RESEARCH SUMMARY:
Challenges with Offshore Business Process Outsourcing
By neoIT

More than half of the world’s top 500 companies outsource work to offshore locations. Over time, the offshore initiatives have moved from simple IT projects to long-term IT initiatives and now to ever more complex business processes. Analysts estimate that more than 50 percent of the simple ITO offshore engagements are failing\(^1\) to meet expected results. Still, the market has yet to realize the full effects of offshore BPO. There is a serious lack of qualified suppliers; the ones that do exist have short track records. Many of the offshore IT suppliers have seized the opportunity to offer BPO services to clients without making the necessary investments. As the volume of BPO deals accelerates, will companies be able to manage the complexities and anticipate the challenges?

Key issues: What are the unique challenges of BPO? What does the future hold for offshore BPO? How can clients ensure that their offshore BPO initiatives will succeed?

---

1 The definition of a failed offshore engagement in this context refers to a company that failed to achieve the full potential of cost savings and performance targets outlined in the contract. Please refer to Issue 8 of the neoIT white paper series, titled Offshore Program Management, published in May 2003.
Introduction

Many people see Business Process Outsourcing (BPO) as a company’s natural evolution from IT Outsourcing. And while it may be the logical next step, BPO presents distinct opportunities and challenges. Like ITO before it, offshore Business Process Outsourcing (BPO) will evolve through three distinct phases of increasing complexity, from managing transactional to area to comprehensive services.

Transactional processes are single, simple and can easily be handled by one supplier. Examples would be payroll processing or benefits administration. Area processes may include several inter-related services and are slightly more complex to manage. A good example of an area process would be workforce management, including both recruiting and staffing. Comprehensive processes are the transactional and administrative processes of a functional department, like HR or finance and accounting.

The Evolution of Offshore BPO

Offshore BPO has been around for a number of years disguised as simple, low-level, labor intensive work like teleservices, application processing, medical transcriptions, etc. The market is still immature and while many clients have become sophisticated with their approach to offshore, there is still a lot of confusion as to who the suppliers are and how BPO will vary from their offshore IT operations. As the market moves on from transactional to offshoring more area and comprehensive services, we anticipate many hiccups along the way.

Why Are Companies Adopting Offshore BPO Now?

- **The economic reason is strong.** No one can debate that cost pressures will continue. BPO is the next level of opportunity for companies after outsourcing manufacturing and IT. Over the last few years, companies have demonstrated 40%-60% cost savings over their existing operations.

- **The outsourcing process is continuous.** Outsourcing has traditional followed the renegotiation and expansion model. As companies become more comfortable with their offshore ITO models, BPO is the logical next step.

- **Extension of existing supplier relationships.** Many of the large traditional outsourcing suppliers (IBM, EDS, CSC, Infosys, Wipro, TCS) have invested heavily in
expanding their global delivery models. Companies that trust these organizations want to leverage their offshore capabilities to expand their relationship into offshore BPO services.

- **Infrastructure maturity.** Advances in communication technology for Data and Voice, telecommunications and other elements of infrastructure, improvements in overall technology, and investments in training and language development are allowing even more complex processes to be handled from offshore.

- **Knowledge of offshore markets.** Whether through the web or interaction with experts, the amount of readily available information on offshore markets has increased dramatically, thereby reducing perceptions of risk caused by fear of the unknown.

- **New markets provide new ways to leverage old investments.** Markets where manufacturing has been mastered (i.e. China, Mexico) are enticing companies to take a closer look at how they can leverage these markets for services outsourcing.

- **The shared services center opportunity.** Rather than continue to invest in shared services centers companies are now thinking about how to transition the centers to external service providers. Others are developing strategies to leverage the centers as a potential source of revenue.

- **Resourcing flexibility.** The offshore BPO investments allows enterprises to develop a flexible resourcing model for managing growth.

- **Speed of operation.** The differences in time zone across multiple offshore locations has the potential to allow enterprises to significantly speed operations, and provide 24/7 coverage to their constituents

---

**What are the Challenges?**

The usual list of challenges with moving and managing offshore resources exist: geopolitical, cultural, infrastructure, legal, etc. Companies are familiar with this list, but offshore BPO will provide some additional challenges due to a few fundamentally unique characteristics:

**Immaturity of Suppliers**

The phenomenal growth seen in the offshore BPO market over the last 3 years, is a result of the advantages discussed above. It also mirrors the comfort US enterprises have developed after nearly 15 years of exposure to the offshore IT services business. However, the supply-side for offshore BPO is not as mature as IT services, resulting in much higher level of risk, and consequently a much higher level of due-diligence required.

**Level of Control Requirements**

Effective outsourcing for business processes requires the suppliers to have a significant level of knowledge around the business environment they support. The providers need process expertise, infrastructure and systems, experienced human resources, and a set of established best practices to leverage.

