is outsourcing – should I be bothered?
- What should you outsource - and importantly, what not to outsource?
- Why should you outsource – will it make a difference to my bottom-line?
- Where should you outsource to – why all this talk about India?
- Whom should you outsource to – who can I really trust?
- Will outsourcing hamper innovation – am I giving away the crown jewels?
- Why things go wrong – we've all heard the stories?
- Assessing what processes to outsource?
- Why Op2i?



## *What is outsourcing?*

- Outsourcing is nothing new.
- From the 1600's and earlier, the British have had work done for them abroad, even if it was simply the processing of sugar in Antigua.....
- Outsourcing is essentially an elaborate description for an arrangement whereby a company carves out certain services that it has been providing internally and retains a third party to provide these services.
- Offshoring is sometimes described as outsourcing to service providers in another country.



## *Benefits of outsourcing?*

- The typical benefits from outsourcing include:
  - Allows focus on “core” competence of the company
  - Cost-savings from reduced overheads and consequent reduction in training needs
  - Cost-savings through economies of scale gained by the outsourcing service provider
  - Higher levels of service and performance due to specialization of the service provider
  - Reduction of capital expenditure (IT systems, support systems etc)
  - Shorter times to market for a customer’s services (more flexible and responsive process for the outsourced services)
  - Standardized IT infrastructure and processes – possibly in a shorter time than it would be feasible without outsourcing.
  - Improvement in processes and their documentation – something that tends to get ignored internally
  - and in Offshoring – labour arbitrage...



## *Cost and risks of outsourcing?*

- The typical costs and risks that a customer must assess include:
  - Loss of day-to to-day management control of outsourced services and excessive dependence on the service provider for performance.
  - Dependence on the service provider for strategic information on internal technology, operational and business options.
  - By transferring employees and assets to the outsourcing service provider, the customer risks losing valuable knowledge and experience from displaced workers.
  - Additional costs associated with managing the outsourcing service provider.
  - Reassuming responsibility for the outsourced services on termination of outsourced services can be inherently difficult and risky
  - Potential risk of IPR theft
  - Data protection
  - Regulatory obligations still responsibility of company
  - Bad PR and press

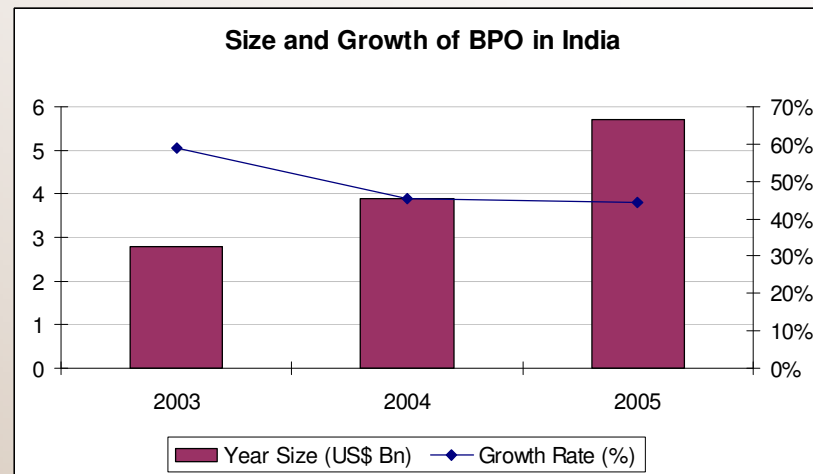
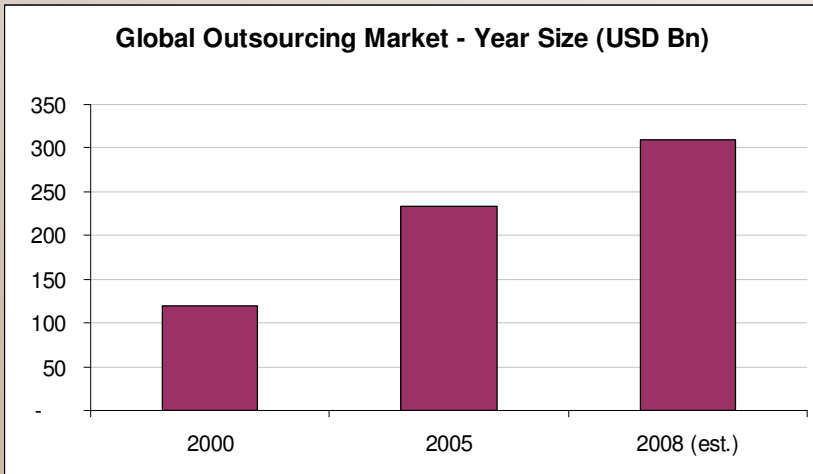


