**School of Economics
and Management**
Lund University

Department of Business Administration

Optimizing Business Process Outsourcing –
Three Dimensions of Outsourcing Success

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'Imagine the improvement in company performance – and in the economy as a whole – if all the energy expended in "pleasing the Street" were redirected toward the factors that create true economic value.'

Michael E. Porter 2008

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Abstract

Within inter-organizational relationships and governance the concept of risk management has become a key issue. The importance of generating and sustaining competitive advantage through inter-organizational relations has become more crucial, due to the emerging business model business process outsourcing (BPO). Nowadays, this business model facilitates companies' attempts to improve and support their operational effectiveness and strategic position. Therefore, it is intended to elaborate if relational risk mitigation solely determines outsourcing success and how BPO engagements are optimized.

The outcome of this thesis will rest on the significance of relational risk mitigation to optimization of BPO efforts, which is approached through three case studies that incorporate different viewpoints. These perceptions represent the advisor perspective, the client perspective, and provider perspective that will triangulate the issues of BPO optimization and outsourcing success. We believe that looking beyond relational risk mitigation and contractual governance, and include integrated management control systems and strategic fit will result into a higher degree of outsourcing success and result in optimization of business process outsourcing.

Key words: Business Process Outsourcing, Optimization, Satisfaction, Operational Effectiveness, and Sustained Competitive Advantage.

Preface

The presented thesis will answer for our Master's dissertation at the Department of Business Administration within the School of Economics and Management, Lund University. This degree project in Corporate and Financial Management seeks to capture the very essence of Business Process Outsourcing from a strategic point of view, which gives insight in how outsourcing efforts are optimized.

The authors would like to acknowledge the representatives from the case companies for their valuable contribution in the form of qualitative interviews.

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Executive Summary

Course:	BUSM36 – Degree Project in Corporate and Financial Management
Level:	Master, D-level
Title:	Optimizing Business Process Outsourcing – Three Dimensions of Outsourcing Success
Authors:	Van Engelen, Q., Enlund, V. & Shwan, A.
Supervisors:	Kedström, C. & Kjellström, E.
Statement of Purpose:	The purpose of this thesis is to elaborate if relational risk mitigation solely determines outsourcing success and how BPO engagements are optimized. The intended outcome of this thesis will rest on the significance of risk mitigation to optimization of BPO efforts. Outsourcing perceptions that go beyond satisfaction may be in order to fully understand and grasp the nature of BPO optimization.
Research Questions:	*Is solely relying on relational risk mitigation sufficient when optimizing business process outsourcing. *How are business process outsourcing efforts optimized?

Methodology:

The research approach consists of three case studies that incorporate different viewpoints. The empirical data is derived from qualitative interviews with respondents that represent case study 1 the advisor perspective; case study 2 the client perspective; and case study 3 the provider perspective. The combined perceptions are intended to triangulate the issues of BPO optimization and outsourcing success.

Conclusion:

Collectively viewing sustained competitive advantage, operational effectiveness, and satisfaction as the optimal outsourcing success means that outsourcing initiatives cannot solely focus on relational risk mitigation and contractual governance. Therefore looking beyond relational risk mitigation and contractual governance, and include integrated management control systems and strategic fit will result into a higher degree of outsourcing success and result in optimization of business process outsourcing.

Key Words:

Business Process Outsourcing, Optimization, Satisfaction, Operational Effectiveness, and Sustained Competitive Advantage

Table of Content

Figures and Tables

I. Importance of Business Process Outsourcing

The chapter will present the thesis' problematical background in the course

of describing the importance of BPO, which is narrowed down to the reason

for examining BPO optimization. This is then clarified within the statement of purpose and through our research question.

1.1 Drivers of BPO Importance

The extensive growth within the business process outsourcing (BPO) industry gives evidence that outsourcing has become increasingly important as an emergent business model. Inter-organizational relationships, such as business process outsourcing have become more intense and important in these last decades. With outsourcing and BPO we mean the following: *breaking of large business processes from a company's value-chain, which are developed into independent entities with a client-provider relationship*. The industry profile of the Global Data Processing and Outsourced Services (2009) incorporates three industry segments, where 6.5 % represents electronic data processing (EDP), 50.4 % represents information technology outsourcing (ITO), and 43 % represents other business process outsourcing (BPO). The market value of the industry rose with 11.1 %, an increase from USD 365.1 billion in 2004 to USD 556.0 billion in 2008 (Global Data Processing & Outsourced Services 2009: 9-11). The appearance of this importance has become more visible due to the impact of the main drivers for this emerging business model. Globalization is one major contributor for the importance of inter-organizational dependency, thus resulting into inter-organizational relations becoming critical to achieve and maintain success. Fierce competition, customer shifts, and emerging markets have made outsourcing an important factor for corporations to position themselves differently, thus being more adaptable to changes through collaborations (Kraus & Lind 2007: 270-1). The increase in information technology development has changed information patterns and knowledge flows, resulting into rapid technological transformations, which is another driver for an intensification of inter-organizational relationships. This disables corporations to maintain in-house expertise and competitiveness through core-business activities because of lacking resources. Corporations are therefore motivated to outsource non-core activities so that resources could be reallocated to value adding activities instead (Kraus & Lind 2007: 271). The technical complexity of the products has also had its fair share on intensifying the importance of inter-

organizational relationships. This has given corporations the incentives to have closer ties with each other and jointly coordinating their efforts (Kraus & Lind 2007: 271-2).

