IS GOOD ENOUGH REALLY GOOD ENOUGH?

The Great Talent Paradox in Outsourcing

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Executive Summary

People, Process, and Technology—we all know the key levers for business transformation. And we all claim that the people dimension is the most enduring source of competitive advantage. So why does talent so often get the short end of the stick, so to speak, when it comes to establishing and managing outsourcing relationships? Why is talent treated as the most fungible element in a skills-based industry?

Shedding new light on this “talent paradox” is the focus of new research from HfS, which confirms that outsourcing initiatives only deliver sustainable value when enterprises and their outsourcing providers invest in developing the talent that actually fuels the performance of their outsourced functions and processes.

The consequences are clear. Our findings show that fully two-thirds of enterprise outsourcing buyers are struggling to achieve any genuine business value beyond mere cost reduction and efficiency.

Our research points to shocking shortfalls in the investments that enterprises are willing to make in the talent charged with managing outsourcing relationships and executing the processes and functions that serve the customers. The sad truth is that too many buyers believe “good enough is good enough” and that people are fungible; however, soon that won’t be good enough for ambitious enterprises.

Companies are surprisingly insecure about the quality of their talent. Barely a third of enterprise outsourcing buyers (i.e., customers) believe their current governance talent—the people responsible for managing the service relationship—can drive innovation, define business outcomes, or believe that they have even above-average analytical skills.

In fact, this shouldn’t come as much of a surprise. After all, you get what you pay for. Barely one in four enterprise buyers make formal investments in training and developing their outsourcing management staff in areas that are strategic to their business.
Providers are performing somewhat better and are far more likely than buyers to invest in developing their talent. Yet only about half have established formal training programs to develop industry expertise and skills in analytics and relationship management. More worryingly, only 60 percent of providers invest in “bread and butter” capabilities such as transition management and continuous improvement.

The result is a paradox in the industry’s approach to talent. Even as outsourcing moves from the back office to the middle and front offices, where value creation is paramount, and even though governance executives declare they want to achieve more than just cost reduction, they are not making the investments at the key leverage points in value creation—the people.

Our new research, based on a survey of 282 major enterprises engaged in outsourcing and qualitative interviews with many buyers and providers, confirms that governance leaders must shift their focus toward the development of their own staff and ensure they are engaging on an equal basis with the capable talent presented by their outsourcing service providers. Moreover, providers must raise their game in talent development to meet their clients’ expectations. This report investigates why many of today’s leading enterprises are trapped in a talent paradox—affirming the importance of people on the one hand and, on the other, failing to provide the support and resources necessary to transform talent into competitive advantage. This report also suggests steps governance leaders can take to break out of the paradox and manage their outsourcing relationships for strategic and sustainable value.
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Key Study Findings

Why we have a major paradox with outsourcing talent strategies

In many cases, executives are not putting their money where their mouth is when it comes to talent. On the one hand, they seem to be aware of the importance of strategic skills to outsourcing success. Our research shows that among the top five objectives of today’s enterprises are two highly strategic business skills: defining business objectives beyond cost reduction and efficiency (83% regarded this as either critical or important) and influencing executives (77%). Moreover, the five business objectives that enterprises believe have increased most in importance are all strategic skills and include improving analytics (32% regarded this as more important), defining business outcomes beyond cost and efficiency (28% more important), raising the bar for existing SLAs (28% more important), driving innovation (28% more important), and defining and adding new in-scope processes (25% more important).

Despite the increasing importance of such strategic skills, however, executives acknowledge that their current skill levels are deficient in these areas. When asked to evaluate their enterprises’ talent in fifteen skill areas, outsourcing executives scored all their capabilities as barely above average. Strategic skills such as external benchmarking, driving innovation, improving analytics, and defining business outcomes beyond cost and efficiency ranked last. Less impressively, tactical skills such as contract negotiation and adding additional volumes to existing services were ranked as those where their talent performed best.

As engagements mature, the need for more strategic skills quickly becomes apparent, yet enterprises acknowledge that existing skill levels are extremely immature.

Part of the problem, explored more in the next section, is that despite this acknowledgement of the increasingly critical nature of strategic skills, investments in talent are not following. Indeed, existing teams continue to focus predominantly on tactical rather than strategic outsourcing objectives. One might expect enterprises to become more strategic as time goes on, but the data show this is rarely the case. At the onset of their outsourcing initiatives, four of the five most important objectives for enterprise outsourcing executives were purely tactical, including managing transitions (67% regarded this as either critical or important), managing service-level performance (63%), selecting service providers (62%), and negotiating contracts (60%).

Moreover, when asked about their current objectives, today’s outsourcing executives still feel tactical objectives are actually more vital than strategic objectives. Three of the top five current tactical business objectives show an increase in importance, namely managing transitions (80%), managing service level performance (79%), and negotiating contracts (79%).

Enterprises have great difficulty recruiting and developing talent with strategic skills and capabilities.
Across the board, all enterprises found recruiting outsourcing-related management skills more difficult than recruiting for other skills. Strategic skills such as driving innovation, defining business outcomes beyond cost and efficiency, and influencing executives all ranked among the most difficult skills to recruit.

More tellingly, few enterprises have formal training programs in critical strategic skill areas, such as continuous improvement (45%) and improving analytics (26%).

Outsourcing executives consistently rated their own talent superior to their service providers’ talent, which suggests that executives perceive their service providers as lacking the skills needed to assist them. In fact, some service providers are often blind to the shortfalls of their own talent. Despite the assessments of enterprise outsourcing customers, service providers rate their talent superior to their clients’ talent in every area. Moreover, service providers believe they have better strategic skills, including the ability to drive innovation (19% ranked their own talent better than that of the outsourcing customer) and defining business outcomes beyond cost and efficiency (12% better). There is a clear miscommunication between many providers and their customers on the talent issue, which can easily be resolved if talent performance and quality were higher in the agenda than meeting metrics and pre-defined service levels.

