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Why its summer may be over

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What suppliers would tell you if they could 2

Inside the supplier's mind

What do suppliers think about? And what would they tell you if they could? Well, they think that any problems are probably *your* fault. Professors Leslie Willcocks and Mary Lacity present Part 2 of our popular series. What do suppliers think about *themselves*?

The Autumn 2011 issue of **Professional Outsourcing** led with the feature *What Suppliers Would Tell You If They Could*. That article looked at the challenges of contract negotiation and revealed six things that outsourcing vendors think about their customers. In this exclusive follow-up, Professors Leslie Willcocks (London School of Economics) and Mary Lacity (University of Missouri-St Louis) reveal four things that providers think about an even more challenging area: their own performance. As before, the authors' conclusions are drawn from their long careers talking to over 1,200 executives on both sides of the fence. Some of their findings make uncomfortable reading.

- **"We have internal problems too."**

Providers naturally focus on their strongest attributes during contract negotiations, but once the deal is up and running, the vendor's internal politics are less easy to hide. The supplier's engagement manager may need the client's help to overcome these issues, to help fight for the provider's best resources, or to fill gaps by transferring or loaning staff to the vendor. The client's senior management – including the CEO – may have to intervene at times for the deal to be effective.

"Providers naturally focus on their strongest attributes... But once the deal is up and running, the vendor's internal politics are less easy to hide."

Providers say that salespeople are often incentivised to complete a deal quickly, and that this can sometimes leave loose ends – unrealistic prices, scope vagueness, overly ambitious deadlines – for those who have to make it work. A providers's own staff may not always be aware of capacity problems in other parts of the business.

Staffing can be difficult in any organisation that is committed to maximising the use of its human resources, leaving little slack to service new customer problems or requests. This can create bad feeling, given that the supplier is supposed to be taking care of a customer's business functions. Often, the best people are in short supply and the 'A-team' is moved from client to client to wherever the need is greatest.

Here's looking at you: Suppliers think that the real problem is usually their client.

In this day and age, many providers are structured to be as efficient as possible internally, rather than to address a client's every need; after all, few can afford staff who are not doing anything. Budgetary processes can mitigate against competitive pricing as well. For example, one major provider added an internal profit margin to every resourcing transaction between its internal departments. Its insurance company client swallowed the high aggregate prices, mainly because it was unaware of how they had arisen. However, when the client's new CIO dug into the details later, there were heated meetings, a price reduction and a negotiated rebate.

At the bid stage, providers talk a lot about economies of scale, superior skills and management, but are sometimes forced to admit that these cannot be delivered as well as they originally claimed. Internal networks of influence can be a factor in this: one account executive may not have the political clout of another within the same company, for example.

"One major provider added an internal profit margin to every resourcing transaction between its departments."

One Asia-Pacific bank executive said: "We get account executives from the [US] parent country coming over on two-year cycles. The differences are remarkable. When X was in place nothing happened. But then Y came from the provider's HQ and was really well connected. It showed up in better pricing and faster resourcing."

When providers run into internal problems, some admit that their instinct is to cover them up. However, others feel able to share these challenges with their clients, as revealed in the case of an oil giant and its supplier. The client manager said: "The new account executive said they were not making any money. So we cut some of the loss-making parts out of the contract, took them back in-house, and renegotiated some of the pricing. We liked their work, but they had clearly just got their sums wrong."

So does offshoring solve these problems, and do lower labour costs make a difference? Not automatically. One pharma giant signed up an Indian provider for IT development work, because labour arbitrage ➔

➔ made prices 50% cheaper – plus the provider's developers were technically superior to the customer's staff. However, its middle management was weak.

The provider said: "When we finally understood their expectations we realised that we did not have the middle managers to cope. We ended up with the client supplying us with three middle managers and then helping our people get more experience for 18 months. It was an outlay for them, but it made us more flexible – and more capable for the client too."

Providers say that clients often help in outsourcing arrangements, and this strengthens the relationship. One provider executive spelt out the implicit contract in these cases: "Given their sunk investment and the switching costs, clients quite often help us. But we have to be credible, and clearly working in their interests."

• "It's probably your fault."

Providers say that blame is part of the reason for them being there. This is not such an outrageous claim: the authors carried out independent studies in 2001 and 2009 which found that, more often than not, 60% of the fault is probably the client's when outsourcing projects go wrong.

Consider the following admission from a senior executive of an Asia-Pacific bank, which was in a five-year deal with a global provider: "We never resolve the issues. They're insoluble, because the bank still doesn't lead, or own, the outcome. So while we [the client staff] continue to blame the outsourcer for not delivering something that we can neither describe, nor write down, nor articulate, nor agree on, it's obviously just not going to work." Another outsourcing client said: "90% of the service lapses were inherited from us."