BPO can improve and support a company's operational effectiveness and strategy. As mentioned above, BPO is a rapidly growing business model between organizations that involves firms taking over other firms functional operations and providing them with benefits and advantages, which could not be achieved by providing it in-house. *Operational effectiveness* can be achieved through superior performance of similar activities compared to a company's rivals, thus being able to utilize its resources better (Porter 1996: 61). Companies that outsource parts of their operations can gain operational effectiveness through: less expensive business process solutions; resources that can be allocated to core business processes; and superiority and effective performance (David 2007: 201). However, formulating a company's *strategy* the need of diversification becomes more significant (Porter 1996: 61-4). Strategy means performing core activities differently than its rivals or performing similar activities in different processes: 'Competitive strategy is about being different. It means deliberately choosing a different set of activities to deliver a unique mix of value' (Porter 1996: 64). Strategically companies that engage in an inter-organizational relationship with a external outsourcing provider can gain advantages, such as: aligning with an expert provider that outperforms the special task; adaptation and flexibility towards shifts in customer needs; and most importantly concentrating on value creating activities that is critical to sustaining competitive advantage (David 2007: 201). Hence, a company that decides to outsource must be able to create a valuable position, which involve a different set of value adding activities.

1.2 Optimization vs. Satisfaction

Strategy should not only determine which activities to perform and how they are configured, but should also determine how activities are fit together. According to Porter (1996) this is because *strategic fit* drives both competitive advantage and sustainability. However, it can only be achieved when rivals have a complex system

of interlocked activities to match. A position that is built on a system of activities becomes harder for rivals to outmatch when the system rests on activities that are consistent, reinforcing and activities where efforts are jointly optimized. For instance, having a high coordination effort with external providers can eliminate the performance risks (Porter 1996: 70-4), which are often recognized when engaging an inter-organizational relationship with an external outsourcing provider.

Within inter-organizational relationships and governance the concept of risk management has become a key issue. This is due to the degree of involvement from external providers. Recent studies reveal that the relational dimension between a client and vendor is vital to outsourcing success, but can also mitigate risk and keep contracts mutually beneficial (Alpar & Saharia 1995; Aubert *et al*. 2005; Dibbern *et al*. 2004; Klepper 1995; Lacity & Willcocks 1998, 2003; Lee & Kim 1999, 2003; Willcocks *et al*. 2004; Willcocks *et al*. 1999; Willcocks & Lacity 1999; and Willcocks & Margetts 1994). However, the common denominator for measuring outsourcing success has been fulfilled within the academic field through the term 'satisfaction', thus meaning that: '(…) the level of fitness between the customer's requirements and outsourcing outcomes' (Lee & Kim 1999). The contradictory factor when measuring outsourcing success with satisfaction is that in some instances solvable decision problems that are complex in nature need optimal decisions. This means that when deciding on engaging in a BPO vendor it often rely on decisions that are optimal: '(… decisions) that maximizes the expected outcome' (Encyclopædia Britannica 2009). It would therefore be of great significance within the studies of inter-organizational relationships and governance to elaborate on the significance of solely relying on relational risk mitigation to optimize BPO-engagements. The main theme within this thesis will be to contrast the optimization of BPO engagements and outsourcing success.

1.3 Statement of Purpose

The importance of gaining and maintaining competitive advantage through inter-organizational relations has intensified during the past decades. An emerging business model – BPO – has been composed to facilitate a solution to this effort that improves and supports a company's operational effectiveness and competitive advantage. As

companies outsource whole business processes the risk of not achieving success becomes higher due to the degree of involvement from external outsourcing providers. It is therefore important to elaborate if relational risk mitigation solely determines outsourcing success and how BPO engagements are optimized. The intended outcome of this thesis will rest on the significance of risk mitigation to optimize BPO efforts. Applications of more elaborative models that go beyond satisfaction may be in order to fully understand and grasp the nature of BPO optimization. The statement of purpose is clarified in the following two research questions.

* Is solely relying on relational risk mitigation sufficient when optimizing business process outsourcing.

* How are business process outsourcing efforts optimized?

1.4 Disposition

Within this chapter we have now presented the thesis' problematical background and statement of purpose, which has been clarified through our research questions. Next the thesis will put forward and present the methodological foundation and motivation of why research has been taken upon the field of inter-organizational governance. Afterwards, the theoretical framework will be presented where various theories, models and normative perceptions are clarified within the research of outsourcing and BPO. This is followed by the thesis' analysis, which investigates motives for outsourcing and BPO optimization. Finally, the authors will present their main conclusions, knowledge contribution and limitations, followed by some suggestions on future research within the studies of inter-organizational relationships and governance.

II. Why Research Business Process Outsourcing

This chapter will present why research is endured on the subject of BPO and how the research approach within outsourcing optimization is processed. Therefore a motivation on research significance and methods to take upon the research is augmented within this section.

2.1 Significance of Portraying BPO Reality

Influenced by the studies of corporate and financial management, we the authors were seeking a higher level of insight within the field of post-contractual (relational) governance within inter-organizational structures, such as those that are observable in outsourcing and BPO engagements. The considerable growth in *the global data processing and outsourced service-market* and the emerging importance of the business model had significance in the decision of choosing our research subject. Also previous academic experience and interest within the field of outsourcing in general resulted into the decision to deepen this knowledge.

After reviewing recent studies within the field that were relevant to our research theme it was founded suitable to decide on using these contemporary findings and examine if it had any bearing effect on the optimization of BPO engagements and outsourcing success. These new findings are referred to Wullenweber *et al*. (2008) research on mitigating outsourcing risk through relational dimensions and Blumenberg *et al*. (2009) research on the significance of contractual governance and its effect on relational quality and outsourcing success. The negligence to compute any considerations on how these findings may or may not optimize outsourcing and BPO outcomes incorporates the limitations of their research. Neither is aligning outsourcing success solely to cliental satisfaction sufficient enough. Not having any relation to operational effectiveness and sustained competitive advantage, which is created through integrated management control and strategic fit computes the credibility of their findings. This means that outsourcing efforts that only focus on satisfaction do not lead to operational effectiveness and sustained competitive advantage. Being the case outsourcing success cannot solely be relied on relational risk mitigation and contractual governance. The intention with examining this research subject is to portray the reality of the concepts and the models (see Lundahl & Skärvad 2009: 41) that is present within the field of BPO. Therefore

when researching the reality of BPO optimization we will be able to shed some light on outsourcing success.