When service providers are selected and leveraged for their strategic skills, the results can be impressive. Interviews with leading enterprises show that not every buyer ignores the importance of talent. Successful firms develop new competency models for governance and business leaders that emphasize relationship management, collaboration, executive-influencing skills, which reflect the need to rely on and partner with service providers more. They view strategic talent as more important than operational talent in their selection processes. They revamp expectations for their retained team to ensure they have the skills to focus on business issues. In addition, they continuously set new goals that push existing talent to improve more.

In short, outsourcing is at an inflexion point. CEOs know that their enterprise’s talent pool creates a competitive advantage. Moreover, successful analysis, innovation, and business transformation hinge upon strategic skills. Outsourcing relationships can—and in fact must—operate as a collaborative extension of an enterprise’s talent pool, with both parties focused on developing the skills needed to drive higher levels of business value from the
relationship. Exhibit 1 sums up the challenges and opportunities facing enterprise leaders regarding their outsourcing talent:

**Exhibit 1: Today’s talent management challenges and opportunities with outsourcing**

**The Challenges – Today’s Outsourcing Talent Shortfall**
- Enterprise outsourcing executives are dissatisfied with internal career opportunities, with many lacking career direction and having poorly-defined roles.
- Strategic and analytical skills are enterprises’ weakest talent capabilities.
- Recruiting strategic talent has become difficult.
- Development programs for key skills areas are immature.
- Many service providers need to provide better staff development programs.
- Many service providers are struggling to attract the talent clients need to create value.

**The Collaborative Outsourcing Opportunity – Leveraging Each Other’s Strengths**
- Enterprises should be continually inspired and challenged by their service providers’ talent and capabilities.
- Quality service providers should make real investments in talent to help their ambitious clients beyond the “old world” cost-arbitrage outsourcing model to one that is delivering value based on current business objectives and outcomes.
- Quality service providers should help provide direction and focus to their clients’ roles and career direction.
- Service providers should be qualified and empowered to support key strategic areas and not relegated to producing transactional low-value work.
- Outsourcing relationships should constantly be challenged by both the enterprise’s client and provider to evolve the combined business goals and desired outcomes. The ”status quo” is no longer an option.

*Source: HfS Research, 2013*
Two-thirds of outsourcing relationships are leaving a great deal of value on the table

Our research shows that too many outsourcing engagements (two-thirds) deliver little business value beyond “operational” delivery, meaning that the combined enterprise/provider team is not enhancing its capabilities to access and interpret data, improve processes, or work together on a strategic, regularly evaluated performance agenda to plan and improve the business. Consequently, HfS classifies outsourcing customers into three fairly evenly distributed camps based on their differing attitudes to their relationship with their outsourcing service provider:

#1: THE “LIGHTS-ON OUTSOURCING” CAMP - These enterprises’ main goal is to drive out expense without any costly disasters occurring. They see little, if any, strategic value in the outsourcing of processes and, therefore, little strategic value in the people performing those processes. If the talent is not strategic, why invest? As long as it is cheaper to have someone else run the process or function without disrupting their business, then they are content with that outcome. Typically, these enterprises will establish a small “no noise” governance team that causes corporate leadership management few headaches, manages to the SLAs, and succeeds in “keeping the lights on.”

Most of these corporate leaders do not want to hear about problems or additional investment requirements of any kind, especially those concerning talent management. To them, outsourcing is “handle-turning”; they will revisit the engagement when the renewal is up to see if they can squeeze a few more dollars out of the provider, but the goals, metrics, and service levels have been set—and as long as they are being met, victory can be declared. If the shareholders are happy with the immediate returns, nothing needs to change, including their outsourcing engagements.

#2: THE “EFFICIENT OUTSOURCING” CAMP - These enterprises often struggle to see the potential for competitive differentiation in their outsourced processes. They are happy they saved that initial 30% or so from the initial outsourcing phases but see they have hit a wall. They recognize that they can achieve more value if they develop a management program to facilitate continuous improvement and efficiency gains. Many enterprises in this category plan for phased process improvement and continually evaluate additional processes to externalize in the future.

These companies are not yet investing in improving the skills of those running the outsourced processes, but they do see they need help in specific areas. For example, in many cases, these enterprises will engage with Six-Sigma black belts to oversee a multi-year cost-efficiency plan—either from their current service provider or with assistance from an external management consulting firm. For example, some of these enterprises will take 20% savings immediately and reinvest 10% to supplement or develop their internal investments to ensure that further efficiency gains will be made further down the road.

#3: THE “STRATEGIC OUTSOURCING” CAMP - These enterprises tend to be experienced with outsourcing. They have learned that simply moving work offshore is only a short-term cost reduction measure and that these costs will eventually reappear if only an onshore-to-offshore staff exchange occurs with some basic process
transfer. They have learned that, once processes have been moved into either their own shared service center or into the hands of a third-party provider, if they fail to invest in process improvement, the performance of the business function itself will stagnate.

They have also learned that outsourcing as much work as some providers and outsourcing advisors tell them they can is not always going to be the best answer. They focus instead on outsourcing those processes that make sense and on working with the provider to inject their ideas and capabilities into improving overall business performances.

Moreover, enterprises in the strategic camp are intent on having their provider’s talent understand their institutional processes and issues, no matter how broken they may be. They ask their provider’s staff to understand how to help define and improve business outcomes based on the combination of their in-house teams, their shared services personnel, and processes externalized to third parties.