In the current offshore supply landscape, most providers have only invested in infrastructure and the capacity to provide cost efficient resources, but the process expertise, systems and practices need to be acquired from the client enterprise. This form of ‘out-tasking’ demands much higher levels of operational control by the client enterprise, thereby requiring continued management focus on the outsourced process and diluting the achievable cost savings.
**Constraints of Support Infrastructure**

India has been among the biggest beneficiaries of the growth in offshore BPO, and continues to attract significant business from enterprises both in the US and Western Europe. The level of growth, however, is beginning to stretch the capacity for development work on support infrastructure provided at the local government level. While the national issues with the telecommunications system is being adequately addressed, the local infrastructure (roads, bridges, airports, etc.) are becoming bottlenecks to expansion of capacity.

**Standardization of Processes/Challenges in Driving Innovation**

Human interactions as well as IT systems and applications will need to enable the dynamic allocation of workflow and support quality assurance. Organizations need to gain a level of comfort in relinquishing control over previously proprietary processes while implementing capabilities that allow offshore processes to be measured and improved over time. Still, one of the key attributes of successful offshore initiatives has been process standardization. Service providers have invested significant resources in ensuring consistency and standardization in development and delivery processes as an important tool in managing the complexity of the global delivery model. This attribute has proved valuable in the realm of IT services, but in business process support this attribute may negatively affect an organization’s ability to innovate and stay competitive. The disciplines of program and process management must address the advantages and challenges presented when part or all of a project moves offshore, and the management needs to develop and disseminate best practices for achieving project success as well as cost savings. As enterprises accelerate their offshore BPO initiatives to include increasingly more core processes, they begin to risk their ability to experiment and innovate, while trying to standardize and optimize.

The nature and magnitude of these challenges differ depending on whether an enterprise chooses to build its own offshore capability directly or to develop an indirect relationship with an onshore or offshore service provider to access offshore resources.

**Management Practices**

For both individual enterprises and the service providers, offshore relationships challenge the staffing, style, and formal and informal information systems of organizations that implement them. Particularly, HR departments would be required to become more adept at managing disparate workforces and incorporating stylistic and cultural differences in communicating and problem solving. It becomes critically important for management to create policies and practices to incorporate a more flexible approach to labor allocation. Regulatory and legal issues also come increasingly to the fore as countries deal with the political issues that offshore sourcing is raising. Thus it is imperative the organization supports relationships with offshore players and assure that objectives, contracts, delivery models, and measurement are aligned.

**Recommendations: The Future of Offshore Business Process Outsourcing**

Offshore BPO will continue to grow steadily for years to come. In light of such phenomenal growth and competitive opportunities that offshore BPO provides, there are basic preparations and investments clients and suppliers can make before they take the next step. Base your decisions in the short and medium term on risk tolerance, control issues and supplier maturity.
**Client Recommendations**

- **Help build the market:** The offshore BPO market is changing rapidly. Companies that are serious about the opportunity should figure out ways to help it mature. Clients have to either set-up their own operations or help suppliers succeed in this segment.

- **Use an expert:** Whether internal or external, someone who has been there before can prevent many of the unexpected challenges along the way.

- **Focus on building the solution:** Spend time thinking of the right solution and give the supplier flexibility to innovate rather than just focusing on service levels.

- **Knowledge transfer:** Help the offshore resources understand the business process and its integration with the rest of the organization. Focus on the role of the business process and not just its mechanics.

- **Invest in management:** Management of offshore BPO requires a different approach. Offshore BPO is not as mature as offshore ITO, therefore there are less experienced managers. Companies need to focus on not only program management (relationship, performance, resource, contract and financial), but also transition management and change management.

- **Know your own service levels:** Before building an offshore strategy companies need to fully understand their process improvement opportunities and create the metrics to gauge success. As offshore BPO is relatively new, industry best practices are yet to be established.

**Supplier Recommendations**

- **Service level compliance:** When it comes to adhering to stringent Service Levels (SLs), offshore BPO suppliers do not have much experience, their process maturity is lacking. Only the suppliers that have process maturity will survive.

- **Domain expertise.** Suppliers in the offshore BPO space do not have enough domain expertise to commit to process improvements or process transformations. Help clients to implement best practices and share the risks and rewards for such changes. Suppliers are not mature enough to manage this on their own.

- **Focus is key.** Stop trying to be all things to all people. As the market matures, specializations in verticals, or specific BPO offerings, will be critical.

- **Build strength, not volume.** Develop client-specific capabilities, expertise, experience, disaster recovery plans, robust infrastructure, costing models.

- **Invest in people.** Set up effective training processes to ensure retention, productivity as well as a steady stream of trained professionals. Offer incentives to keep your best people.

- **Customize pricing.** Figure out a way to offer varied pricing models (risk & reward, time and materials) to stay competitive.

- **Invest in R&D.** In order to better understand client needs, develop stronger process models, domain expertise, vertical expertise, higher level project managers, enhanced collaboration tools and processes, enhanced program management, services assurance.
Contact Information

For more details about neoIT’s offshore advisory and management services, please contact:

Allisson Butler
Marketing Director
San Ramon, California
allisson@neoIT.com
925-355-0557
www.neoit.com

neoIT Global Headquarters
2603, Camino Ramon, 2nd Floor
San Ramon, CA 94583 USA

neoIT Asia Headquarters
210, Bellary Road
Upper Palace Orchards
Bangalore 560 080 India