2.2 Applied Research Approach

The research approach in our thesis is composed by an *adductive* relationship between *theory* and *empirics*. Therefore defining what is treated, as theoretical and empirical issues will be discussed first. According to Patel and Davidson (2003) the concept of experience can function as a synonym to empirics. Thus, what is characterized as empirical is the belief that knowledge is based on observing the reality (Patel & Davidson 2003: 18). The notion of theory is conceptualized as: '(…) a system of related concepts, which together portray an understanding. The theory exposes in which way the concepts are related to each other, which explains and foretells the understanding and the understanding of its significance' (Translated from Patel & Davidson 2003: 22).

The configuration of integrating theory and empirics when choosing an adductive research process is therefore structured through both *inductive* and *deductive* approaches. A deductive research process means that the research subject is drawn from theory and confirmed by empirical findings when observing the reality (see Patel & Davidson 2003: 18, 22; Bryman & Bell 2005: 25; Bryman 2006: 22). Contemporary theories by Wullenweber *et al*. (2008) and Blumenberg *et al*. (2009) will be tested of their significance, when applied to companies' attempts to generate and sustain competitive advantage. This is achieved through the construction of hypothesis that is related to the significance of relational risk mitigation. According to Patel & Davidson (2003) researchers can form a conducted investigation into a test of hypotheses if a problematic field is overwhelmed with theoretical knowledge. This will enable the following research to test if it constitutes a truthful description of reality. A hypothesis is: '(…) a linguistic proposition in which different concepts are related to each other' (Translated from Patel & Davidson 2003: 20). By constructing a hypothesis, the approach can create an explanatory research by developing and testing propositions. Therefore this applied research approach or level of research is consistent with Carney's (1990) *Ladder of Analytical Abstraction*. A research approach is sufficient if it is designed for testing a hypothesis and reducing the variety of the data for analysis of any tendency (Craney 1990; in Miles & Huberman 1994: 92). The thesis' hypotheses are illustrated as followed.

﹡ H0. Solely relying on relational risk mitigation is sufficient to optimize business process outsourcing.

﹡ H1. Solely relying on relational risk mitigation is not sufficient to optimize business process outsourcing.

Nonetheless, the empirical findings are then tested if any disclosure can be done regarding the optimization of BPO engagements and outsourcing success. Thus, the inductive research process will be constructed through the integration where empirical observations of reality are exposed to explanations that foretell the understanding of BPO efforts, which result into the optimal outsourcing outcome (see Patel & Davidson 2003: 18, 22; Bryman & Bell 2005: 25; Bryman 2006: 22). This means that if the hypothesis H0. is rejected and H1. is confirmed, outsourcing success should not only incorporate one dimension, but also others. This way new knowledge will enable outsourcing parties to look beyond satisfaction as an outsourcing outcome.

2.3 Case Studies that Triangulate the Nature of BPO

The strategy for applying our research approach is to study cases that facilitate conceptualized information on the outcome of outsourcing efforts and BPO engagements. Research that is based on case studies can be interpreted as: 'investigation of a limited group. A case could be an individual, a group of individuals, an organization, or a situation' (Translated from Patel & Davidson 2003: 54), which is also acknowledged by Lundahl and Skärvad (2003). However, their view on case studies is that the investigation only incorporates one or a few cases, which is or are, studied more in detail and with multiple dimensions (Lundahl & Skärvad 2003: 187). Three different representatives from three different organizations compose the case studies in this thesis. The representatives are chosen for their common interest for outsourcing and BPO, which is differentiated from their specific point of view and their organizations standpoint. These case studies are applied to gather the empirical material. To gain the empirical data, qualitative interviews have been chosen as the research method. This approach gains a deeper and more thorough knowledge base with a few respondents than other approaches, such as quantitative research methods e.g. questionnaire surveys. The main reason for choosing the empirical gathering

through qualitative case studies and in-depth interviews was to strengthen the relevant data from the respondents that facilitated conceptualized information that is embedded within the studied case companies *modus operandi*. Additionally the research method also enables the identification of concepts and patterns that are related to each different theoretical theme that are presented in the thesis. Meaning that focus on linguistic contexts of the gathered empirical data can be achieved, which constructs a tool that provides a higher possibility to investigate the subject in matter more deeply (Bryman & Bell 2005: 40).

Bearing in mind that every qualitative research is unique and may vary from one to another, Patel and Davidson (2003) recognize a general problem regarding validity. Problems can evolve within a qualitative approach when gathering information, analyzing information, communicating and presenting the result. The quality of validity is enhanced within a qualitative approach through the method of triangulation. Triangulation can be applied for gathering empirical data from various methods (Patel & Davidson 2003: 102-4). In some instances triangulated research strategies can result into contradictory results. Bryman and Bell (2005) present the two main arguments against a combined method strategy. *First*, there is a perception that different research methods are built on differing foundations. *Second*, there is a perception that quantitative and qualitative researches stand for different paradigms (Bryman & Bell 2005: 501). However, triangulation can create validity when research is applied to different empirical sources. Meaning that empirical data is gathered from different people, places or timeframes where the actual research subject is expressed (Patel & Davidson 2003: 104). Thus, using the same method fore the three different case studies, i.e. in-depth interviews, the effect of contradictory results from the triangulated approach is minimized. Validating the research from different empirical sources is another advantage when approaching the research question and the constructed hypothesis through a triangulated research strategy. Names omitted for privacy reasons, however short descriptions of the representatives in our case studies are presented next.

2.3.1 Case I – The Advisor Perspective

The advisor case company (Company A) is an organization of 70 associate firms that has a global reach and is operating in nearly 150 countries. Company A provides a

broad range of professional services including audit, tax, consulting and financial advisory services. The company provides its services to all major sectors and targets national and middle market enterprises, public institutions, privately owned companies and public sector organizations. The consulting division is engaged in providing services to clients across the world within strategy, operations, technology, human resources and outsourcing consulting services.

