"12 Capabilities to evaluate in your Business Process Outsourcing Provider "

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Abstract

The Business Process Outsourcing (BPO) market is large and diverse, covering everything from the outsourcing of quite simple processes or call centers to, more recently, the transformation of entire back office functions of major corporations. The supplier base is equally diverse, stretching from locally based specialists in particular applications and/or industry sectors, through offshore providers who base their appeal on their ability to provide what may be well qualified staff at low unit labour costs, to 'transformational' outsourcers who apply a combination of sophisticated management techniques and technology investment to achieve new levels of process performance. Client organizations are challenged to identify a BPO provider whose capabilities are most appropriate to their needs.

In this article, we first identify three potentially critical areas of provider competency:

- Delivery Competency – defined as the extent to which the supplier is equipped to deliver service to specification on a sustainable basis
- Transformation Competency – defined as the scope of supplier ability to achieve radical improvements in the quality, cost, and functionality of the outsourced service
- Relationship Competency – defined as the ability (and willingness) of the supplier to work in true partnership with the client, with aligned incentives operating through the life of the contract

We then describe 12 capabilities which, based on our research experience, underpin the three target competencies. Each capability is illustrated by specific examples drawn from the outsourcing experiences of by firms such as BAE Systems, Lloyd's of London, Deutsche Bank, Bank of America.

Having first clarified which competencies are required to achieve their BPO goals, client organizations can evaluate potential BPO providers based on their demonstrable mastery of the capabilities relevant to achievement of those goals

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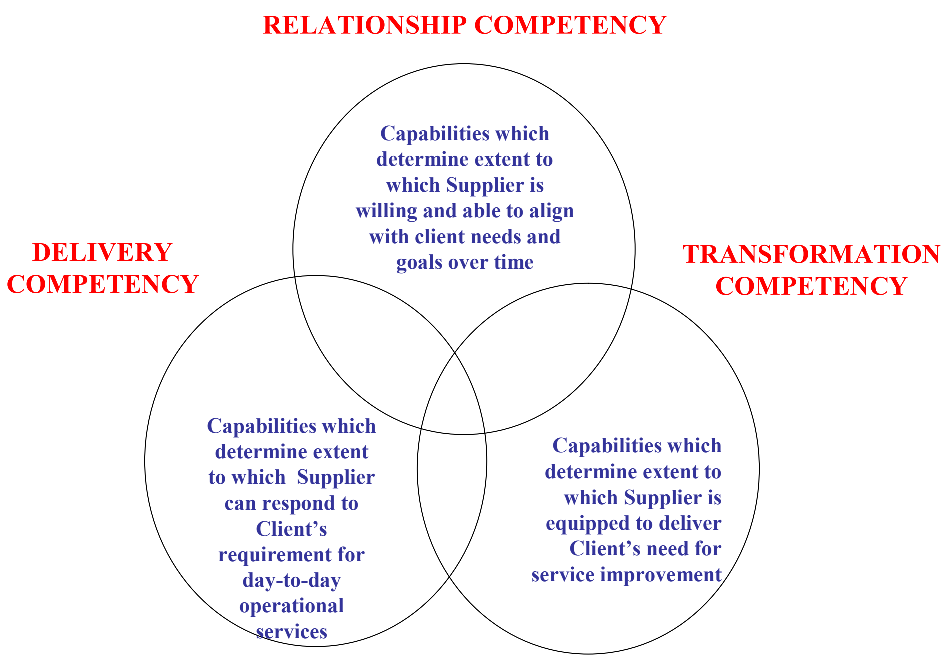
In our experience senior executives commonly express dissatisfaction with back office processes and functions in areas such as human resources, information technology, indirect procurement, finance, and accounting. They perceive them as costing too much, providing too little, and responding too slowly. At the extreme, some of our largest companies - having grown through a series of mergers and acquisitions - face a heritage of disparate and poorly performing processes across the back office step-children which can only be corrected by the application of very substantial investment dollars and scarce change management capacity. Their executives are conscious that the management attention and resource investment required will represent a diversion from what they see to be the more critical requirements of their 'core' business activities. And even if they agree to commit the resources, some doubt they can create the environment for back office success:

"If (back office) change was going to be achieved, it needed the injection of a catalyst by an outside party. Culturally it needed a kick up the backside." -- CEO, Lloyd's of London