Additionally, these enterprises have realized that outsourcing engagements exist in a dynamic business environment and that whatever goals and performance metrics may have been established at the onset of an outsourcing engagement, they are unlikely to be entirely appropriate or relevant in two, three, or four years’ time. They know that performance metrics need to be revisited at least once a year and evaluated against the strategic goals and objectives of the business.

This perspective then leads to a very different approach to talent development. With this kind of strategic outsourcing relationship, talent needs to be managed strategically as well. They see the outsourcing people and the retained organization as a team of employees who are developed and regularly evaluated. The team’s joint goals are regularly set and monitored, and performance is evaluated against the real business objectives of today, as opposed to some period in years past when the original deal was signed.

Exhibit 2 depicts this talent evolution that many enterprises must address in order to move from the “old-world” legacy of the outsourcing relationship to a collaborative approach that is proving to bring much more value to the enterprise:
Breaking Out of the Paradox: Shifting the Outsourcing Focus from Cost to Value

Most enterprises are relatively new to outsourcing. Significant business process outsourcing (BPO) engagements have barely been in existence on a large scale for more than a decade, and IT outsourcing (ITO) only started to be adopted by the enterprise mainstream in the 1990s and early 2000s. Most enterprises today are only just waking up to the reality that outsourcing is much more than a transactional contract—it is an ongoing partnership that requires leadership, insight, and collaboration between an enterprise customer and its outsourcing service provider.

For the last decade, a “cost at all cost” mindset has frequently dominated the outsourcing strategies of many enterprises. As our research shows, one-time tactical objectives, such as selection, negotiation, transition, and execution, were the cornerstone of outsourcing initiatives as they got off the ground (see Exhibit 3).
Exhibit 3: Importance of initial business objectives at the commencement of outsourcing initiatives

- Managing Transitions
- SLA Performance Management
- Service Provider Selection
- Influencing Executives
- Contract Negotiation
- Managing Financial Business Cases
- Defining Business Outcomes Beyond Cost Reduction
- Driving Innovation
- Improving Service Provider Relationships
- Adding Addition Volumes to Existing Services
- Improving Analytics
- Defining and Adding New In-Scope Processes
- Improving Industry Acumen
- Raising the Bar for Existing SLAs
- External Benchmarking

Source: HfS Research 2013, N = 282 Buy-side Executives

Not surprisingly, outsourcing as a discipline has developed along the lines of this tactical emphasis. Experienced outsourcing governance executives documented transition methodologies, developed contract templates, and hired staff with the skills to negotiate and manage complex and highly detailed service-level agreements. Operations executives’ and procurement professionals’ skills became stronger, and outsourcing-specific centers of excellence sprouted-up in nearly every enterprise. On the periphery, boutique outsourcing advisors, specialized teams of lawyers, and professional development associations grew to support governance teams with these tactical objectives. The lesson is rather stark: Much of today’s outsourcing industry has, in fact, grown up around yesterday’s objectives.

That fact has critical ramifications for skills. The skills that were needed at the onset of an outsourcing engagement have to be continually revisited.

If you focus only on doing what you’ve always done, you’ll only hire people to do what you’ve always done slightly better instead of revisiting capability models and matching them to new strategic objectives and opportunities.
Developing initial cost goals and performance metrics only move enterprises to the next phase in their evolution. These goals and metrics must be continually evaluated and measured as the needs of a business evolve. For example, if an engagement was initiated in 2009, the economic outlook was a lot gloomier than it is at the beginning of 2013. Many enterprises are looking at more aggressive growth strategies today as opposed to the cost-containment focus that dominated the recent recession years.

Based on their experience, training, and recruitment strategies, some providers have resources and talent that can help support a growth strategy, but are customers aware that their providers have those skills? Are providers being forceful about developing and offering additional capabilities that could help their client? For example, the service provider could be engaged to provide skills that can help the enterprise understand risk models for moving into new markets or regulatory challenges brought about by Wall Street reforms. However, if the enterprise governance team is trained only in monitoring budgets and assigning penalties, it is unlikely much of this potential value will ever be unlocked.

Why Talent is Poorly Aligned with the Objectives of Today’s Outsourcing Relationships

As discussed, too many enterprise outsourcing relationships today are focused on solving yesterday’s challenges—namely, driving out labor costs, mitigating risks, and achieving a basic level of operational performance. These are now “table stakes”—or should be—for any serious enterprise customer or provider. However, if your talent pool is hired and developed only to perform against those objectives, how exactly do you expect to rise to the next level of performance?

How different are today’s business objectives compared to yesterday’s? Due to global expansion, dramatic regulatory makeovers, and a tougher competitive climate, the objectives are often markedly different. Our research shows that strategic outsourcing objectives, such as defining business outcomes beyond cost reduction, developing compelling solutions, and driving innovation and improving analytics, are quickly increasing in importance when compared to the tactical objectives established when the engagements were initiated.

As shown in Exhibit 4, four objectives have increased most in importance as outsourcing has matured into a strategic management practice: improving analytics, driving innovation, defining business outcomes beyond cost reduction, and improving SLA performance expectations. Equally notable is the increased importance in influencing executives, which is crucial when such a large proportion of business leaders need educating regarding the benefits and challenges of outsourcing.
Exhibit 4: Strategic objectives are becoming much more important to enterprises after commencing their outsourcing initiatives

Exhibit 5: Enterprises assess their own strategic talent capabilities as their weakest skills. Moreover, the top four business objectives that have increased in importance fall into their bottom six weakest skill areas.