Company A's representative that was interviewed (2009-05-07) is a *Senior Manager* within the company's subsidiary that is located in Stockholm, Sweden. The representative has been a consultant for 10 years, where the representative has worked with *shared services*, *outsourcing advisory*, *change issues* and *transformation challenges* regarding finance functions and with some focus on other business processes. This expert representative has been chosen to facilitate the advisor perspective regarding outsourcing and BPO issues. Before working as a consultant the representative worked within finance related functions, such as a controller and other operational functions for major international companies. However, the representative has been with Company A since 2002.

2.3.2 Case II – The Client Perspective

The client case company (Company C) is the holding company for one of the world's largest electronics companies and has subsidiaries in over 60 countries across Europe, Africa, North America and Asia Pacific. The company's business is separated into three major segments, which are consumer electronics, medical systems, and lighting. Company C has also joint ventures and alliances with various companies around the world. The company was established in 1891 where the founder started manufacturing incandescent lamps and other electrical products.

Company C's representative that was interviewed (2009-05-12) is a *member of the executive management board*, which is located in the Amsterdam, Netherlands. The representative joined Company C in 1973 and has worked for the company around the world in a number of key management positions. This expert representative has been chosen to facilitate the client perspective regarding outsourcing and BPO issues. The client representative entered the position in 2006, but is currently retired.

2.3.3 Case III – The Provider Perspective

The provider case company (Company P) is one of the leading providers of consulting and outsourcing services through a global delivery network of over 53 centers in the world. The company's business is structured around five operating groups, which incorporates products, communications and high tech, financial services, resources, and public service. Company P has experience and capabilities across most of the industries, business functions and operates in more than 52 countries. Their offerings fall under three segments, such as consulting, systems integration and outsourcing.

Company P's representative that was interviewed (2009-04-27) is *Chief Operating Officer* for the System Integration and Technology organization at Company P's subsidiary located in Copenhagen, Denmark. The provider representative coordinate, assures project quality, and allocates resources to projects regarding IT consulting, application maintenance and application outsourcing issues. This expert representative has been chosen to facilitate the provider perspective regarding outsourcing and BPO issues.

2.4 Qualitative Approach of Interpreting Existence

The research method to gather the empirical data, as previously mentioned by means of qualitative interviews, has been conducted in a *semi-structured* approach. This facilitates a combination of predetermined questions and spontaneous remarks relating to a respective subject. Further, the interviews will aspire to identify unfamiliar characteristics and phenomena on the subject (Kvale 1997: 36) of outsourcing and BPO. The aim of the interviews is to gather qualitative empirical data regarding if outsourcing success can or cannot solely be relied on relational risk mitigation and contractual governance. These interviews will enable us to shed some light on the nature of outsourcing success. Accordingly, this approach will give room for both the interviewer and the respondent to talk freely and come with insightful knowledge within the research subject (Bryman & Bell 2005: 363).

The qualitative empirical data must also be studied, interpreted and understood in a scientific manner. The perspective of hermeneutics or interpretivism enables researchers to understand other human beings and real situations through interpretation of existence that comes to exist in speech, script, human behavior, and

perception (Patel & Davidson 2003: 29; Bryman & Bell 2005: 29). This perspective will function as the fundamental foundation for qualitatively approaching the research subject and interpret its existence, which is primarily achieved through interpreting the subjective perceptions that are derived from the respondent's interpretation of theoretical models, statements, and experiences during the interviews. Thus, resulting into a conceptualization of BPO and outsourcing that is aligned with the specific organizations opinion and their way to handling BPO in practice, thereby achieving significant level of objectivity.

2.5 Research Complications and Methodological Limitations

In some instances a hermeneutic perspective can generate complications that are essential for the research process and the research outcome of this thesis. We as authors and researchers face complications regarding the mutual understanding of the theoretical models and statements in our interview discussions and sessions between the representatives and us. Complications can also arise when we interpret the interview respondent's replies. Nevertheless, because of the importance to understand and interpret through a hermeneutic perception within a qualitative research approach (see Patel & Davidson 2003: 29; Bryman & Bell 2005: 29), we as researchers deliberately must interpret the existence in a truthful manner by understanding the interviews in the most reliable way as possible. To minimize these critical complications an open communication between the interview respondents and a consistent interpretation regarding outsourcing and BPO issues is needed. This is facilitated through conducting our interviews in a semi-structured manner (Bryman & Bell 2005: 363). Meaning that the open discussion with the representatives can straighten misunderstandings when conducting the interviews, thus resulting into the generation of insightful empirical data.

III. Business Process Outsourcing

In this chapter we will finish off with a discussion on relational risk mitigation and management control systems from a strategic point of view

to give a theoretical insight on what proportions BPO optimization is based on. Nevertheless, we will commence with the determinants that outsourcing decisions are based on and follow with measurements of outsourcing success.

3.1 Cliental Outsourcing Evaluation

Reasons to outsource are currently discussed from two influential theories, *transaction cost economics* (TCE) and *resource based view* (RBV) (McIvor 2009). The TCE-approach determines what constitute the most efficient governance structure from the properties of the transaction, such as BPO transactions between external outsourcing provider and outsourcing client. The focus on governance structure is mainly concerned with cost reducing mechanisms associated with contractual hazards, such as opportunism, rationality, and so forth, meaning that the BPO engagement is decided from a cost management point of view. The TCE-approach argues that the transaction specific cost should determine if an economic exchange is to be managed internally or externally. Conversely, it ignores the complexity of organizations through too narrow assumptions regarding asset specificity, uncertainty and frequency (Williamson 1975, 1979, and 1985). The RBV-approach acknowledges the firm as a collection of different resources, assets and capabilities that can create competitive advantage if engaged distinctively. The RBV-approach has been criticized for its lack in determining value creation and is often used for complementary means (Priem & Butler 2001: 36). However, according to the RBV, for resources to become the capability that creates competitive advantage it must meet a number of criteria. This will determine if the resources are to be managed inside or outside the company. The criteria that the resource or capability must match up to be valuable, rare, un-imitable and fit the organization (Barney 1995, and 2001). In some instances the different approaches can be contradictory, which is illustrated in the following figure.