Not surprisingly, rather than deal with the mess themselves many senior executives are now outsourcing back office processes – even entire global back offices – to the growing army of Business Process Outsourcing (BPO) providers. By now we are all familiar with the phenomenon of the back office service support call centre which has been outsourced – whether to a 'local' or to an 'offshore' provider. More recently a number of mega-deals have attracted headlines, such as the decisions by BP and Bank of America to outsource the transactional side of their HR activity to Exult[1]; and Accenture and others have introduced the phrase 'transformational outsourcing' to capture their proposition of radical change to client business processes.[2] The CEO of Lloyd's (quoted above) and the HR Director of BAE Systems both selected the UK-based supplier Xchanging as their partner. For BAE Systems, Xchanging financed the upfront investment to transform the company's decentralized HR--scattered across 70 sites--to a shared service utility, complete with a brand new building, new business processes, and new web-enabled technology. Xchanging inducted 462 BAE Systems transferees to a front-office culture, identified and defined 400 HR services for improvement, and delivered 10% cost savings to BAE in the first year. For Lloyd's of London, Xchanging financed a similar transformation for policy administration and claims processing. Beyond delivering cost savings and service improvements to Lloyd's, Xchanging also commercialized the services, sharing with Lloyd's the profits it gained from a growing number of external customers.

In short, BPO has not only become a very large and growing market; it is a diverse market populated by an ever increasing number of providers. Client organizations must look very carefully at the goals they are seeking to achieve, and be clear about the supplier capabilities which are required to achieve them. During the course of a 15 year research program – initially focused on IT outsourcing, but now extended to BPO (see sidebar 'About the Research') – we have previously described ways to analyze appropriate outsourcing goals; and provided a widely adopted model for identifying the capabilities which need to be retained in house by the client.[3] In this article we identify and describe the capabilities which BPO providers potentially bring to the outsourcing relationship. Finding a supplier who provides the capabilities appropriate to client goals is key to BPO success.

Three types of Competency the Supplier may bring



To greatly varying degrees, every BPO supplier possesses competency in three domains: delivery, transformation, and relationship.

- The most obvious and basic domain is that of **Delivery Competency**, which determines the extent to which a supplier is able to respond to the client's requirement for day-to-day operational services. What scope and complexity of services can this supplier sustainably provide? To what levels of cost, quality, robustness, flexibility? No matter what level of cost saving is on offer, the client is not going to outsource unless they are confident that their minimum required standards of service will be met during the life of the contract
- Increasingly clients have the expectation that outsourced services will in fact improve over time, providing some combination of cost/quality/functionality

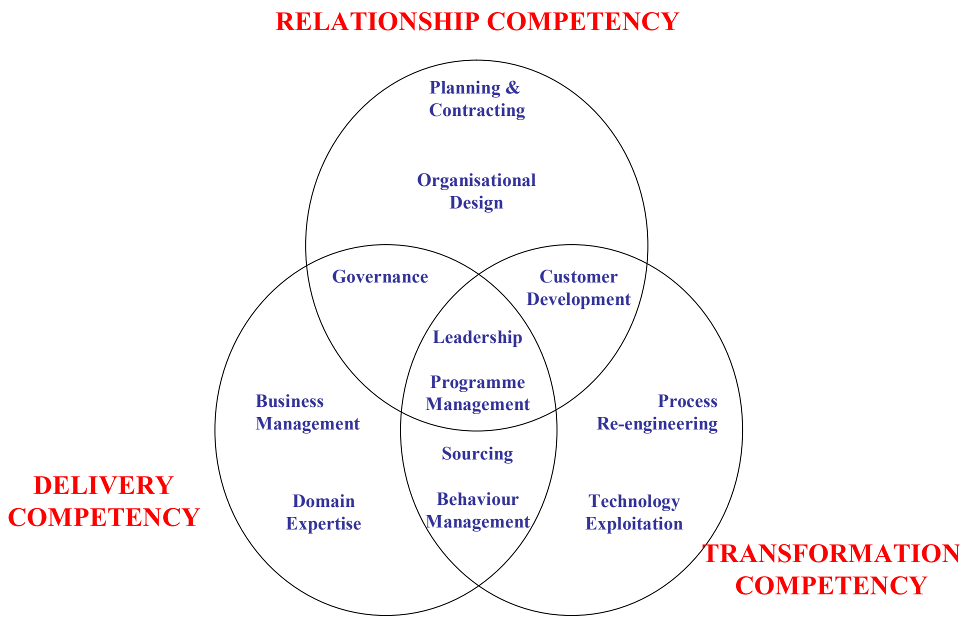
benefits. The **Transformational Competency** determines the extent to which the supplier is equipped to deliver on these formal or informal expectations. As we shall see there are several potential levers for achieving radical change and improvement, and suppliers may vary greatly in terms of which such capabilities they have convincingly mastered