Source: HfS Research 2013, n = 282 Enterprise Buy-side Executives

The increasingly important business objectives outlined in Exhibit 4 require new and very specific skills and capabilities from the operations team. However, as Exhibit 5 shows, enterprises assess their own strategic talent capabilities as their weakest skills. Moreover, the top four business objectives that have increased in importance fall into their bottom six weakest skill areas.
Exhibit 5: Enterprise’s self-assessment of their talent

Current staffing priorities reflect this talent deficit. The research illustrates that too many enterprises’ outsourcing governance teams are comprised largely of procurement professionals, contract negotiators, and project executives who are not being re-skilled to shift their current focus from the tactical project management to strategic business alignment. They are grounded in “what they know,” often waiting until their leadership has the mandate and desire to invest in training and development to change the focus of the governance organization. In other words, much of today’s enterprise outsourcing talent is simply too poorly developed to deliver on the strategic business objectives that are rapidly increasing in importance to their enterprises.

Source: HfS Research 2013, n = 282 Enterprise Buy-side Executives
New hiring strategies are needed to attract and retain a new generation of talent

The most critical skills needed to move enterprises toward higher-level strategic objectives for outsourcing—skills such as defining business outcomes and influencing executives—are among the most difficult to recruit. Hence, not only do companies lack the right talent to achieve address the most critical issues, they also struggle to find it externally. HfS believes this is because of a general skills deficit lag in the industry. If enterprises, in general, are not developing strategic outsourcing skills, how could such skills be readily available for hiring?

Exhibit 6: How difficult or easy has it been to attract and source talent for your team with the following skills?

Source: HfS Research 2013, n = 282 Enterprise Buy-side Executives

Far too many enterprise outsourcing governance leaders are operational managers, schooled and experienced in managing large departments of operational personnel but not in driving toward additional business value. They follow rules and processes to ensure a function is operationally efficient instead of working to align outsourcing relationships with corporate growth objectives and strategic business outcomes.

This situation is unlikely to change in the immediate future. Recruiting armies of analytics talent or strategically focused operations managers may be well beyond the reach and resources of the majority of enterprises today.
However, in a few successful cases, enterprises are reaching outside of their organizations to bring in outsourcing leaders who can influence leadership and can shift the mindset of outsourcing from one of cost to one of achieving business value. The presence of a senior “mover and shaker”—one with a strategic mindset who also has the communications and interpersonal skills to align senior stakeholders and convince them to invest in developing their talent and work more collaboratively with a quality service provider—is a step we at HfS are already seeing reap very positive results for several enterprise customers.

For example, one major enterprise recently recruited a former CEO from a consulting firm to lead all its outsourcing initiatives; this enterprise has quickly reaped the benefits, at the executive level, of better focus and attention on achieving a higher performance benchmark with their existing outsourcing initiatives. This executive brought to the table a strategic mindset as well as seasoned sales and interpersonal skills, rather than just knowledge of processes and operational issues.

There is ample precedent for taking this broader perspective on the business skills needed by senior outsourcing executives. They know that aligning technology delivery to the needs of the business and understanding how IT can support finance, HR, the supply chain, and so forth is much more relevant to the business than simply knowing how to implement software or arbitrage labor costs. The same approach applies to finance, HR, procurement, and other operations functions where the function leader needs to align his or her department goals with the needs of the business rather than focusing solely on delivering the operations. Whether or not processes are outsourced, they need to be aligned with the needs of the business, as outlined in Exhibit 4.

The majority of enterprises need formalized training for their outsourcing management talent

When it comes to how enterprises are approaching the training and development of their staff (Exhibit 7), it is clear that the vast majority of enterprises are still struggling to develop adequate training programs, especially regarding developing strategic business skills. For example, in the areas of continuous improvement and analytics, the majority of enterprises have no training programs in place, whether formal or informal. In fact, beyond project management skills, fewer than half of all enterprises have any formal development programs, either internally or externally, to develop skills related to outsourcing management.
Exhibit 7: In which of the following areas does your enterprise train and develop staff?

<table>
<thead>
<tr>
<th>Area</th>
<th>None</th>
<th>Informal Efforts</th>
<th>Formal Internal Program</th>
<th>Formal External Program</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sourcing and selection of service providers</td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Industry acumen</td>
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<tr>
<td>Analytics</td>
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<tr>
<td>Transition management</td>
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<tr>
<td>Contract negotiation and management</td>
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<tr>
<td>New hire training program specific to...</td>
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<td></td>
<td></td>
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<tr>
<td>Relationship management</td>
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<tr>
<td>Financial management</td>
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<td></td>
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<tr>
<td>Continuous improvement</td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Project management</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Process-specific training program</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: HfS Research 2013, n = 282 Enterprise Buy-side Executives

Skills development for outsourcing managers must focus on areas beyond just those required to oversee basic operations. The majority of enterprises’ outsourcing governance teams have been so overwhelmed just dealing with the operational and tactical challenges that they have taken their eye off the ball when it comes to developing their own teams’ broader skillsets.

Not doing so has serious consequences. Enterprises that fail to develop their talent early on will be left with a staff that is ill-equipped in the future to, for example, drive innovation programs or work with other business functions to align outcomes around common goals. In addition, when conducting this research, HfS observed a worrying lack of awareness within many outsourcing governance organizations that the skills needed to manage a department of (for example) 500 accountants are very different from the skills required to align services with enterprise objectives and manage a relationship with an outsourcing service provider. As mentioned earlier, developing skills around business outcomes-evaluation, communications, and stakeholder alignment is now required of those enterprises that view their outsourcing engagements as strategic opportunities for their organizations.