Figure 3.1: Complementary and contradictory perceptions of the RBV and TCE in outsourcing decisions (Retrieved and customized from McIvor 2009: 61)

Resource Position			
	Superior	*Contradictory* RBV – Perform Internally TCE – Outsource	*Complementary* RBV & TCE – Perform Internally
	Weaker	*Complementary* RBV & TCE – Outsource	*Contradictory* RBV – Outsource TCE – Perform Internally
		Lower	Higher
		Potential for Opportunism	

According to the presented figure, the following propositions are offered regarding outsourcing decision. If an activity in which an organization has a superior resource position and where there is lower potential for opportunism, the RBV-approach would prefer to manage the activity internally whereas the TCE-approach would more likely prefer to outsource the activity. If an activity in which an organization has a weaker resource position and where there is higher potential for opportunism, the RBV-approach would advocate outsourcing whereas the TCE-approach would advocate internal management of that specific activity. In some instances both theoretical approaches are complementary to each other. Both the RBV- and TCE-approach would advocate outsourcing if an activity in which an organization has a weaker resource position and a lower potential for opportunism. Conversely, both approaches would prefer internal management if an activity in which an organization has a superior resource position and higher potential for opportunism (McIvor 2009: 60).

The above argument puts forward valuable criterions for clients that are considering BPO-engagements. However, no elaborative context on how outsourcing providers can be capable to strategically fit with an outsourcing client is taken into consideration. Neither are propositions on how business value can be created through strategic fit in an outsourcing relationship given. Hence, a discussion on business value enablers within outsourcing is needed to fully understand the nature of

outsourcing relationships between clients and providers. First we will discuss on what kind of capabilities outsourcing providers must have in order to optimize their outsourcing competency.

3.2 Providers Outsourcing Competency

To understand external outsourcing providers' competencies, regardless of their specific areas of expertise they withhold three main key areas. These are *delivery*, *transformation*, and *relationship* (Feeny *et al*. 2005). Delivery competencies include the external outsourcing provider's response to outsourcing client's demands and therefore expose their service scope and service complexity. Transformation competencies signify the level of the provider's responsiveness to the client's anticipation that the processes they outsource will advance and help improve their operational effectiveness. One crucial advantage that external outsourcing provider experience is the growing post contractual bargaining power that builds up over time, by increasing the dependency of the outsourcing relationship. This creates an importance of relationship competencies, which refers to the outsourcing provider's willingness to maintain a good relationship that creates mutual beneficial pre-contractual agreements where the bargaining power is higher for the outsourcing client (Feeny *et al*. 2005: 42).

The normative proposition is that outsourcing client's demands and conditions will determine what bundle of capabilities they are looking for. Depending on the degree of operational service needs, service improvement needs and long-term viability needs, outsourcing clients may select valuable capabilities or characteristics from the external outsourcing provider that will lead to different outcomes of the BPO. External outsourcing providers can incorporate twelve unique capabilities that differ in relevance for the client (Feeny *et al*. 2005: 43). These key competencies and relevant capabilities are presented in the figure 3.2.

Figure 3.2: Twelve Capabilities of Outsourcing Providers (Retrieved and customized from Feeny *et al*. 2005: 45)
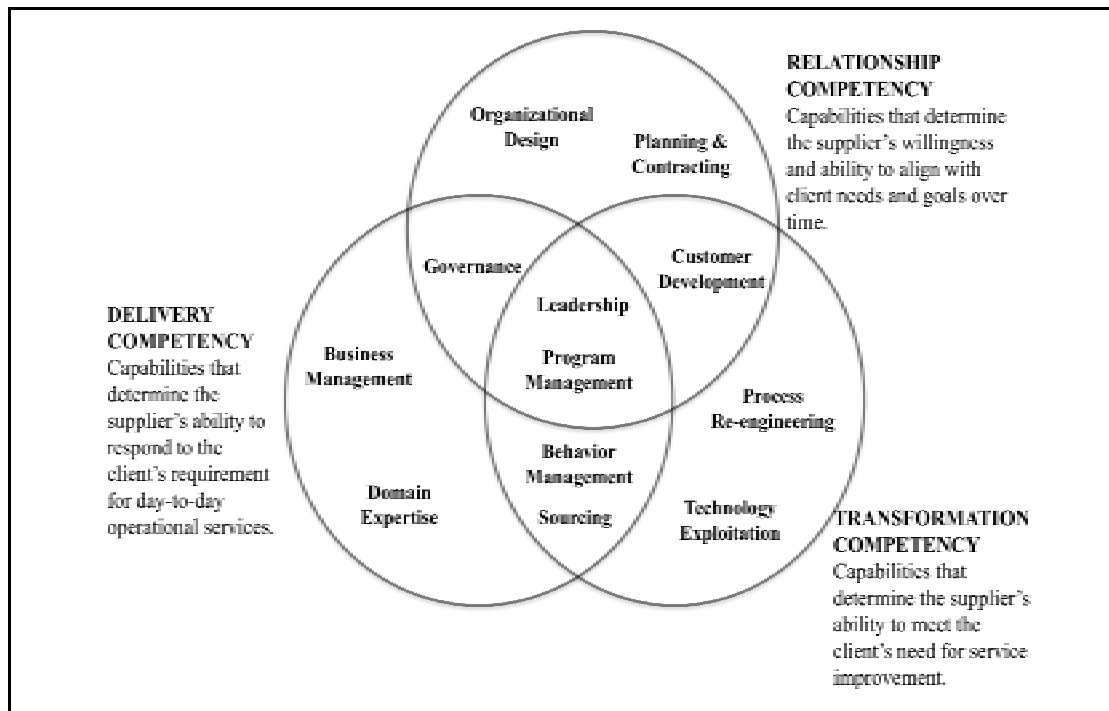
The above figure illustrates the different capabilities that are necessary for outsourcing providers. *Domain Expertise* refers to the external outsourcing provider's capability to apply and retain sufficient knowledge and skills of the target process that is required of the outsourcing client. *Business Management* is related to the provider's capability to meet the service level of the agreement with the client and its own business plans. *Behavior Management* relies on the provider's qualitative side, such as moral, motivational ability and people skills. *Sourcing* refers to the provider's capacity to fill the resources required to meet the client's targets. *Technology Exploitation* is related to the ability of the provider in deploying technology to improve and support outsourcing service targets. *Process Re-Engineering* relies on the provider's ability to design and implement changes to the business process that meet the improvement targets of the client. *Customer Development* refers to capabilities that ease the client's need of user-to-costumer transition, meaning that customers are developed in order to facilitate any transformation of competency, which requires relational criteria e.g. developing trust. *Planning and Contracting* is related to the external outsourcing provider's relationship competency regarding the ability to develop and execute mutual beneficial contracts and business plans. *Organization Design* relies on the capability to execute business plans through organizational structures and processes. *Governance* is related to the provider's ability