- To date outsourcing has been dominated by so-called ‘fee-for-service’ contracts which separate the price which the client is obligated to pay for the service from the costs which the supplier incurs in providing it. It has become increasingly clear that this apparently straightforward arrangement can lead in practice to serious ill-will and difficulty, at least during lengthy (up to 10 year) contracts. At the outset of the relationship, the client has typically used bargaining power to obtain a very attractive price. However, bargaining power shifts post contract, and as change occurs in the business and hence its requirements – or in the factors which determine supplier costs, such as the labour market or technology – the supplier is often perceived to be taking full advantage. Many clients will therefore wish to give weight to the **Relationship Competency**, which determines the extent to which the supplier is willing and able to deliver the ‘Win/Win’ relationships that more successfully align client and supplier goals and incentives over time

Thinking about competencies in relation to outsourcing goals is the first step towards finding an appropriate supplier. Do we need a supplier whose delivery competency is geared to a ‘Cadillac’ level of service? Or will a ‘Chevrolet’ service be sufficient to meet the need? Is there clear evidence that the present service is ‘broken’ and in need of radical change through the supplier’s transformation competency? Or are we simply looking to transfer out a back office service that is already satisfactory in order to free up more management time to address ‘core’ activities? Are we looking for a services ‘vendor’ who can easily and quickly be substituted if performance is unsatisfactory? Or do considerations such as switching costs imply that we need a long term ‘partner’ whose business success is linked over time to our own? (A common mistake is to choose a ‘partner’ through a procurement process that encourages a bidding war; the resulting ‘winner’s curse’ leads to protracted hostilities as the chosen supplier seeks to restore profitability to an initially disastrous business model[4]).

The next challenge is to evaluate which suppliers possess the level of ability identified as appropriate to client need in each area of competency – and we encounter a second common mistake. When evaluating competencies client executives have a tendency to assess suppliers' *resources* such as physical facilities, technology, and workforce composition, rather than supplier *capabilities* to effectively manage and deploy these resources for the customer's benefit. For example, they ask for evidence of excellent supplier employees in the technology area because they have identified technology as a key driver of the transformation required in the service. This assessment does not distinguish between suppliers because all credible suppliers have excellent people. But a supplier who instills in its technology people a culture of 'rapid and regular delivery of benefits to the business', supported by a component based platform architecture, will deliver a very different experience to the client than the supplier whose approach bundles system requirements into large infrastructure projects. Evaluation of a particular supplier capability involves understanding the infrastructure, values and methodologies it brings to that area, as well as the processes it uses and the skills it has available. In the next section we identify the 12 capabilities we have found to underpin achievement of the 3 target competencies. Each is described in turn, and illustrated with examples that show capability at a high level - drawn from case studies of leading suppliers who are working with major corporate clients. The supplier capabilities model provides a tool to help clients evaluate potential providers, and may also help suppliers to assess themselves and their relative strengths versus the competition.

12 potential Supplier Capabilities



The capabilities we have identified through our research are labeled Domain Expertise, Business Management, Behavior Management, Sourcing, Technology Exploitation, Process Re-engineering, Customer Development, Planning and Contracting, Organization Design, Governance, Program Management, and Leadership. As shown in the diagram we have found that some capabilities support a single element of supplier competency, while others contribute to two or even three different domains. Each is of potential importance, depending on the competencies needed by the client.

1. Domain Expertise Capability

The first and most obvious capability to assess is Domain Expertise, defined as the ***supplier's capacity to apply and retain sufficient professional knowledge of***

***the target process domain to meet user requirements*.** Of course many supplier organizations acquire domain expertise through the employees transferred to them by their major clients - Deutsche Bank is moving its procurement people across to Accenture, Barclays transferred check-processing staff to Unisys, Exult and Xchanging gained HR domain expertise from employees transferred by Bank of America and BAE Systems respectively. This arrangement has two potential advantages from the client point of view: first, it becomes the supplier's rather than the client's responsibility to adjust capacity, eliminate poor performers, leverage the untapped potential of the best people; secondly both parties are assured that staff operating the service are familiar not only with the functional domain such as HR, they also understand the specifics and idiosyncrasies of the client's existing HR service. As the suppliers grow their own critical mass of expertise in the target domain and become more reluctant to accept more transferees, new clients will want to carefully consider the second point – does the supplier have the capability to apply domain expertise which fits their own specific context?

Other differences in client goals will impact the evaluation of Domain Expertise. For example a client seeking to build external capacity to cater for periodic variations in service demand will look for a supplier's commitment to build expertise specific to their own context. The client who seeks to take advantage of low labor costs through offshore outsourcing will want to ensure it retains its own critical mass of expertise:

"It has become very clear that in order for offshore to succeed, we need to groom, reward and retain our own subject matter experts. They are the ones with the greatest knowledge of the business units and the ones who are responsible for creating the statements of work. The developers in India don't understand and can't be expected to understand the core business functions" -- Senior Vice President, Fortune 500 Financial Services Company