When asked about this issue of broader skills development, one Global 50 organization with significant outsourcing experience described the task of developing their staff’s strategic talents as akin to “changing the wheels of a car while driving.” However, the company mandated three hours of training in outsourcing governance per week for its managers, something that is already reaping dividends for this buyer through increasing job satisfaction and advancing the objectives of their major outsourcing engagements. The firm initially engaged an external consultant to help devise and set up the program but now has the capabilities internally to develop their own staff and enhance their own internal training programs.
Without taking definitive action to develop formalized outsourcing management skills, enterprises will continually be short-handed, under skilled, and forced to rely on their legacy tactical skills to produce results. Ultimately, that’s a recipe for failure because an organization’s current talent pool is not equipped to drive outsourcing initiatives toward the new levels required to compete more effectively in today’s markets.

**Some Service Providers Can Help Enterprises Address Talent Shortages, but Many Are Falling Short**

The talent shortage in the outsourcing area facing enterprises is becoming increasingly severe. Shouldn’t the providers themselves be able to help here? After all, most outsourcing service providers aggressively seek to differentiate themselves in the market by promising clients access to their global talent. Smart providers are also recognizing that those customers sitting in the “efficiency” and “strategic” outsourcing camps are likely to be most concerned with augmenting their talent capabilities, while those in the “lights-on” camp are likely to be a lost cause and thus unlikely to be worthy of attention.

Can service providers provide the analytical skills, process reengineering, and customer-centric redesigns that companies need? Let’s examine our research:

- **Service providers at the quality end of the market invest in training their talent.** While enterprises have traditionally built their “indirect” functions as support structures for the production, delivery, and servicing of their primary products and services (often referred to as their “back office”), the outsourcing service providers’ delivery staff is their core offering. Consequently, some service providers invest in developing their talent through formal training programs, as shown in Exhibit 8. In every category important to outsourcing, service providers are more disciplined than their customers in the development of talent.

- **Surprisingly, however, not all service providers invest in formal talent training.** While service providers are clearly more focused than enterprise buyers on developing talent, our research reveals that barely half of providers actually have formal programs in place in key disciplines such as industry skills, analytics, and relationship management. Even more worryingly, only 60% of providers even have formal training and development programs in “bread and butter” areas such as transition management, governance training, or continuous improvement.
Some service providers create career opportunities for their staff that specialize in process excellence. Our research shows that there is a significant gap between enterprises and service providers in their ability to create career opportunities. As shown in Exhibit 9, enterprises’ operations and outsourcing management staff feel they have limited career growth within their own enterprises, however, their service providers’ delivery staff are generally more satisfied. Ultimately, service providers are able to create career opportunities for their staff because administrative services in finance, procurement, customer service, and IT are core businesses to them, not neglected back-office teams.

HfS sees the establishment of formal training and development programs as critical to creating defined career paths and roles for outsourcing personnel. One Fortune 500 organization has engaged its outsourcing provider to help develop internal training programs with career development being a significant component of the programs. The enterprise outsourcing leadership believes the definition of roles and career goals is having a significant impact on staff morale and is also improving the success of business-alignment initiatives.
Service provider talent varies and has a critical impact on the business outcomes of an outsourcing engagement. HfS believes the quality of service provider talent is as critical to the long-term success of an outsourcing initiative as the skillset of the buyer outsourcing management, and companies should be focused on both. Our frequent discussions with enterprise customers clearly show there are often marked differences in the quality of the talent presented by the service providers. Some providers opt to select higher-caliber university graduates and place them into formal training programs, whereas others, those who cut corners with the quality of staff, tend to suffer from higher attrition, which can significantly undermine the continuity and quality of a client engagement. As Exhibit 9 illustrates, far too many providers clearly lack discipline, focus, and investments when it comes to developing their staff and have job satisfaction scores barely above “neutral.” If the service provider talent is not bringing new skills, discipline, or capability to the table and is not actively developing the skills of its workforce, then there is little likelihood of the client achieving much more value, over and above the cost savings achieved, from the lower cost labor being provided. This is more of an issue in business process outsourcing engagements that rely heavily on talent from India where there are fewer structured training programs between the universities and many of the service providers in areas such as finance, analytics, and industry process -- for example, insurance, banking, or life sciences. Enterprise buyers need to vet the skills and capabilities of their provider teams and training practices thoroughly when making selection decisions.

Exhibit 9: Job satisfaction of outsourcing staff: enterprise buyers versus service providers

<table>
<thead>
<tr>
<th>Category</th>
<th>Service Providers</th>
<th>Buyers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intellectual Challenge</td>
<td>Satisfied</td>
<td>Satisfied</td>
</tr>
<tr>
<td>Compensation</td>
<td>Neither satisfied nor Dissatisfied</td>
<td>Neither satisfied nor Dissatisfied</td>
</tr>
<tr>
<td>Career Opportunities Outside of Your Organization</td>
<td>Satisfied</td>
<td>Satisfied</td>
</tr>
<tr>
<td>Non-Monetary Recognition</td>
<td>Neither satisfied nor Dissatisfied</td>
<td>Neither satisfied nor Dissatisfied</td>
</tr>
<tr>
<td>Workload</td>
<td>Neither satisfied nor Dissatisfied</td>
<td>Neither satisfied nor Dissatisfied</td>
</tr>
<tr>
<td>Skill Development</td>
<td>Neither satisfied nor Dissatisfied</td>
<td>Neither satisfied nor Dissatisfied</td>
</tr>
<tr>
<td>Career Opportunities Within Your Organization</td>
<td>Satisfied</td>
<td>Satisfied</td>
</tr>
</tbody>
</table>

Source: HfS Research 2013, n = 282 Enterprise Buy-side Executives and 171 Service Provider Executives
Poorly executed outsourcing engagements result in a disappointing talent experience

Far too many enterprise buyers view service provider talent as substantially inferior to their own (see Exhibit 10). While service providers may provide a similar ability to increase the scope or scale of an outsourcing program and have close to the same ability to manage efficiency improvements, most enterprise executives feel their own talent remains superior in all other areas.