to jointly (with the client) review, evaluate and take corrective actions regarding the outsourcing outcome. *Program Management* refers to the capability of the provider's project management and their level of prioritization, coordination, and mobility that is required when looking into the long-term relationship. Regardless of the perceived *leadership* context that is linked to governance capabilities more effective providers exercise leadership in a more direct fashion (Feeny *et al.* 2005: 43-7).

Bundled together in different ways these capabilities will result into the provider's competency that is specifically relevant to the client. However, propositions on how business value can be created through strategic fit in an outsourcing relationship are still required for understanding the nature of outsourcing relationships between clients and providers.

3.3 Business Value Creation as Outsourcing Outcome

The reasons for outsourcing have shifted from a cost management perspective to a business value perspective (Weeks & Feeny 2008), resulting in strategic fit becoming more significant in outsourcing relationships than before. The view of external outsourcing providers being able to infuse external perspectives and new knowledge to clients that may contribute to creating business value, drive decisions regarding outsourcing issues. Value creation is for that reason a critical issue for most companies, which result into business value and competitive advantage. Potentially the quest of value and innovation is categorized and incorporates issues in *operational-*, *business process-*, and *strategic levels* where value-adding outputs can be formed. The optimal outcome is to create a better business through outcomes such as new business value, partnership development, and exploration of new ideas (Weeks & Feeny 2008: 130-5).

Understanding the key enablers of business value becomes an essential approach to determine outsourcing outcome. There are three critical enablers that determine the outsourcing outcome. These are *client enabler*, *provider enabler* and *relationship enabler*. Client enablers are composed of different set of determinants for a successful outsourcing outcome, such as *technology skills* (important to have a common base of prior related knowledge between partners, which is necessary for the transformation of new ideas), *selective sourcing mindset* (important to have the best breed of providers for an activity, thus enabling a client to recognize a portfolio of activities to decide from), *organizational alignment* (important to have a match between a specific business process and the corporate structure), and *leadership* (important to have a executive level of leadership to enable e.g. organizational alignment) (Weeks & Feeny 2008: 135-8).

Provider enablers are composed of two sets of categories, although basic ones, such as technology and management skills, and operational innovative applications are taken for granted. *Business process design knowledge* is important for the provider to create a platform so that prior related knowledge can result into a higher level of transformation regarding new ideas and innovation. *Client-industry scope* of the provider determines what external knowledge that is brought to innovation initiatives (Weeks & Feeny 2008: 139).

The relationship enablers are composed of three categories, such as a *high level of trust* (important to have within an outsourcing relationship, both before and after an outsourcing contract is signed creating personal trust, competence-based trust, and motivational trust becomes a critical issue), *high levels of measurement specificity* (important to have when monitoring detailed value adding activities), and *effective innovation governance* (important to have when determining what ideas to invest in, what processes should be used to mange implementation, and how success should be rewarded) (Weeks & Feeny 2008: 141-2). These key enablers of business value creation are important determinants for an outsourcing outcome, which is illustrated in figure 3.3.

Figure 3.3: Achieving Innovation in an Outsourcing Relationship (Retrieved and customized from Weeks & Feeny 2008: 136)
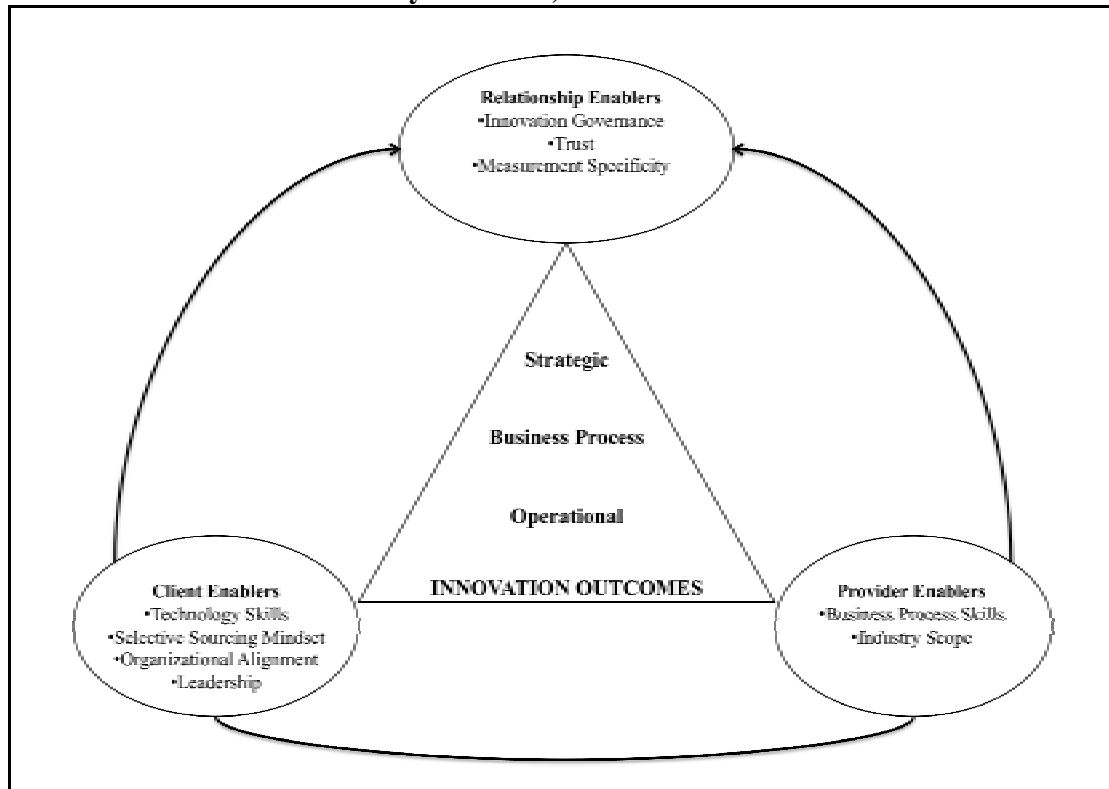
The figure highly illustrates how three key category sets of enablers determine outsourcing relationships potential to create innovations and business value. The relationship enablers are important factors for both client and provider that are engaged in a BPO, because it deliberately facilitates a level of alignment between clients and providers. First, the improvement of operational effectiveness is achieved through superior business process performance and superior operational performance. Second, it supports the strategy in ways where the outsourcing relationship results into the creation of business value through the alignment of reinforcing and optimizing activities. It could therefore seem that mitigating relational risk between organizations can improve and support key enablers from both parties when engaging in a BPO agreement. In doing so, a higher degree of outsourcing success can be experienced, due to the fact that all levels, such as strategic, business process, and operational outcomes are related to the quality of the relationship. However, we will therefore examine if relational risk mitigation solely is sufficient when striving to optimize the outsourcing outcome, later on in this chapter.