2. Business Management Capability

The second fundamental requirement of any BPO arrangement is that the supplier possess the ***Business Management capability to consistently deliver against both customer service level agreements and its own required business plans***. Failure on one front will inevitably lead in time to failure on the other, but it seems that clients sometimes forget this. We have studied adversarial relationships where the clients focus on high priced items within the supplier's bundle of services and threaten to erode the supplier's margin by downsizing or eliminating these items. At the same time these clients fail to credit the supplier for other items in the bundle where unit prices are below external benchmarks of unit price. In successful relationships we find client and supplier business managers ensure frank discussions about the supplier's business returns as well as service performance:

'We have to sit with our agency department representatives and with EDS to make expectations reasonable. We get accused by the agencies, "Why are you siding with the supplier? You are supposed to be on our side." But you need to be even-

handed. Suppliers have to make a reasonable margin to stay in business. You don't want them to lose money because the worse their business gets, the worse your business gets.' –Client Contract Manager, Australian Public Sector organization

We saw a different example of business management in action – involving volume rather than pricing issues – in the BAE Systems procurement deal with Xchanging. During the first year of the deal it became clear to Xchanging that there was a major shortfall in the expected (£80 millions per annum) value of transactions being handled. The two parties worked hard over several months to identify additional categories of business which could be transferred to ensure that Xchanging could get back on track with its business plan, while providing the targeted savings to BAE Systems.

3. Behavior Management Capability

A common client objective when considering BPO is to seek qualitative as well as quantitative improvements in the outsourced service. Will staff transferred from their own under-appreciated 'Cinderella' back office function suffer further reduction in morale; or will they exhibit new behaviors as employees of a service provider business? Clients will want to evaluate the supplier's ***Behavior Management capability, the capacity to motivate and manage people to deliver service with a 'front office' culture.*** Of course all major suppliers – Accenture, EDS, IBM, CSC, Unisys, HP, CGI, ACS and their like – have employees to be proud of in terms of experience, skills and knowledge. Clients should also look for evidence that the relevant workforce will also be customer oriented, satisfied, and empowered. How do potential suppliers orient new employees to their culture? How do they reward and incent the desired behaviors?

At CGI there is a reorientation process for transferred employees called 'harmonization'; it begins before contracts are signed:

'CGI does harmonization to soften the blow caused by change to these employees. We take harmonization very seriously. We have a budget for this. We hold harmonization sessions, training, Q&A. This is much more than an orientation. We want to show every employee – not just a subset – this is what we do, how we do it, the timing. We want to set the stage beforehand for good behavior management, not react to bad behavior afterwards.' – Ed Standridge, CGI Partner

BAE Systems is one client who experienced the difference such a capability can make, after their HR transferees had been through Xchanging's four stage induction model:

'They have become a lot more professional. They have a lot more understanding of what drives a business. They understand the cost base and how you actually get value out of a business. It has been quite a nice surprise to see that happen, and happen so quickly.' – Kim Reid, Divisional HR Director, BAE Systems

4. Sourcing Capability
Another potentially critical contributor to meeting client goals may be the supplier's ***Sourcing Capability, the capacity to access whatever resources are required to deliver service targets***. Depending on the nature of the service – and on the level of need to 'transform' – the need may be for access to economies of scale, to lower unit labor costs, to scarce professional skills, to investment in superior infrastructure, or simply to supply management. The aforementioned deal for procurement services between BAE Systems and Xchanging was based on two of these: Xchanging's application to 'indirect' procurement categories of the high level of professional skills that BAE itself could only consistently attract to 'direct' categories; and the supplier's ability to access scale by aggregating BAE's needs in these categories with those of other clients.

ATT's wish to take advantage of the high skills and low costs of the IT sector in India provides a contrasting example. Rather than build one himself, the ATT CIO persuaded IBM to create a 'captive' IT service center in India. He was willing to trade off some costs savings in return for less risk – management and political risk. Today nearly 40% of ATT's application development work is done offshore through IBM's captive center – with reported cost savings to ATT of around 30%.

5. Technology Exploitation Capability
In our experience it is often readily accepted in companies that their back office processes are suffering from years of neglect, unable to compete with core processes for the technology investment that could transform the cost, quality, and functionality of the service. Furthermore top management may be all too aware of the consistently problematic record of technology based projects, particularly those which do not attract their own attention and active championship. Many clients are therefore strongly interested in a potential supplier's ***Technology Exploitation capability, the ability to swiftly and effectively deploy technology in support of critical service improvement targets***. As previously rehearsed, this is a capability that requires careful evaluation – looking beyond the pure technical skills which all major suppliers possess. What is the approach of the supplier in question? What values and behaviors do they bring to technology exploitation? What processes do they employ? What existing infrastructure do they use as a base?