Exhibit 10: Enterprise buyers’ talent self-assessment and the perspective of service providers

These data beg the question, “If, in the eyes of enterprise executives, service providers are not as capable as their own enterprise to achieve any corporate objective, why do they outsource in the first place?” Our research suggests three reasons for this paradox.

» **Many enterprise operations managers are placed in governance roles without any training and simply defend the status quo.** From our interviews, it became clear that too many outsourcing buyer executives feel they get buried in the minutia of managing operations and tough transitions. The blood and tears shed simply to get their outsourcing engagement functioning often permanently scars many executives. In their tunnel vision, they can see only negatives and forget the positives. Consequently, the same staff who may have previously overseen transactional work is put in governance roles, which require very different skills;
however, little if any investment is actually made in retraining the staff for those new roles. Most of their career skillsets are not suited to their new roles, and they revert to what they are comfortable with, as opposed to fulfilling the requirements of their new roles. It is not unlike asking a waiter to start managing his restaurant with no real training in management; without such training, he is likely to keep focusing on the operations of getting the food to the customers instead of focusing on overall customer satisfaction, changing the menu to entice new customers, etc. That individual may well have the deep-rooted desire to learn to become a manager, but intentions are not enough. Focused and relevant investments in training and development are required to turn intention into capability.

» The “keep the lights-on” approach to outsourcing has failed many enterprises in delivering any business value beyond initial cost savings. Far too many enterprises dived into outsourcing initiatives with unrealistic expectations. Simply put, limited (if any) investment was set aside for business transformation programs, change management, innovation projects, etc. This “keep the lights-on” approach means many outsourcing service providers have simply ended up performing services in the same indifferent manner that their clients were before. Expecting outsourcing to provide a transformational experience when the engagement is based on low-cost labor and no real transformation has proved to be a disappointing experience for many enterprises.

» Too many enterprises have selected the wrong service provider because they were overly focused on cost reduction; so, they have “gotten what they paid for.” Driven largely by cost savings objectives, many enterprise executives use their procurement organization to run highly competitive RFPs and may even hire negotiation specialists to drive prices as low as they can (50% of major outsourcing engagements have engaged a negotiation specialist to squeeze down pricing from their providers over the last two years). This process is inherently biased towards low-cost solutions and those service providers who specialize in delivering the cheapest possible services. These engagements are structured to keep the “lights on” as opposed to a long-term strategic agenda to achieve business value. As a result, enterprise executives often unreasonably expect that solutions that have cost reduction at their heart will somehow magically provide exponential strategic value to their businesses. The truth is that their service provider selection traps them into a cycle of limited investment in their business operations, which constrains their future opportunities to create business value. Moreover, many enterprises have found themselves in a “lights-on” outsourcing scenario from which it is nearly impossible to escape without having to renegotiate their contract and possibly switch to a more appropriate service provider.

If the outsourcing provider is simply replicating what the buyer was doing in the first place, then the buyer will rarely think the provider can do a better job than they were.
How Outsourcing Governance Leaders Can Develop and Align Their Talent to Create Continual Value

Despite the talent paradox in outsourcing that traps many enterprises in a situation where their strategic intentions are not matched by the skills required to execute such strategies, our research has uncovered several strong examples of enterprise leaders who have learned that service providers can boost talent-related results for their firms. After many discussions with such enterprise leaders, HfS has identified four ways enterprises have successfully leveraged the talent of their service providers:

**#1: ENTERPRISES MUST FOCUS TALENT INVESTMENTS ON ENHANCING THEIR CORE BUSINESS SKILLS** - Companies that have been successful with outsourcing stopped investing in external experts with skills only in operations management, procurement, and service-level measurement. Over time, they have developed a good number of operations managers in-house, and their service provider excels in these activities. Such companies are now investing instead in skills that improve their core business. For example, a senior vice president for a large health insurer who oversaw a major transformation program in his enterprise said, “We’ve morphed from an insurance firm into a services enterprise. As a result, in many ways we act nothing like a traditional insurer. We now have consulting and business services skills that we market. Talent is critical for us.” And when companies learn to leverage their service providers for operations management expertise, they stop investing in duplicating their provider’s operations talent. A vice president of finance at a large investment bank explained it this way, “The core talent is what we invest in, and everything else is outsourced.” The bank focused on developing investment bankers and leveraged the outsourcing service provider’s expertise in back-office business processes, allowing each to excel at its own specialties.

**#2: ASSESSING THE AVAILABILITY OF STRATEGIC TALENT MUST BE A TOP PRIORITY DURING SERVICE PROVIDER SELECTION** - Operational capabilities are now just table stakes and are not true differentiators anymore when a buyer is choosing a service provider. Yet too many buyers continue to assess providers based on an outdated capability model.

In some cases, that older mentality is coming back to haunt enterprise customers. The failure of providers to provide strategic talent was a common issue raised by customers during our interviews. A senior vice president for a media and publishing enterprise put it this way, “Our business leaders went into the F&A deal expecting the vendor to have a better understanding of general accounting principles. They are process experts, not subject matter experts. On the other hand, on the payroll side [different provider], they are certified payroll professionals. They are subject matter experts, but are weaker in terms of process.” Ultimately, the F&A service provider had not differentiated itself, while the investment in talent by the payroll service provider demonstrated higher levels of value for their customer.
The point of differentiation was so important to some companies that they were willing to pay more to get more than just commoditized operations executives. According to one outsourcing governance executive, “We find that providers that have methodologies, analytics, and talent are more valuable to us, so we're willing to pay the appropriate premium for their services.”