## *What functions are being outsourced?*

- Information Technology Outsourcing (ITO) was the original and still leads in terms of outsourcing.
- Business Process Outsourcing (BPO) has emerged as an effective sourcing strategy for organisations seeking to reduce their operating cost base while also improving service delivery and support for their customers, suppliers and employee.
- Knowledge Process Outsourcing (KPO) is the new wave. It is different from business processes in terms of the value proposition to the client, which leads to a clear demarcation in process complexity, the amount of intellectual intervention in the process, the skills required and the ability to scale.
  - While business processes are essentially process driven and rule based, knowledge processes involve judgment.

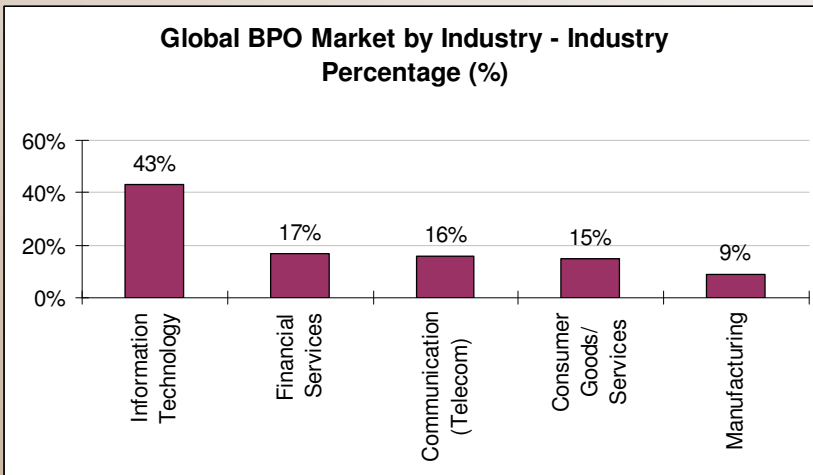
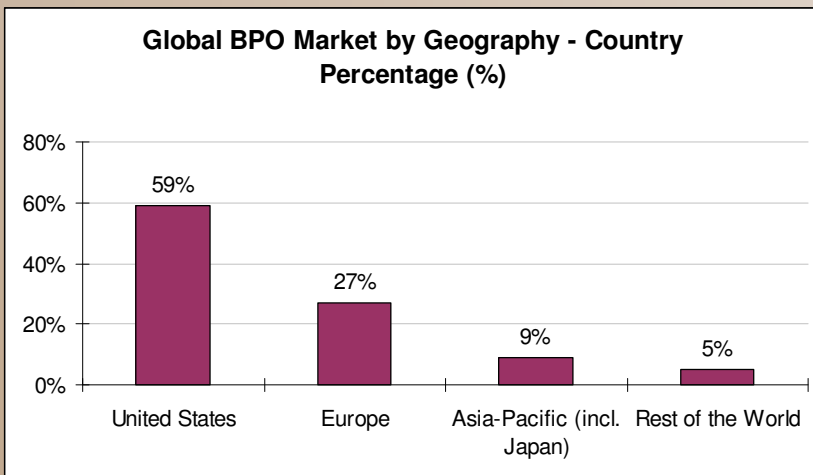


# Outsourcing market size?



The **potential** of the global **offshore** BPO market was around €120.7 billion in 2005 (McKinsey)

Gartner estimates that the worldwide offshore BPO market will grow to about € 19.3 billion by 2007