As the likes of Exult and Xchanging have shown with their rapidly deployed 'e-enabled' HR services delivered to the desk top, an excellent supplier technology exploitation capability can enable 'surprise and delight'. Similarly Lloyd's of London in 2003 had the welcome experience of watching Xchanging win the 'Market Initiative of the Year' award for the claims convergence proram they had implemented within their contract; as well as being 'highly commended' in the 'e-business Initiative of the Year' category..

But technology is expensive and clients will want to be sure that it is the servant, not the master of the business. CGI's approach is to jointly develop with the client an annual technology plan which identifies mutually agreed investments and projects without the need to revisit the contract. Another supplier's less fortunate client complains:

'The suppliers take your architecture where their business is going, not where you want to go. Suppliers want vanilla, our customers want chocolate. We even have discussions on the supplier's standards. We want to run this security environment, not their security environment for their reasons.' – Client contract manager

6. Process Improvement Capability
Besides technology, the other prominent potential lever for service transformation is of course the supplier's ***Process Improvement Capability, the ability to design and implement changes to the service process to meet improvement targets***. For many major suppliers this is by now well established territory and – given the prominence gained by GE's corporate initiatives – most clients will be looking for Six Sigma methodologies or alternatives such as Capability Maturity Model processes. But again it will be important to look beyond the tools to consider the people and behavior aspects. In whom are the skills vested? Who owns the change process? Who defines what is an 'improvement'? And who benefits? We have seen too many examples – particularly in IT outsourcing – where improvements seem targeted at the convenience of the supplier rather than the benefit of the client and the service user.

7. Customer Development Capability
'When I became Accenture Partner responsible for the London Stock Exchange' recalls David Andrews (now CEO of Xchanging) 'I found I had 200 users who complained about everything. A critical task was to change their mindsets so that they became customers.' This quote goes to the heart of the supplier's ***Customer Development Capability, which transitions 'users' of an internally provided service to 'customers' who make informed choices about service level, functionality, and the costs they incur***. BPO arrangements are usually negotiated by senior client management, but experienced by business units and end-users who may not share the enthusiasm. It is in the client's long term interest to identify a supplier who can generate the user to customer transition. Our research suggests three key steps the supplier will need to take:

- Establishing personal contact and understanding of service use, the pre-cursors of trust and personal relationships
- Formal definition and communication of service required, with reporting of performance and capture of satisfaction over time
- Enactment of a business relationship in which the customer feels fully informed of service options, potential enhancements, and cost behaviors; and able to make choices to meet changing needs of the business over time

This might sound rather obvious but under the still dominant form of contract it is not easy to achieve. In a fee-for-service deal we typically find that the supplier sets out to provide a centrally specified service level and price package which often differs from that the user claims to have been receiving; and the supplier's management time is consumed by extensive (and central) negotiation over a long list of 'anomalies' which pre-contract due diligence had failed to identify. The net result is that, far from the establishment of trust, the user feels neglected and hard done by and relationships are off to a rocky start. In practice we find that customer development capability works best as part of a supplier relationship competency.

8. Planning and Contracting Capabiliy

Delivering such a relationship competency starts with the supplier's ***Planning and Contracting capability, its capacity to develop and contract for business plans which deliver 'win/win' results for customer and supplier over time*.** The planning component involves creation of a vision of the potential prize and how it can be achieved over time. The vision and plan must be open and shared. We recall the occasion when we were asked to facilitate a workshop between putative client/supplier partners. The breakthrough came when the supplier was at last persuaded to hesitatingly reveal the extent of his ambition for new revenues from the deal; to his surprise the client executive immediately affirmed that unless the supplier succeeded in achieving at least that level of success the partnership would have failed for the client company as well. By contrast, the recent deal between Deutsche Bank and Accenture for procurement services clearly identifies the vision, the rewards, and the plan for their achievement. Accenture is committed to fund and create a new platform for procurement, with 200 people assigned to the development; it expects to gain a substantial new revenue stream from Deutsche Bank and the further opportunity to attract other clients to the service. Deutsche Bank sees that the plan promises to deliver 15%-20% savings through consolidation, standardization, and re-tooling of its existing 14 procurement units. A plan for win/win.

The contracting component then defines how rewards will be shared as the plan is delivered. Many variations are possible: Bank of America chose to take an equity stake in its HR services supplier Exult, as well as a share of Exult's revenues from external clients[5]; Xchanging structures its major deals as profit sharing arrangements, with open book accounting. The essential principle is that the contract enshrines win/win results from a business plan that both parties are incented to pursue.