**#3: REVAMP SKILLS EXPECTATIONS FOR THE RETAINED TEAM** - To move beyond the old-world talent perspective, which was overly focused on operational skillsets, successful companies have looked for strategic skills by redefining the job competency models of individuals managing service providers. “People in the sourcing space need to have a genuinely wide skillset,” explained a vice president in a US health insurance enterprise. “Surely they have to be good with numbers and have great socialization skills because this is all about relationships and building and sustaining trust, but we’ve found a strategic view of the market forces that affect customer experience to be essential.” Skills they found essential were analytical, influencing, process transformation, and consulting skills. One enterprise went so far as to hire the retained team before it selected a service provider. “We hired the retained team before we selected our service provider because we knew the retained team was the key to success.” This executive even hired individuals with proven experience in driving innovation pipelines. “If you have an innovation process that doesn’t work, it destroys the relationships. It creates enormous frustration among service providers when all they hear is ‘No,’” explained an executive from a large insurance firm.

“Many people running the old processes were experts as the way we did things for 20 or 30 years, no the way we could do it [today],” explained an executive from a large insurance firm.

**#4: ESTABLISH SHARED STRETCH GOALS THAT ENCOURAGE THE DEPLOYMENT OF SKILLS ON A REGULARLY REVIEWED BASIS** - It is normal for an outsourcing relationship to “hit a wall” or to plateau at some point over time. Too many such relationships operate on a mentality along the lines of, “If it’s not broken, don’t tinker with it; or, in other words, if the SLAs are green, service must be good”. The problem with this approach is that it causes the governance staff to become complacent and lose interest in challenging its organization and provider to find ways to continue to improve performance. Moreover, the failure of enterprises to review goals, metrics, and objectives regularly with their providers leads to a misalignment of the outsourcing goals with the business objectives of the client. As mentioned earlier, if the enterprise leadership is merely content to keep the “lights-on” and achieve adequate cost-performance against financial objectives, then this approach may be sufficient. However, HfS believes two-thirds of enterprise buyers do not wish to get trapped in this “lights-on” purgatory, where goals are only revisited every five years or more. For example, one large financial services organization began its global accounts payable BPO project by centralizing mailrooms, keying centers, and workflow technology. Once phase one was stabilized, the executives of both the buyer and the service provider brought their teams together to brainstorm how they could improve the process yet further. The result was a mandated electronic invoice submission via a web-accessible supplier portal that eliminated manual effort for most invoices. Still, that was not enough for the engagement leads. In the heat of a financial system’s failure, they again brought their teams together to re-position their solution to suit business needs. The team put aside operational performance issues and tried to improve cash flow and financial terms. Soon, the two enterprises deployed dynamic discounting to improve payment terms and widened purchasing card use (because they have built-in rebates). They also invested in spend analysis tools to understand how spending could be consolidated and
strategically sourced. This mentality of continuous step-change is essential for enterprises that want to leverage their talents’ best capabilities, as is the need to focus on business issues instead of process performance metrics.

The Bottom Line: Enterprises Leaders Who Care About Improving Their Capabilities, Must Focus on Talent When Outsourcing

What organizational leaders fail to recognize is that outsourcing any intimate business or IT functions should never simply become “done”, if their leadership has the ambition to improve productivity, efficiency and access to critical data.

This notion that there is some finite initiative, a specific number of deliverables that can be checked off an old punch list to complete the task of outsourcing, is a very common misconception by the leadership in many of today’s organizations.

As this research study has clearly shown, the keys to improvement lie in the talent pool available to organizations – not only their own internal talent, but the talent being provided by the service provider.

Enterprises must manage their governance organizations like business functions, not like cost centers, with specific value goals attached. Expectations about the value outsourcing can deliver must change, and such change begins by training enterprise outsourcing governance teams to focus on business issues, not merely administrative cost reductions. In far too many enterprise outsourcing situations today, tactically-oriented operational specialists and project management executives are left managing the relationships. Most such managers have been successful at negotiating contracts and transitioning services; however, when it comes to directing the outsourcing relationship toward larger business issues, many simply lack the necessary business acumen. Formal training programs that develop governance staff’s communication skills, business acumen, and goal-setting capabilities as well as improve their ability to align stakeholders and analyze data are critical in moving outsourcing in a strategic direction.

Service provider talent is critical for achieving value with outsourcing. Too many service providers are poorly positioned to support their enterprise clients who are in dire need of a talent infusion—some because they are simply poorly resourced with talent themselves and others because of the poor design and execution of the outsourcing engagement by the enterprise customer. However, most enterprises do not have the resources to hire armies of new talent. They must focus instead on developing the staff they currently have—and that includes their service provider talent. The right service provider can help its client move toward
more strategic outsourcing by offering talent with higher-level skills. Indeed, outsourcing relationships will only perform at a higher level if the service provider has a sufficient quality and depth of talent.

**Long-term value is created only when service provider talent is managed as an extension of the enterprise.** The right provider should bring the capabilities enterprises need, but they must to be prepared to work in partnership with the provider to create value. Moreover, bringing skills to their clients is only half the provider’s challenge; the other half is the enterprise leadership having the desire and the capability to change its whole approach to developing and managing its talent.
Appendix: Survey Methodology and Demographics

Exhibit 11: Demographics – Enterprise Buyer Industries

Source: HfS Research 2013, n = 282 Enterprise Buy-side Executives
Exhibit 12: Demographics – Enterprise Buyer Locations

Source: HfS Research 2013, n = 282 Enterprise Buy-side Executives
Exhibit 13: Demographics – Company Size

Source: HfS Research 2013, n = 282 Enterprise Buy-side Executives
Exhibit 14: Demographics – Job Title

- CEO, C-Level, EVP: 4%
- SVP, Function Head: 8%
- Other: 5%
- VP: 14%
- Director: 26%
- Manager: 43%

Source: HfS Research 2013, n = 282 Enterprise Buy-side Executives
About the Authors

Phil Fersht

Phil Fersht founded HfS Research in early 2010 and has overseen the growth and development of the enterprise to become the leading analyst authority and knowledge community for global business and IT services.

