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Outsourcing Strategies in the High Tech Ecosystem

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Abstract

The high tech ecosystem has honed the sourcing of global capabilities and the serving of global markets to tremendous maturity in the last 40 years presenting customers the twin delights of standardized, globally available products with consistently improving features and falling prices. To the ecosystem, this has meant challenges to managing growth and delivering profits - achieved by developing an operating model based on sourcing discrete products and processes at the optimal quality, cost and level of service, globally. Supporting services such as BPO evolved in the late 70s to enable this model. While the BPO industry has reported a steady 10% Y-o-Y growth in the last decade, competitive provider growth and falling margins are leading some clients and analysts to predict pain in client organizations due to a shortfall in innovation in services outsourced. This PoV discusses why clients and providers need to collaboratively redefine value creation and fine-tune their outsourcing strategies to achieve the next level of business benefits through outsourcing.

Context setting:

Starting with payroll, accounting and customer service, BPO has now evolved to help semiconductor makers, component distributors, EMS, OEMs, SIs work together to source and assemble components, transport goods, sell and deliver products tailored to customer needs.

With low cost and offshore delivery having become the norm in outsourcing contracts and with more and more core processes being outsourced, Clients are looking closely at the overall value they believe outsourcing provides and asking fundamental questions of outsourcing providers:

1. Are providers able to understand the business context and customize services (E.g. Aligning fulfillment support processes such as material planning, expedite and vendor management to minimize working capital and manage obsolescence)
2. Are they able to manage risk and enable clients to "sleep peacefully at night" (E.g. Align supplier management processes to delivery and product failure risk)
3. Provide a true business case for outsourcing as SG&A and outsourcing costs do not continue a downward trend, in-house teams deliver better on meeting overall supply chain goals

On the other hand, providers too are grappling with key challenges:

1. Pressures on profitability driven by price-based competition limits the flexibility to hire top-tier talent, invest in solution development and meet advanced needs.
2. Partnering with clients and creating true business value: Process leadership, ability to create and sell commercial models that abstract value created by outsourcing from a larger client transformation program
3. Commercial, labor, infrastructure and environmental constraints to expand the global delivery model

Clearly, BPO providers and clients need to understand each other's positions, identify which BPO relationships are strategic and determine the future direction of outsourcing strategies for realizing business benefits.

Infosys View:

The market for BPO services has matured today from the focus on labor arbitrage and lowestprice provision of prices to a focus on a flexible, scalable capability to deliver enabling processes in various functional areas like F&A, Procurement, Order Management, HRO, Knowledge services and customer services. This capability will not only deliver BPO services to support the global operations of clients to optimize their SG&A and COS, but also open up opportunities to drive revenues. Several leading providers too understand client needs and would like to deliver transformational business value at an order of magnitude higher than the price of BPO services.

Infosys believes that an understanding of the unique characteristics of BPO services in high-tech will help design future models and outsourcing strategies

1. BPO is high-impact yet does not receive sufficient management attention
   BPO is inherently high-impact as it entails interface with internal and external customers globally, access to several internal systems of record and commerce and co-ordination across powerful internal functions in the client organization. This is in significant disproportion to the cost of BPO services which typically dictates the management attention conferred on it. The fact that BPO is delivered from locations remote from global HQ and does not one single owner within the client further contributes to this
2. Business functions in high-tech companies are globally dispersed and mature in the use of outsourcing and technology tools to deliver service
   Today a clients have sales offices in California, R&D centers in Raleigh and Bangalore, sourcing in Singapore and manufacturing in China in-house/outsourced in locations of lowest cost for that skill, using the latest technology tools to collaborate and access support services. Traditional labor arbitrage, change management or technology augmentation models need to be replaced by aggressive partnership models which deliver a committed business benefit

3. The same global delivery model is responsible for high costs of co-ordination and enhanced operational and financial risk
   Formerly routine functions such as establishing Available to promise from the factory and dispatching components to OEMs now require interface with multiple partners who may not have your world-class operational efficiencies. Eg: Fulfillment co-ordination and inventory management with 5 different contract manufacturers each with 20+ separately managed sites. This opens companies to significant risk in delivery schedule, product cost and failure.
4. Clients therefore still expect providers to provide stability in the form of stable workforce, continuity of service and "no-surprises". The high growth rate of the BPO provider industry compels providers to move in the opposite direction as the focus keeps shifting to the next higher level of offering.
5. Leadership in the outsourcing environment, while not yet a well-researched topic, can be said to emphasize attributes such as Ability to think across organizational boundaries to mix and match capabilities, sell outsourcing within the organization to senior management, offer alternative career paths to employees to dispel the fear of "job loss"

Infosys approach:

1) Focus on the basics

Requirements capture, definition of specifications, transition to new provider and service which delivers predictable, measurable output are the basic expectations from any service. Creating and meeting expectations in performing these activities is the origin of the disconnect between clients and providers today.

During a BPO outsource, such activities require specialist capabilities and yet should not be entirely delinked from BPO provider operations and handed over to 3rd party consultants. An in-house "Solution design" comprised of a mix of process consultants supported by a robust Discovery and Transition methodology brings in a disciplined approach to As-is process capture and operating model design through program management and toolset-driven rigor and sign-off based handover to Operations.