9. Organization Design Capability

Business plans are delivered through organization structures and processes. The next question is whether the supplier demonstrates the ***Organization Design capability needed to deliver the necessary resources, wherever and whenever they are needed to achieve the business plan***. We find that suppliers vary greatly in terms of their organizational approach, in the choices they make and the degrees of flexibility within that. For example, some emphasise a 'thin' front end client team which interfaces to the consolidated service units (silos) which have profit responsibility and ownership of most of the resources; all new client situations are migrated to this configuration. Clearly such arrangements – while they tap available economies of scale - may constrain ability to deliver the business plan for a specific client. At the other end of the spectrum, Xchanging allocates most of its resources to the 'Enterprise Partnership' units – essentially strategic business units – it creates for each new major deal. Each enterprise partnership has its own Chief Executive, its own full executive team, and its own core resources. It is responsible and accountable for delivery of the business plan.

The second issue in supplier organizational design concerns the resource allocation process. This is an area that clients with service transformation goals will need to evaluate particularly carefully. A potential supplier may be seen to have impressive capabilities in all of the areas of transformation leverage – sourcing, technology, process re-engineering. But the need for those capabilities will fluctuate considerably during the life of the contract. How 'well geared' is the supplier to be responsive to the needs of the client (and the shared business plan) as they change over time?

10. Governance Capability
The supplier's ***Governance Capability refers to the ability to define and agree, to track and assess, the performance of service over time***. It is likely that every supplier will point to some form of (jointly staffed) service review committee or Board. In the large relationship oriented deals - such as Accenture/Deutsche Bank, Xchanging/BAE Sytems – we also find a joint Board of Directors, which signals the expectation that the client is now an active partner in the enterprise.

The establishment of jointly staffed governance mechanisms makes a good start, but there are important follow-up questions. What reporting processes will be in place to ensure that each part of the governance structure is kept properly informed? What problem escalation procedures are defined? And what powers and sanctions are available through the governance structure?

In the past we have seen joint Boards of Directors lead to managerial schizophrenia[6]. What hat does a client executive wear when they sit on the Board of the service business? Should they be pressing for more services at lower cost to benefit their host organization? Or encouraging the service business to maximize external revenues when it might divert attention from their existing service needs? We see the existence of multiple joint Boards as helping to provide checks and balances in the midst of potentially competing objectives. For example the Insurance Services deal between Lloyd's of London (25% ownership), the International Underwriting Association (25%) and Xchanging (50%) has a joint Board of Directors which is focused on achieving revenue and (shared) profit growth for the 'Enterprise Partnership'. Xchanging has a majority on this Board to ensure operational control. But service quality is protected by the separate Service Review Board on which the clients have equal membership with Xchanging. A service problem escalated to this Board requires a remedial action plan which must be achieved in a maximum of three months. The Service Review Board has enforcement power through its ability to reduce prices. Its ultimate sanction for continual poor performance is the removal of the enterprise partnership CEO.

11. Program Management Capability

A basic assumption is that every BPO supplier needs a level of project management and change management capabilities in order to survive – every new contract implementation requires the execution of these capabilities. But clients whose goals extend to service transformation and long term relationship will need to look beyond these project level capabilities to evaluate the supplier's ***Program Management capability, the capacity to prioritize, coordinate, ready the organization, and deliver across a series of inter-related change projects.*** Directly or indirectly our previous paragraphs have pointed to the need for a multi-phased induction and re-culturing of transferees; to a parallel transitioning of end users into customer mindsets; to technology and process based projects which deliver a series of service improvements over time; to an overarching shared business plan to which all this must contribute. This is change at a level not for the faint hearted! Clearly it will involve methodologies and processes and high professional skills. But we suggest Clients will also want to look again for values and motivations within this supplier capability. Is the supplier so proud of its sophisticated Program Management apparatus that it risks operating a bureaucracy that inhibits achievement of business benefit imperatives? One very experienced practitioner of the art described it this way during our research:

'(Program Management) is guided by a healthy paradox. It blends the rigorous project management disciplines exemplified by world class consultants with the practicality and pragmatism that is only gained from running operations…It requires intellectual flexibility to vary or reverse a traditional approach according to circumstance…As a result there are no rules, only guidelines'

12. Leadership Capability

While governance creates structures and processes as a context for leadership, the supplier's ***Leadership capability is needed to identify, communicate, and deliver the balance of activities required to achieve present and future success – for both client and provider***. In management literature generally, individual leaders are regularly credited with a surprising degree of influence on the outcomes which their businesses achieve. The general phenomenon does seem to carry across into the specifics of leading the supplier's Client-facing team. After completing 76 case studies of customer-supplier relationships in IT outsourcing, we found that the individuals fulfilling supplier (and indeed client) leadership roles did have considerable impact on relationship success[7]. In 80% of all cases the supplier was either EDS, IBM, CSC, or Accenture. Although these firms were consistent in the way they contracted and governed across the case studies, 76% of deals were judged successful and 24% were not. The main differentiator between success and failure was seen to be the individuals who were leaders of the supplier (and client) account teams. If we look at how these leaders make a difference, we see three sorts of pattern:

- In unsuccessful cases, the 'leader' of the supplier team was often seen to be focusing on delivery – meeting contractual service levels while delivering required margin to the host supplier company. These issues are of course important, but we have identified them earlier as Business Management - not Leadership - capability
- The quality of the supplier leader's personal relationship with the client leader is usually a driver of the wider relationship between client and supplier organizations
- Least obviously but most importantly, we are finding that the quality of the relationship between the supplier leader assigned to the client and the top management at the supplier's headquarters is a critical factor in success. Because most suppliers create more of a front end team rather than a full function business unit to serve the client, the local team is very dependent on their leader's 'clout' with headquarters to access key resources and enact client-aligned business policies.

This recent example provides an appropriate finale to discussion of the leadership capability, and the 12 capabilities overall:

A large corporate client placed a $200 millions contract with supplier A. Supplier A assigned 'a great person' to lead the account team, but he had no clout with headquarters and could not get anything done. So the client broke the contract with supplier A and signed up with supplier B. Supplier B assigned to the account a leader with great street credentials gained from managing previous large contracts. But once again the leader had no influence with Head Office – in this case because he was a recent external hire. Eventually the client called Supplier B's CEO and said 'Send me someone who can act on your behalf'. The CEO assigned a person from Head Office, who took 18 of supplier B's best people with him to the client team. The contract has now been in effect one year and is considered a great success.

From Capabilities to Performance

The objective of this article is to provide a framework which helps client companies to evaluate which suppliers possess the competencies required to address their BPO requirements. We have explained and explored 3 supplier competencies, and the 12 supplier capabilities we find essential to their delivery. In discussing the capabilities we have tended to provide the 'richest' version we have so far encountered. But richness is not of course necessarily goodness; richness is available at a price that can only be justified against the potential to create value. Outsourcing of a simple and stable back office process with a cost reduction objective requires a level of delivery competency – and not much more.

Example: *for some years New York City has outsourced the digitization of its (paper based) parking tickets. In 2002 this contract was moved to Ghana, Africa, when the*

City administration identified that the incumbent company in India had become too expensive(!)[8]

But there is a sequel to the story. More recently New York has signed a contract with CGI's AMS division to manage the complete end-to-end parking violation process, now being transformed by the use of portable technology which captures details of offending vehicles on the spot. In other words, even the simple situation may become more complex over time. As experience of BPO increases, and confidence in its benefits grows, clients will more often be seeking sophisticated – and lasting – BPO relationships.

And of course choosing a 'capable' supplier is not enough to deliver performance. The research base that underpins this article suggests three imperatives for companies that wish to add value through use of the BPO services market:

- To identify the competencies they should be accessing in the BPO marketplace, client firms should think carefully about their likely future needs from any process to be outsourced. What role does this process play within the overall business model? Therefore what improvement goals for the process – cost, quality, functionality, flexibility – make most sense over time? And given the existing versus target status of the process, what combination of Delivery, Transformation, and Relationship competencies will be required. Our research experience has continued to confirm the 'selective' approach we first advocated in 1996[9], with the refinement that multiple relationships with a single supplier can be an effective approach.
- The decision to choose a particular supplier – or to extend the relationship with an existing one – should then be guided by thorough evaluation of relevant strengths in the 12 capabilities we have described. Capabilities, not skills and resources or brand name, determine the right choice.
- Last but not least, it will be essential for the client firm to stay involved in the action rather than step aside in the belief that 'now it is up to the supplier'. The level of involvement, and the extent and nature of client resources needed, will of course be another function of the context (see for example the model we provided for the IT domain in 1998[10]). Thinking about client-side dependencies for the successful execution of each supplier capability will provide at least one level of insight into what is required.

Outsourcing has been too often, in our experience, a case of 'Marry in haste, repent at leisure' As one senior executive of a major supplier observed: 'Outsourcing contracts are agreed in concept, but delivered in detail, and that's why they can break down'. Benchmarking the twelve supplier capabilities against strategic and operational intent is at the heart of effective practice.

Sidebar: About The Research

We have been researching outsourcing arrangements for many years, and.multiple research bases are drawn upon for this article. The first consists of 112 sourcing - mainly IT - case histories studied longitudinally from 1990-2001 (Lacity, Feeny and Willcocks, 1996, Kern and Willcocks, 2001, Lacity and Willcocks 2001). The second is a 2001-2004 longitudinal study of business process outsourcing practices, with a particular focus on four cases in aerospace and insurance (Lacity, Feeny and Willcocks, 2003 and Feeny, Willcocks and Lacity, 2003). We also draw upon a study of ten application service provision outsourcing arrangements (Kern, Lacity and Willcocks, 2003) and two studies of offshore outsourcing arrangements (Kumar and Willcocks, 1998, Lacity and Rottman, 2004). The approach in all cases has been to interview multiple stakeholders - senior business executives, functional leaders, and operational staff in both clients and vendors - and to review related internal documentation. For example, the on-going BPO study has conducted over 40 formal interviews to date and draws upon over 120 original documents, including contracts. We studied practices and progress over time, and assessed these against outcomes. Typically, outsourcing success was measured by comparing objectives against outcomes, cost savings (most deals demanded some degree of cost saving) and 'satisfaction' reported. The satisfaction measure varied with stakeholders from deal to deal but examples include service levels, end-customer opinion, speed of conflict resolution, innovation achieved, number of times penalty clauses invoked.