Providers are frequently taken to task for not hitting service level agreement (SLA) targets, but clients may cause this to happen in a variety of ways: for example, by not defining requirements rigorously enough; by not following agreed procedures; by not providing accurate information; or by not communicating.

"When we understood the client's expectations, we realised that we did not have the middle managers to cope. We ended up with the client supplying three of them."

When blaming the provider for something, it would be wise to remember that it was the client, not the supplier, that:

- worded the contract
- selected the provider
- decided the scope of the project
- agreed the pricing
- set up the governance and measurement mechanisms
- and staffed its internal capability to run the deal.

Clients have also been known to change their minds about the details after a contract has been signed, ignore supplier recommendations, disempower them on decisions, and fail to heed their warnings. This is not a recipe for successful SLAs!

• "There are limits to smart work."

Clients can become fixated on driving down prices and upping service standards, while also throwing in demands for innovation. At the same time, clients often suspect providers are padding out the price. Clients also – reasonably – expect providers to keep the contractual and verbal promises they made, but this can be a problem when clients have changed the conditions under which those promises are to be implemented.

Put another way, clients often want to pass onto their providers the headaches, adverse risks and costs they wish to limit within their own organisations. These can be received internally from problems with business units, or externally from events such as a credit crunch or recession. Faced with such pressures, providers like to say that there are limits to working smarter.

There may be other reasonable limits on the provider doing so, too. It is possible, for example, that the client has already achieved most of the potential efficiency gains in-house before out-sourcing, or might have received those gains from the provider in the early days of the deal.

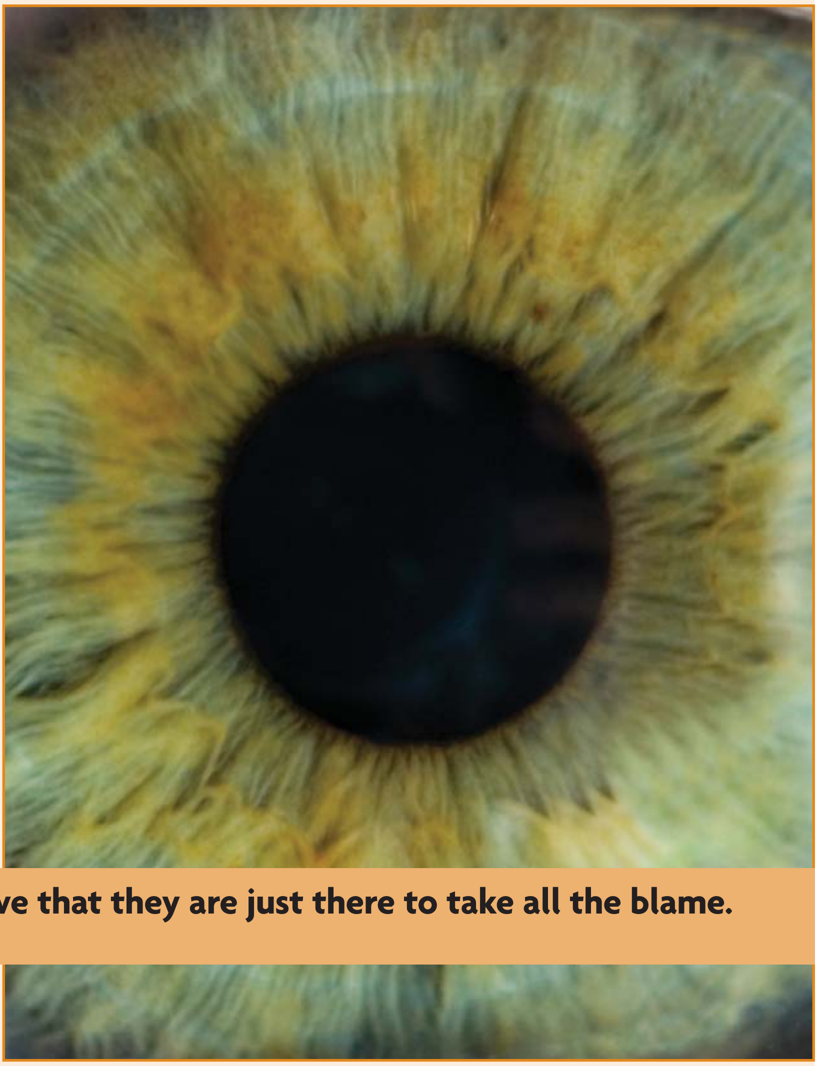
This was acknowledged by the IT director of an oil company when he outlined his experience of outsourcing

with three different providers: "We didn't expect big savings; we were looking for a dampener on future costs. That, together with our ability to refocus, get the headcount down, and make costs flexible. We really did get most of the savings out in the standardisation and centralisation efforts we made over the three years before outsourcing."