2) Predictable service delivery through Operations Excellence as the foundation of value creation

A hierarchy of expectations exist within client organizations with respect to outsourcing. Predictability of service delivery enabling clients to sleep peacefully at night is fundamental to securing acceptability and building comfort with business and executive stakeholders. Operations Excellence is the foundation of delivering this service predictability through a combination of self assessment, domain expertise, executive and operational dashboard, baselining of metrics and service levels. It is this service predictability that provides outsourcing champions credibility within their organization and the confidence to outsource higher-value tasks and provide entry to strategic programs. Operations Excellence therefore, is not merely a hygiene factor but also a key enabler of the journey to value creation. E.g. Infosys has created an Operations Excellence Management System (OEMS) based on industry standard workflow and MIS systems and aligned it to the balanced scorecard for all business units.

3) Leadership and Governance

Operations managers, process consultants and account managers in a provider operation service multiple stakeholders within the client organization, across functional departments. To translate the strong insight and relationships that result from this interaction into a partnership that delivers value in client business transformation, the provider needs to build strong client-facing competencies in middle management, incentivize provider account managers to cultivate "outsourcing champions" in client organizations, ensure that senior BPO executives such as CEO, Unit Heads network extensively and participate in formal reviews with Client business, sourcing and support function heads through a robust bottomup Governance and communication model. E.g. Infosys hosts atleast 3 personnel visits per account, recommends dedicated Account /Vendor managers based onsite, conducts a QBR (Quarterly Business Review) alternately at client and provider locations where middle and senior management from both entities participate. In turn, clients are setting up dedicated Client Advocates/PMOs comprised of sourcing and business leaders to drive all BPO initiatives, promote a culture of outsourcing and motivate in-house and outsourced teams to collaboratively work on operational excellence and innovation.

4) Innovative operating models to minimize operational and financial risk

Many branded equipment and product makers with distributed supply and demand chains are concerned about the impact of their operating model on their ability to predict demand, deliver products on time, cost and quality and retain a unique competitive advantage. Under the present model, this would demand a very high cost of co-ordination. BPO providers with experience working across the value chain with entities that buy and sell from each other can join client supply chain transformation programs. Process analysts can leverage the rich transaction data flowing across the sourcing, MRP, ERP systems and interface with suppliers, manufacturing, sales ordering and distribution functions to drive behavior by expediting shipments and update of fulfillment status information, follow-up with logistics and distribution service providers and form rapid response teams to troubleshoot operational glitches. Eg: Cross-functional teams working across a technology OEM and its distributor identified the root cause of critical sales orders going on hold to be an error in purchase order format used and freed up working capital.

5) Transformation through process leadership and deep domain knowledge

BPO providers, much like EMS providers, provide infrastructure and processing services to a range of industry sectors and have developed strong capabilities and best practices through servicing a wide variety of requirements. Clients can get to world-class in these processes by funding process leadership programs, connecting BPO providers to leading technology tool companies for product development and instituting specialized knowledge in provider SME teams through secondment. In many cases, this may lay the foundation for a go-to-market strategy based on a joint product offering. E.g.: SMB(Small and medium business) process and system platform for several software vendor and retailer clients of a large technology distributor.

6) Creation of commercial models to create, measure and share value

Traditional sourcing models based on creation of a BPO work team dedicated to the account and charged on effort-basis (per FTE man-year) were relevant in a context where transparent collaboration was required to establish the offshore outsourcing model. Client sourcing teams now employ this model for tactical functions with predictable demand, using reverse auction mechanisms for price discovery. For strategic functions, the emphasis has shifted to aligning the cost of receiving BPO services to the service used (utility model) and the business outcome (benefits model). Price discovery is effected through adoption of tiered transaction pricing, gain-share agreements based on committed reductions in effort reduction, processing time and critical errors.

Supplier discovery now consists of Proof-of-concept demonstrations of process performance, supplier governance models, account business models and technology implementations evaluated through a structure scorecard.

Providers have redefined and aligned their operating metrics and processes to client business metrics, instead of the earlier focus on meeting SLAs which are typically after-the-fact measures of mean performance. This alignment of metrics enables providers to understand what inputs in resourcing, methodology and technology contribute to desired outputs - driving measures as diverse as performance-linked pay, high-performer retention management, SaaS(software as a service) implementations, creation of compliance/ analytics offerings in spend, process management, transaction management and financial planning. BPO providers have then rolled up these service offerings into contractual commitments by making tool and people investments, accepted operating risk from the client business so as to deliver benefits like reducing client spend on indirect materials by 5%, reduced unapplied cash by 3% etc. This is very similar to the kind of bottom-line commitments that partners for core offerings like component suppliers and distributors make today and will culminate in BPO service providers no longer being confined to the back-office in high-tech.

In summary, the future points to one of renewed commitment in partnership between High-tech companies and their BPO providers. This could well be one of the critical organizational strategies to weather the imminent slowdown in the US economy in 2008.

Footnote:

Infosys BPO is one of the pioneers in taking BPO to a global delivery model managing ~$30 bn of customer orders, sourcing ~$5 bn of inventory and supporting ~100 product lines for 9 high-tech clients with a combined revenue base of ~$100 bn.

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