3.4 Contractual governance, Relational Quality and Outsourcing Success

Until now we have conceptualized and elaborated on how outsourcing providers can be capable to strategically fit with an outsourcing client and how a mutual beneficial outsourcing relationship creates business value can result into a higher degree of outsourcing outcome. Nonetheless, it is important not to forget that pre-contractual agreements and contractual governance is important in BPO engagements. According to Blumenberg *et al*. (2009) the view on how important the outsourcing contract is will consequently determine the level of relationship quality. The relationship quality then determines how successful the outsourcing outcome will be. This triple correlation is illustrated in figure 3.4.

Figure 3.4: The Impact of Importance (Retrieved and customized from Blumenberg *et al*. 2009: 2)
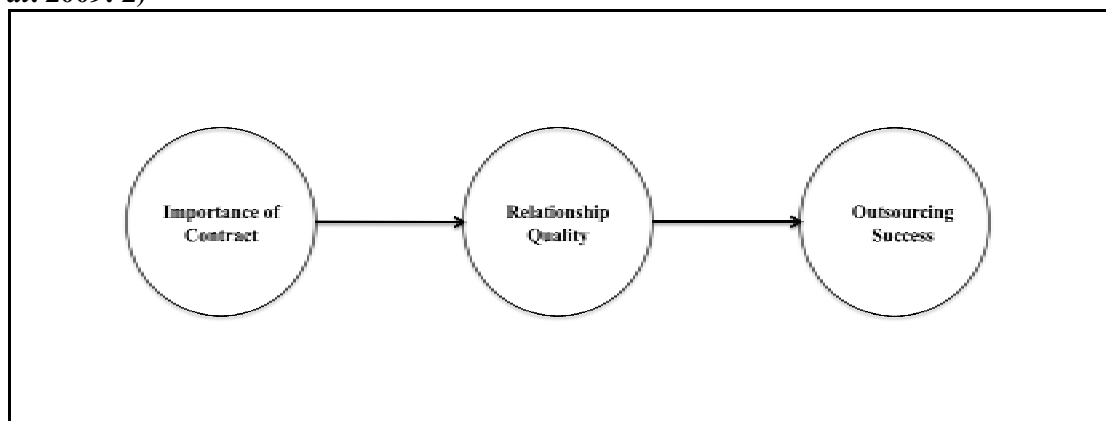
What is of importance in this recent study is that the quality of inter-organizational relationship have been related to the degree of outsourcing success and stipulates the importance of outsourcing has a positive impact on the quality of inter-organizational relationships (Blumenberg *et al*. 2009: 7-8). This does not mean that focus should either rest on contract design and governance, or on relationship development and governance, but rather cohesively considering how contractual issues will impact the outsourcing success through the level of relationship quality, which is indirectly formed when designing the contract.

A current report from *Deloitte Consulting Outsourcing Advisory Services* examined key dimensions of designing successful outsourcing. The proposed dimensions of that successful outsourcing design are concentrated in the following

five parts: rightsizing the deal; build a solid foundation; vendor selection now means something different; striking the deal; and after the deal is signed (Deloitte Development LLC. 2007: 7). The reports research overview is multi-sourced, meaning that outsourcing is analyzed through multiple perspectives, such as external outsourcing provider, outsourcing client, and outsourcing experts (advisors that have significant outsourcing knowledge). The last dimension that dealt with post-contractual agreements stipulates that problems within communications and relationship management were major factors that constrained outsourcing from becoming a competitive advantage for an outsourcing client. The proposed solution to this problem was to manage the relationship, monitor performance, and governance (Deloitte Development LLC. 2007: 23-5).

3.5 Measuring Relational Quality

When measuring the success of outsourcing multiple methods can be used to capture the outcome, such as realized outcomes, quantitative, economic, technological, and strategic dimensions (Lacity & Hirschheim 1993, Lacity & Willcocks 1998; and Grover *et al*. 1996). However, the common denominator for measuring outsourcing success has been fulfilled within the academic field through the term 'satisfaction', thus meaning that: 'the level of fitness between the customer's requirements and outsourcing outcomes' (Lee & Kim 1999).

