

## ■ Outsourcing Risks And Rewards

Customer Interaction Solutions Magazine

John Bugh – President / North America

Intelenet Global Services

USA, July 2006

*The term business process outsourcing (BPO) evokes mixed reactions. Though it has been, and continues to be, a primary catalyst of globalization in today's business world, it has its share of critics who question both its validity and effectiveness. Nonetheless, outsourcing has grown exponentially over the years and is now a household term and a way of life for thousands of businesses worldwide.*

The concept of BPO started relatively small, with only very basic processes and functions such as inbound customer support and basic transaction processing being outsourced. But over the past decade, the functions being outsourced have become increasingly more complex and far-reaching, requiring global strategies, a wide range of talented people and innovative technology solutions.

Today's BPO market is a multibillion-dollar industry that continues to undergo rapid transformation on a global scale. Most of the world's leading companies have already — or are currently in the process of — adopting BPO as a strategic business solution, leading to dramatically increased spending across the board on a wide range of related services. As a result, the BPO industry is extremely diverse with multiple sub-sectors, each with its own unique characteristics.

According to Gartner, by 2007 the size of the global BPO market will be \$173 billion, of which more than \$24 billion will be outsourced to offshore contractors. Currently, the leading verticals in the BPO market are:

- Telecommunications;
- Technology;
- Financial services;
- Healthcare; and
- Energy.

In these verticals, the most commonly outsourced processes include internal auditing, payroll, human resources, benefits management, contact centers/customer care, payment/claims processing, real estate management and supply chain management. But despite the continued growth and potential of BPO outsourcing, many experts feel that it has certain risks. With this in mind, a review of the risks and rewards of BPO is warranted.

### The Risks

- *Loss of control:* Outsourcing key processes may result in the loss of direct managerial control of the process. Many managers suppose it is harder to manage the outsourcing

service provider as opposed to managing one's own employees internally. Although processes are customized to meet the specific needs of clients, discrepancies usually occur early in the business relationship between a BPO provider and the client.

- *Mitigating the risk:* The most effective way to maintain control of an outsourced process is to develop an ongoing communications plan and ensure a strong governance model. In some cases organizations have been known to place an employee onsite with the outsourcer to manage and oversee the process on a daily basis. This is particularly effective early in the relationship.
- *Security threats:* Although rare, an unfortunate reality is that outsourcing can threaten the security and confidentiality of a company's most sensitive data and processes. When a company outsources a highly confidential business process such as payroll, the outsource service provider will be in possession of sensitive information such as salary and social security numbers. It is a delicate process with daunting ramifications, and a company must fully evaluate each potential risk and benefit before deciding which business processes to outsource and/or retain in-house.
- *Mitigating the risk:* Scrutinize the provider's information technology infrastructure to ensure security, document expectations as they relate to sensitive customer information and protect against any breach with strong contractual provisions. In addition, there are a number of worldwide certifications designed to help protect both physical and data security. One of the most common is BS-7799, although BS-1500 is also quickly gaining momentum as the new worldwide standard.
- *Hidden costs:* Generally speaking, the potential hidden costs of outsourcing are not pre-calculated. These silent add-ons may include legal fees and time spent coordinating the contracts between two companies. Hidden fees conspire to reduce the allure of BPO by unexpectedly driving up costs, which is ironic, as cost savings are a major reason why companies outsource in the first place. The hidden and missed costs of outsourcing are hard to predict, which can cause overall costs to be underestimated.
- *Mitigating the risk:* Simple due diligence can go a long way toward minimizing hidden costs in advance. Many companies are providing the master services agreement (MSA) and statement of work (SOW) upfront in the request for proposal (RFP) process to minimize time and costs.

## The Rewards

- *Cost control:* As previously noted, outsourcing is seen by many as a major driver of globalization for many companies. At the same time, for most companies, it offers substantial cost savings. The economic benefits of outsourcing are real and significant. First, outsourcing reduces costs in three areas:
- *Implementation costs:* Client companies save time and money by leveraging the BPO provider's IT investments and professional expertise. Implementations are simplified and streamlined because configuration and customization options are typically limited to proven alternatives.

- **Operational cost:** Companies that internally manage their own processes can spend more than twice as much annually on maintenance and upgrades than those companies that outsource their functions. Such substantial cost savings are largely achieved through the ability of outsourcers to pass economies of scale and efficiencies of centralization on to their customers.
- **Reduction in technical staff:** Companies that manage their own technology typically have a dedicated technical staff — an expensive “black hole.” In contrast, companies that use outsourced technology platforms are often able to reduce their technical staff by nearly 50 percent.

These cost savings are available because outsourcers have developed excellent cost structures. Providers become experts at implementation, configuration, customization and operation of a given process. They integrate content only once and can then share that expertise with potentially hundreds of clients. They also offer highly flexible “standardized” process customizations, which can then be leveraged by multiple clients and can be implemented in minutes. In contrast, “unique” customizations in companies that do not outsource can often take months.

- **Increased efficiency:** Companies that outsource their business processes are often able to capture new efficiencies while simultaneously improving productivity. Again, they are in a better position to reallocate resources to other projects, helping their employees achieve greater efficiency and results in the process. In most cases, BPO providers bring in high-caliber subject-matter experts to design and manage the processes. These experts offer years of experience that many companies do not have access to or cannot afford on an ongoing basis. The end result is the development and adoption of well-defined business processes that allow for productivity improvement without compromising quality.
- **Reallocation of resources:** The more back-office functions that can be offloaded, the more effective the organization. An important facet of business process outsourcing is its ability to free top executives from some of their more mundane day-to-day process management responsibilities. On average, executives spend 80 percent of their time in the management of details and only 20 percent on formulating strategy. But when a business process is outsourced, this ratio can be easily reversed.

At the same time, outsourcing enables employees to assume greater responsibility within an organization. In particular, it often lets managers at all levels spend time saved on activities such as:

- Strategic planning;
- Measurements and analytics;
- Planning and budgeting;
- Work with line-managers to understand business needs; and
- Developing and evaluating new technologies and processes for even greater efficiency and effectiveness.

## **Incremental Value**

Business process outsourcing is particularly beneficial in that it directly influences shareholder value. BPO is all about optimizing business performance to create and maximize value where it did not previously exist. There has been a tremendous upsurge in BPO and related outsourcing industries in developing countries like India because of their ability to reduce costs while increasing quality of service. This has helped outsourcing companies and BPO service providers alike create enormous ROI for their shareholders and investors.

The above points give us an idea of the advantages associated with BPO. In addition, it helps expand global business relations while increasing foreign exchange for countries involved in the process. But there have been certain points that highlight the disadvantages associated with BPO as well.

Outsourcing is a trend that will continue to grow as global barriers to business fall. Increasingly complex solutions, integration initiatives, budget and staff constraints and the demand for diverse talent are among the many factors that will fuel the trend. Companies should consider outsourcing as part of the regular planning and budgeting process. When used under the right conditions, outsourcing can have near-term value to organizations and the clients they serve.