**Approx €100Bn growth potential** within the global offshore BPO market TODAY!



## *Why should you outsource?*

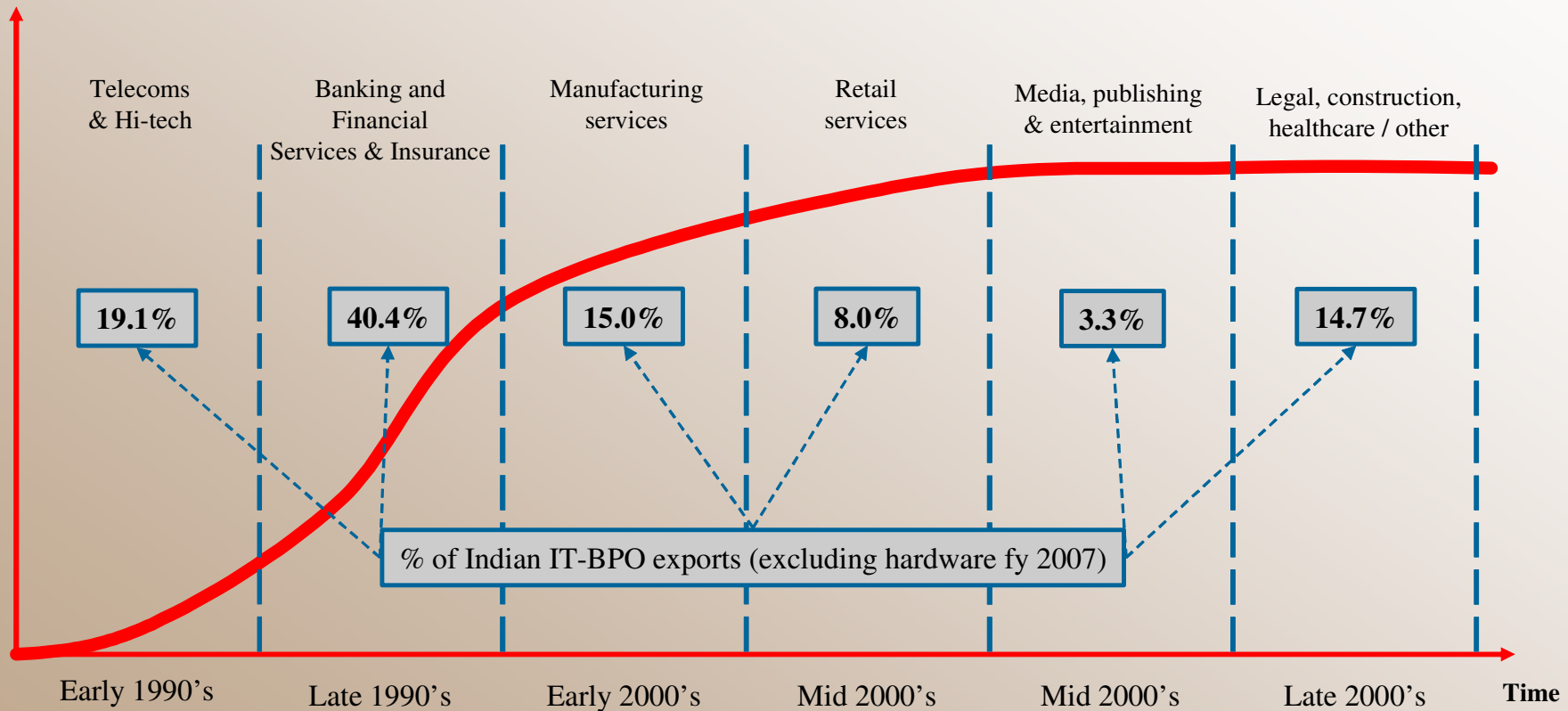
- Mounting margin pressure, global competition, and an increased focus on core business are driving companies like never before to look for new ways to get things done at a lower cost.
- While cost saving is a primary driver of outsourcing, companies benefit in other ways, including freeing up internal resources and accessing world-class skills and capabilities.
- Typical objectives desired from outsourcing include:
  - Improving strategic positioning through increased focus on core functions.
  - Improving competitiveness through operational performance improvements and access to cheaper and more specialist skills.
  - Increasing control through process improvement.
  - Reduction in costs through new technology or innovative practices.



# You're not alone

**60% of the Fortune 500 companies outsource to India  
– it is a proven business model!**

Adopters of outsourcing



Source: Nasscom Strategic Review 2008 and Op2i Ltd



## Where should you outsource to?

	Local	Near-shore	Off-shore (India)
Specialist skills	√√√	√√	√√√
Economies of scale	√√	√√	√√√
Access to large educated workforce	√	√	√√√
Labour arbitrage	√	√√	√√√
Favourable regulations	√√	√√	√√
Experience and maturity of suppliers	√√	√	√√√
Infrastructure	√√√	√√	√√
Cultural alignment	√√√	√√	√
Perception of risk	Low	Med	High

**Offshoring offers the greatest rewards from outsourcing, but the risk perception is also High**



## *Whom and how to outsource?*

- Captive Direct (many of the banks...)
  - Organisations create an organisation within India, often known as captive centers
  - Because captive centers require a sizeable upfront investment, only larger companies have the necessary resources to use this model.
  - Less risks to an organisation than any of the other models, because dedicated management from the parent company directly oversees the Indian operations.
- Joint Venture (e.g. BT and TechMahindra...)
  - A domestic firm partners with an Indian entity for shared control of the Indian operations.
  - In general, because control is shared with the foreign enterprise, this method of offshoring has a higher risk potential than the wholly owned foreign captive direct model, but less risk associated with it than the direct and indirect third-party contracting forms described below.