Fersht was named "Analyst of the Year 2011" by the Institute of Industry Analyst Relations (IIAR), winning the premier analyst award for a second successive year. This is the most coveted global award for industry analysts in technology and services industry. He is a renowned expert in the fields of Business Services and IT Strategies and frequently discusses complex industry-specific issues that impact how enterprises manage their global business operations. He is also author of the leading blog for the services industry entitled “Horses for Sources”, now entering its sixth year.

Over the past 17 years, Fersht has lived and worked extensively in Europe, North America and Asia where he has advised on more than 150 major Outsourcing, shared services and offshoring engagements and consults regularly with senior business operations and IT executives on their global sourcing and services strategies. During his career, Phil Fersht has worked at AMR Research (Gartner Inc), leading the firm’s Outsourcing and IT Services practices. Previously, he served as market leader for Deloitte Consulting’s Outsourcing Advisory Services, where he led numerous Outsourcing and offshoring advisory engagements with Fortune 500 enterprises. He also worked for Outsourcing consultant Everest Group where he helped establish the enterprise’s Outsourcing research practice. Phil began his career at IT analyst IDC where worked across its European US and Asia/Pacific operations.

He is a frequent author and speaker on IT services, Finance, HR and Procurement Business Process Outsourcing trends and issues. He was named both an "FAO" and "HRO Superstar" by FAOToday and HROToday Magazines for 2005, 2006, 2007, 2008, 2009 and 2010 and was featured as the cover story for the December 2006 issue of FAOToday as one of the Outsourcing industry’s most prominent experts. He was also nominated for “Advisor of the Year” at the FAOSummit 2008. He was also recognized, in 2011, by Globalization Today (the official magazine of the International Association of Outsourcing Professionals) in their first ever "Powerhouse 25" list.

He speaks regularly at many leading industry conferences and is quoted extensively in major media, which recently includes lead stories with the Wall Street Journal, BusinessWeek, Investor’s Business Daily, USA Today and CIO Magazine.

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Tony Filippone is Executive Vice President, Research, at HfS Research. He oversees the quality of HfS' overall research agenda and published research and works with the HfS analyst teams to ensure HfS' content is relevant for the firm's buy-side clients’ sourcing strategies.

His prime research focus is delivering practical advice, and imparting real-world vendor management experience to buy-side clients and service providers on what really matters – how to govern Outsourcing programs in a manner that creates real value to all parties. He also oversees the enterprise’s research in the healthcare industry Outsourcing vertical and the document management and call center Outsourcing horizontals.

Prior to joining HfS, Tony spent nine years at WellPoint, the United States’ largest health benefits enterprise, where had multiple leadership roles. Tony initiated and led the enterprise’s enterprise-wide Outsourcing governance for a multi-vendor, multi-process (call center, back office processing, imaging/data entry/mailroom, and KPO) program with thousands of FTEs. Tony led strategic sourcing in complex indirect services procurement, where he managed the selection and enterprise-wide implementation of an industry leading procurement application while simultaneously leading cross-functional sourcing teams in Outsourcing, marketing, consulting, facilities, contingent labor, and human resources categories. Tony also led WellPoint’s strategic procurement initiatives, including creating and leading it’s strategic supplier management program, demand and consumption management analyses, and business process benchmarking. Before joining WellPoint, Tony spent seven years consulting with Accenture and MarchFirst, where he specialized in business process simulation and reengineering, strategic customer relationship management, and post-merger/acquisition integration management.

Tony holds a MA in Communication Management from the University of Southern California’s Annenberg School for Communication and a BA in Enterprisel Communication (Magna Cum Laude) from Pepperdine University. Tony is also a Certified Professional in Supply Management (CPSM) from the Institute of Supply Management (ISM).

When he’s not pondering the future of governance models, you will find Tony growing organic heirloom tomatoes by the wheelbarrow-load and wearing out his wife and two young sons’ patience with his infatuation for manually focused rangefinder cameras.

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About HfS Research

HfS Research (www.HfSResearch.com) is the leading independent global analyst authority and knowledge community for the business and IT services industry. It is unique in the fact that it serves the research and strategy needs of business operations leaders across finance, supply chain, human resources, marketing, customer management, IT and core industry functions.

In addition to researching business operations strategies, HfS educates and facilitates discussion among the world's largest knowledge community of enterprise services professionals, currently comprising 120,000 subscribers. HfS Research also facilitates the HfS Sourcing Executive Council, the acclaimed elite group of sourcing practitioners from leading enterprises, which meets on a bi-annual basis to share the future direction of the global services industry and discuss the future enterprise operations framework.

Led by recognized industry expert Phil Fersht, HfS Research differentiates itself with its global team of expert services analysts with real industry experience, provocative and opinionated research, unrivalled market analytics, and a view of technology as an enabler for business process improvement. Its on-demand expertise relationship model helps clients leverage HfS knowledge and strategic insight in a rapid, responsive and engaging manner.

In 2010 & 2011, HfS was awarded Analyst of the Year by the International Institute of Analyst Relations (IIAR), the premier body of analyst-facing professionals, and achieved the distinctive award of being voted the research analyst industry's most Innovative Analyst Firm in 2013.

Now in its sixth year of publication, HfS Research's acclaimed blog "Horses for Sources" is widely recognized as the leading destination for unfettered collective insight, research and open debate of sourcing industry issues and developments.

To learn more about HfS Research, please email research@HfSResearch.com.

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