Further Reading

The following provide more detailed descriptions of the several research bases drawn upon:

Kern, T. and Willcocks, L. (2001) The Relationship Advantage: Information Technologies, Sourcing and Management. Oxford University Press, Oxford

Kern, T., Lacity, M. and Willcocks, L. (2002) Netsourcing. Prentice Hall, New Jersey.

Kumar, K. and Willcocks, L. (1999) Holiday Inn's Passage to India: A Country Too Far? In Karmel E. (ed.) Global Software Teams, Prentice Hall, New Jersey.

Lacity, M., Feeny, D. and Willcocks, L. (1996) The Value of Selective IT Sourcing. Sloan Management Review, 37, 3, 13-25.

Lacity, M. Feeny, D. and Willcocks, L. (2003) Transforming A Back-Office Function : Lessons From BAE Systems' Experience with an Enterprise Partnership. MISQ Executive, 2, 2, 86-103.

Feeny, D. Willcocks, L. and Lacity, M. (2003). Business Process Outsourcing: The Promise of The Enterprise Partnership Model. *Executive Briefing*, Templeton College, Oxford.

Lacity, M. and Rottman, J. (2004) Offshore Sourcing: Twenty Practices For Swift Learning, Risk Mitigation, Supplier Management, Cost Control and Quality Assurance. MISQ Executive, 3, 4 (forthcoming).

Lacity, M. and Willcocks, L. (2001) Global IT Outsourcing: In Search Of Business Advantage. Wiley, Chichester.

Endnotes

[1]See Adler, P., "Making the HR Outsourcing Decision," *Sloan Management Review***.** Vol. 45, 1, 2003; p. 53 for an account of Bank of America's outsourcing of HR activity to Exult (Exult announced an agreed merger with Hewitt Associates in June 2004). The Conference Board report 'Outsourcing HR in the Power Utilities and Energy Industry', Muson H. and Dell D., *Conference Board Research Report E-0006-04-RR*, has a broader discussion of theory and practice in HR Outsourcing

[2];For an introduction to the Transformational approach, see Linder, J., Cole, M., and Jacobson, A.; 'Business Transformation through Outsourcing'; *Strategy & Leadership* 2002, 30,4; and Linder, J., "Transformational Outsourcing," *Sloan Management Review*, Vol. 45, 2, 2004

[3] See for example Lacity, M., Willcocks, L., and Feeny, D. 'The Value of Selective IT Sourcing', *Sloan Management Review*, 37, 3, 1996; and Feeny, D. and Willcocks, L. "Core IS Capabilities for Exploiting IT" *Sloan Management Review*, 39, 3 , 1998 (listed as an SMR Classic)

[4] For definition and analysis of the 'winner's curse' phenomenon across 85 outsourcing contracts, see Kern, T. and Willcocks, l. and Van Heck, E. "The Winners Curse In IT Outsourcing: Strategies For Avoiding Relational Trauma," *California Management Review*, Vol. 44, 2, 2002, 47-69.

[5] Exult quickly won significant add-on contracts, including a $700 millions deal with Prudential Financial, and a $600 millions deal with International Paper. See Cagle M.L. and Campbell K., 'Taking HR from cost center to Revenue Generator at Bank of America'; presentation at the 2002 Outsourcing World Summit, Florida, February 2002

[6] For discussion see Lacity, M., Feeny, D., and Willcocks, L.; 'Transforming a back-office function: Lessons from BAE Systems experience of Enterprise Partnership'; MIS Quarterly Executive, V2 N2, 2003, pp.86-103

[7] Lacity, M., and Willcocks, L., *Global Information Technology Outsourcing: Search for Business Advantage;* Wiley, Chichester, 2001

[8] Reported in *Knowledge at Wharton*, 9th September 2002
[9] Lacity, M., Willcocks, L., and Feeny, D. 'The Value of Selective IT Sourcing', *Sloan Management Review*, 37, 3, 1996
[10] Feeny, D. and Willcocks, L. "Core IS Capabilities for Exploiting IT" *Sloan Management Review*, 39, 3 , 1998