On the other hand, the client may be so eager to achieve dramatic cost savings that the provider is left with little room for manoeuvre. In one 10-year financial services deal, the provider said that its technology investment policy was severely inhibited by the constant demand for savings. This was despite both sides calling the deal a 'strategic partnership'. The provider said it had no option but to "sweat the IT assets" for five years.

Some providers undertake to work smarter because of the promise of additional work and contracts. But what happens if they never appear? In one 10-year aerospace arrangement with a provider – another 'strategic partnership' – the vendor invested in the front end of the contract, only to find the buyer's business units never commissioned new work. This inhibited the vendor's ability to give the client priority, time, innovation and resources, causing complaints from the very managers who contributed to this outcome.

Internal politics, again, sometimes prevent providers from innovating and achieving real economies. In one insurance company that outsourced its mainframe processing, the provider achieved a 15% cost saving over five years but could not achieve more, or better service, because each of the client's business units demanded its own data centre. As a result, data processing ran across four data centres rather than being consolidated into one.



Hard focus: Some suppliers believe that they are just there to take all the blame.

"Suppliers admit that their clients need well-tuned hype-detectors and be able to discriminate between the services that are available and the ones they actually need."

• "We repackage old ideas."

All outsourcing customers recall the many IT products and services over the years that have been sold as 'new', or 'transformational', or which even required them to reengineer their business. Hype has never been far from IT and, by association, the consulting, ITO and BPO markets whose business it is to bundle services around it. (The editor of this magazine was once told, only half-jokingly, by a vendor CEO that the industry decided to call it 'Cloud' to "make it mysterious and give the consultants something to explain".)

Suppliers interviewed during the course of the author's research have admitted that their clients need well-tuned

hype detectors, and also need to be able to discriminate between the services that are available and the ones they actually need. IT's transformational capabilities are often exaggerated. One client CIO said: "We paid a consultant $100,000 to advise us how to 'leverage Cloud Computing' – only to discover we'd been doing it for five years!" Another client asked: "Isn't business analytics just a fancy term for displaying my stats on a dashboard?"

Many of the technologies that we now call 'Cloud' existed in the 1990s, but were called such things as 'ASPs' (application service providers) and utility computing. In fairness, the recent industry-wide rebranding was not an entirely cynical exercise: many of the enabling technologies, such as wifi, virtualisation and high-speed broadband, did not really exist when utility services appeared.

Oracle CEO Larry Ellison was famously dismissive of the phrase 'Cloud Computing' for years, pointing out from conference platforms that it was just rented hardware running enterprise applications. In September 2008, he said: "I don't understand what we would do differently in the light of Cloud Computing… other than change the wording of some of our ads. It's crazy."

But unknown to many, Ellison was both poacher and gamekeeper, with investments in the Cloud industry that he lampooned. In a sense, he dared the upstarts to succeed – some, after all, are run by ex-Oracle employees. In 2010, Ellison finally used the word 'Cloud' to describe an Oracle product – some hardware, just to ram home the point. Recently, he went further and bought Cloud startups RightNow and Taleo for a combined total of nearly $4 billion.

So it is worth remembering that providers have great marketing – enough to convince a multibillionaire – but these do not automatically translate into client value. Cloud Computing must be put in the context of previous 'revolutions' in technology and services outsourcing. Cloud is best seen as a convergence of technologies, together with a new focus – and a fundamental reliance – on service.

"Customers cannot wrap the rhetoric of partnership around a fee-for-service deal and still expect to receive a high-performing back office."

• Conclusions

Over the course of many years talking to both providers and their customers, it is clear that the outsourcing customer is *not* always right. Customers cannot wrap the rhetoric of partnership around a fee-for-service deal and still expect to achieve a high-performing back office.

Clients have a difficult task. To succeed in outsourcing, they must find a partner with skills in 12 specific areas: planning and contracting; governance; organisation design; leadership; business management; customer development; domain expertise; behaviour management; sourcing; process reengineering; technology exploitation; and programme management.

That is not all. The provider they choose should have the demonstrable ability to protect and secure client data and intellectual property, and maintain their confidentiality. A proven corporate social responsibility (CSR) capability is another key selection criterion.

It is also clear that true economic efficiency has more to do with management practices than any economies of scale that are associated with size. Those management practices include centralisation, standardisation, rationalisation, technology enablement and tight accounting controls.

If clients have already used these practices themselves to reduce costs before outsourcing, then they may leave little room for the vendor to manoeuvre. Indeed, the customer should consider whether they simply need someone to absorb the problems in their business. After all, there are limits to the vendor working smarter when they are really just expected to shoulder the blame. ■

• Professors Mary Lacity and Leslie Willcocks are the authors of *Advanced Outsourcing Practice: Rethinking ITO, BPO and Cloud Services*, published in June 2012 by Palgrave Macmillan.