## *Whom and how to outsource?*

- Direct Third Party (many of the call centres...)
  - Firms outsource operations to a third party service provider located in India.
  - Because the outsourcer has no ownership authority in this form, their control over this working arrangement is limited to the contract terms agreed with the third party service provider, thereby making this model potentially more risky than either the captive or joint venture forms.
  - In some cases the outsourcing customer may elect a build, operate and transfer model, i.e. contracting for services with a third party with an option to acquire the services operation, at some point in time in the future.
- Indirect Third Party (using Op2i...)
  - A company enters into a contract with a domestic outsource service provider, who then subcontracts out all, or a part of the work, to an offshore company.
  - It is quite possible to have a relatively lower risk if the contract is between two domestic companies, as the usual issues of foreign law are not relevant for the outsourcer – essentially the indirect third party bears these risks.



## *Will outsourcing hamper innovation?*

- Maybe, maybe not – depends on nature of relationship and contract...



## *Why things go wrong?*

### **HARD**

- Lack of clear directive.
- Poor decision making.
- Poor project management.
- Low executive commitment.
- Inadequate skill proficiency and experience.
- Poor quality assurance and control.
- Stability of technical infrastructure.
- Inadequate contracts
- Poorly constructed SLAs

### **SOFT (and perception bias)**

- Unrealistic financial expectations.
- Anti-outsourcing sentiments.
- Conflicting communications styles.
- Mismanagement of their staff attrition.
- Misunderstanding regarding capital investment requirements.
- Lack of professionalism.
- Conflicting work-style, holiday schedules etc

**Similar to any Process Improvement / Change Management programme....**



# Practical Outsourcing



## *Which processes should you outsource?*

- The essential core of strategy is cross-functional or cross-activity integration.
  - The integration of the different competences of a firm together with the correctly managed processes, produce the products and services that are delivered to the customer
  - Processes are the backbone of the organisation - the glue that binds the organisation
- Processes are the least well managed asset in most companies - yet fundamentally affect how well strategy is executed.
  - Processes tend to be viewed as operational, disjointed, functions that evolve on an ad-hoc basis
- Process objectives should cascade from top-down, while performance measures should feed upwards towards the strategic aims.
  - Any process analysis or improvements projects should be viewed in the context of the overall organisational objectives

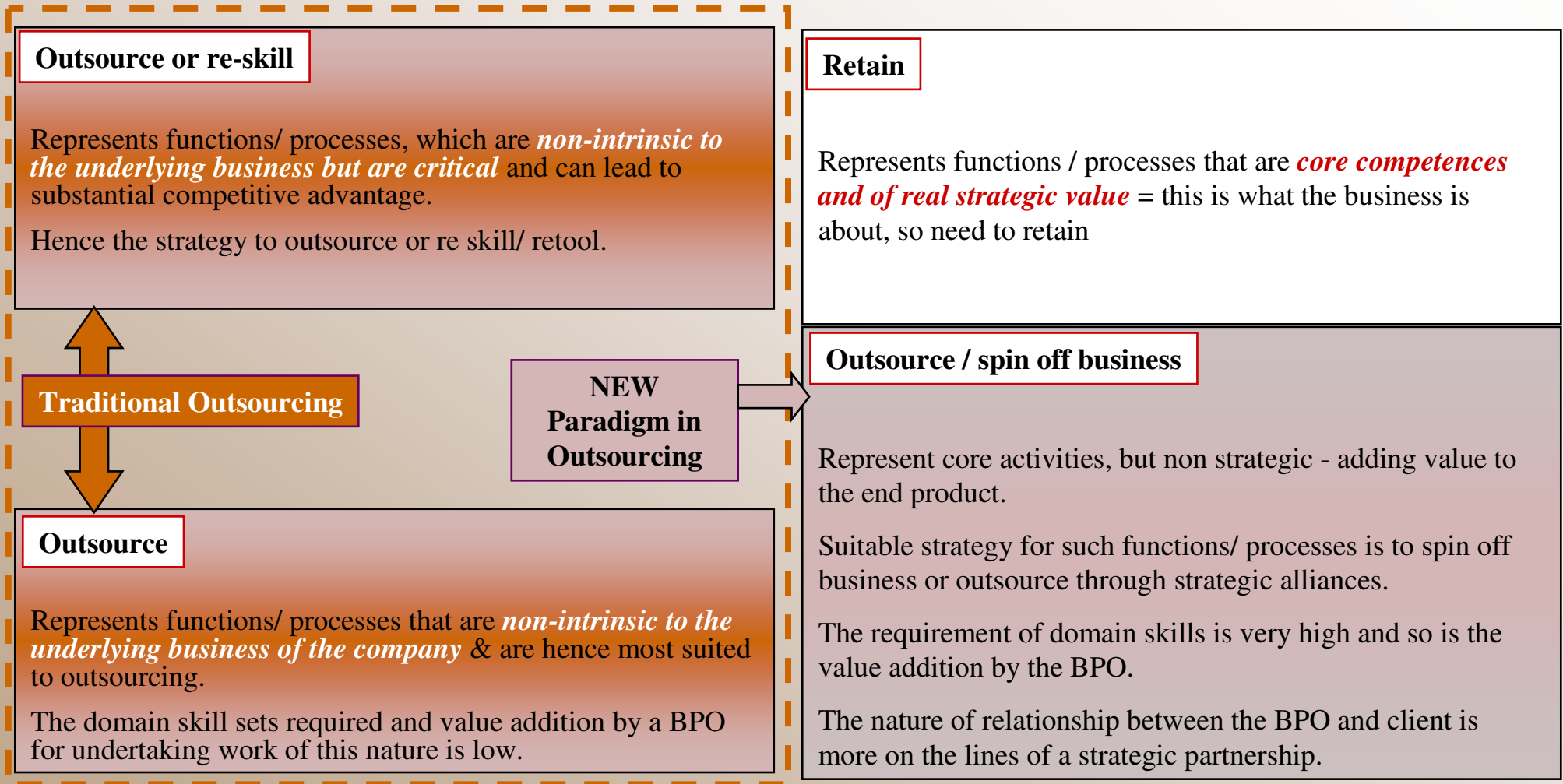


## *Traditional Vs new views on strategy*

- Traditional strategic thinking and analysis has centred on an “**outside-in**” perspective - essentially based on porter’s five forces model.
- Intensified competition, sustained globalisation and customer choice means this perspective no-longer has sustainable value.
- A **inside-out** perspective is now required which does not replace the traditional view, but complements it - new strategic view focuses on competences and capabilities – a resource based view.
  - Competences describe the resources themselves
  - Capabilities refer to the ability of the firm to deploy resources
- The successful competitive advantage of firms is not in its products but in their core competences.
- Competences represent a potential and therefore cannot contribute to competitiveness or performance unless they are successfully translated into new processes, products and services.
- Resource based view of strategy is beginning to develop into the “Knowledge based view of strategy”.



# Assessing what to outsource and what not to outsource?





**Any function / process which is not a core competence  
*and*  
of strategic importance  
can potentially be outsourced**



## *Outsourcing as a tool to business process improvement*

- Deductive improvements
  - Seeks to define current process
  - Process mapping by relationships between activities
  - Minor improvements – impact on end process may be minimal
- Inductive improvements
  - Business Process Re-engineering (BPR) is an extreme case of innovation
  - Re-conceptualisation as business processes
  - Focus on inputs and outputs
  - Central role and importance of IT
  - Wide-scale radical change and rapid implementation

*Outsourcing can be viewed as a business tool which brings about inductive improvement in business processes - quickly and cheaply*



## Contact us

*This Perspective has been written by Bharat Vagadia, CEO Op2i - a business improvement firm specialising in outsourcing.*

*Services offered include: advisory, training, project management, governance and arbitration services throughout the outsourcing lifecycle.*

*Bharat is a Board Director of the UK National Outsourcing Association (NOA) and an author of a leading book on outsourcing.*

*The views expressed in this Perspective reflect only the views of its author and not the NOA. Please contact Op2i for further information or support:*

*<http://www.op2i.com>*

*Email: [Bharat.Vagadia@Op2i.com](mailto:Bharat.Vagadia@Op2i.com)*

**Bharat Vagadia LLM, MBA, B-Eng, DipM**

CEO Op2i Ltd

Board Director: UK National Outsourcing Association

Author: Outsourcing to India - a legal handbook

Mob: +44 7711 898089

Fixed: +44 207 193 4339

Email: [Bharat.Vagadia@Op2i.com](mailto:Bharat.Vagadia@Op2i.com)