Figure 3.5: Perceived Service Quality (Retrieved and customized from Parasuraman *et al*. 1988)
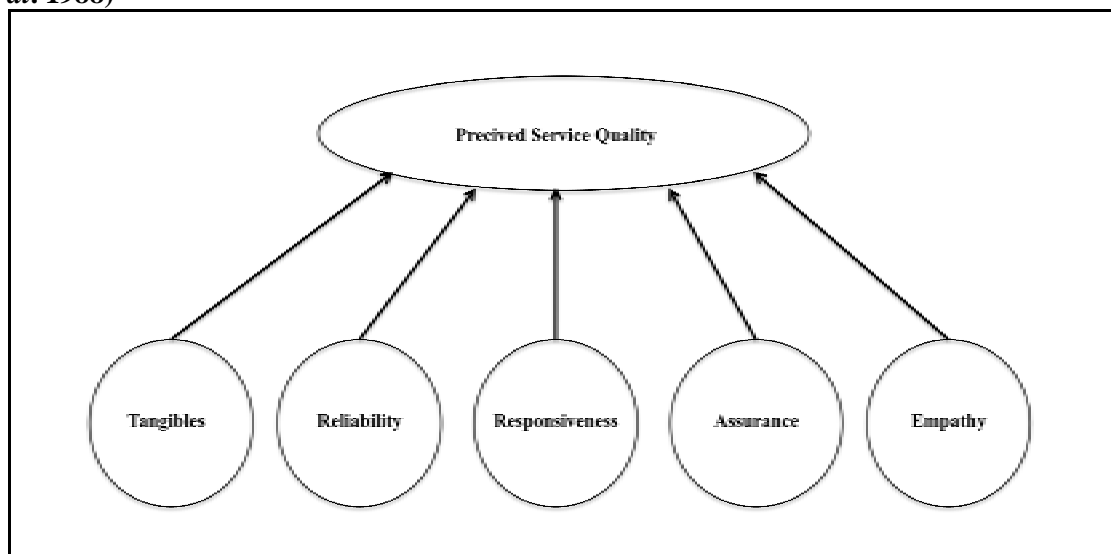
According to Parasuraman *et al*. (1994) quality is measured through five major parameters, may it be outsourcing quality or service quality, which are displayed in the figure 3.5 and table 3.1. They state that service quality is also measured through satisfaction. This is composed by the service that is *desired*: 'the level of service representing a blend of what customers believe "can be" and "should be" provided', and the *adequate* service: 'the minimum level of service customers are willing to accept' that is expected. In between this *zone of tolerance* the performance that a customer would consider satisfactory is represented (Parasuraman *et al*. 1994: 202).

Table 3.1: Scales for Measuring Service Quality (Parasuraman *et al*. 1994)

Reliability
* Providing services as promised.
* Dependability in handling customers' service problems.
* Performing services right the first time.
* Providing services at the promised time.
* Maintaining error-free records.

Empathy
* Giving customers individual attention.
* Employees who deal with customers in a caring fashion.
* Having the customer's best interest at heart.
* Employees who understand the needs of their customers.
* Convenient business hours.

Responsiveness
* Keeping customers informed about when services will be performed.
* Prompt service to customers.
* Willingness to help customers.
* Readiness to respond to customers' request.

Tangibles
* Modern equipment.
* Visually appealing facilities.
* Employees who have a neat, professional appearance.
* Visually appealing materials associated with the service.

Assurance
* Employees who instill confidence in customers.
* Making customers feel safe in their transactions.
* Employees who consistently courteous.
* Employees who have the knowledge to answer customer questions.

However, to capture the relational quality different models, and more longitude measurements must be taken into consideration. Liljanders and Strandviks (1995) model for relationship quality has four main characteristics (see figure 3.6. and table 3.2). *First*, it distinguishes between levels of interaction episode quality and levels of relational quality. *Second*, it comprises client satisfaction and the client's experience of value within a quality frame. *Third*, it enables an expansion of the traditional verification concept that is used in statistical models of perceived quality, thus including an amount of comparative norms. *Finally*, it takes client behavior into consideration (Liljander & Strandvik 1995: in Grönroos 2004: 98-103).

Table 3.2: Conceptualization of Relational Quality (Translated from Liljander & Strandvik 1995: in Grönroos 2004: 98-103)

Concept	Episode	Relation
Comparative Norm	All comparative norms.	All comparative norms except of predictive expectations.
Conformation	Direct or indirect recognition of the comparative norms.	Direct or indirect recognition of the comparative norms except of predictive expectations.
Effect	Experienced outcome of episode.	Experienced outcome of relationship.
Area of Tolerance	Acceptable variety of performance. Quality measurement.	Total acceptable of service effect in the relationship.
Cost	Perceived costs at level of episodes compared with explicit comparative norm.	Perceived cost of total episodes compared with explicit comparative norm.
Value	Episode quality compared to episode costs.	Relational quality compared to relational costs.
Satisfaction	Client's cognitive and emotive judgment of subjective experience of episode.	Client's cognitive and emotive judgment of subjective experience of total episode.
Image	Holistic view of service supplier; filtering the performance and the comparative norms. It also influences the component of attitude regarding commitment or engagement within a relation. All kind of bonding factors can color the firm positively and negatively. In particular the psychological bonding.	
Commitment	Refers to both parties' intentions and purpose for engagement; and their attitude toward their mutual inter play.	
Behavior	Client behavior and communication behavior (rumors, complains etc.). Loyalty that is based on the client's positive commitment is interpreted as having a strong relationship instead of basing it on continuing purchases. The bonding between provider and client also affects the behavior within the relationship. Using the same provider strengthens the bond between them.	
Bonding	Barriers that bonds a client to a provider, thus also establish the relationship. Bonding can take the form of legal, economical, technological, geographical, time based, knowledge based, social, cultural, ideological, and psychological.	

Figure 3.6: Relational Quality (Retrieved, customized and translated from Liljander & Strandvik 1995: in Grönroos 2004: 98-103)
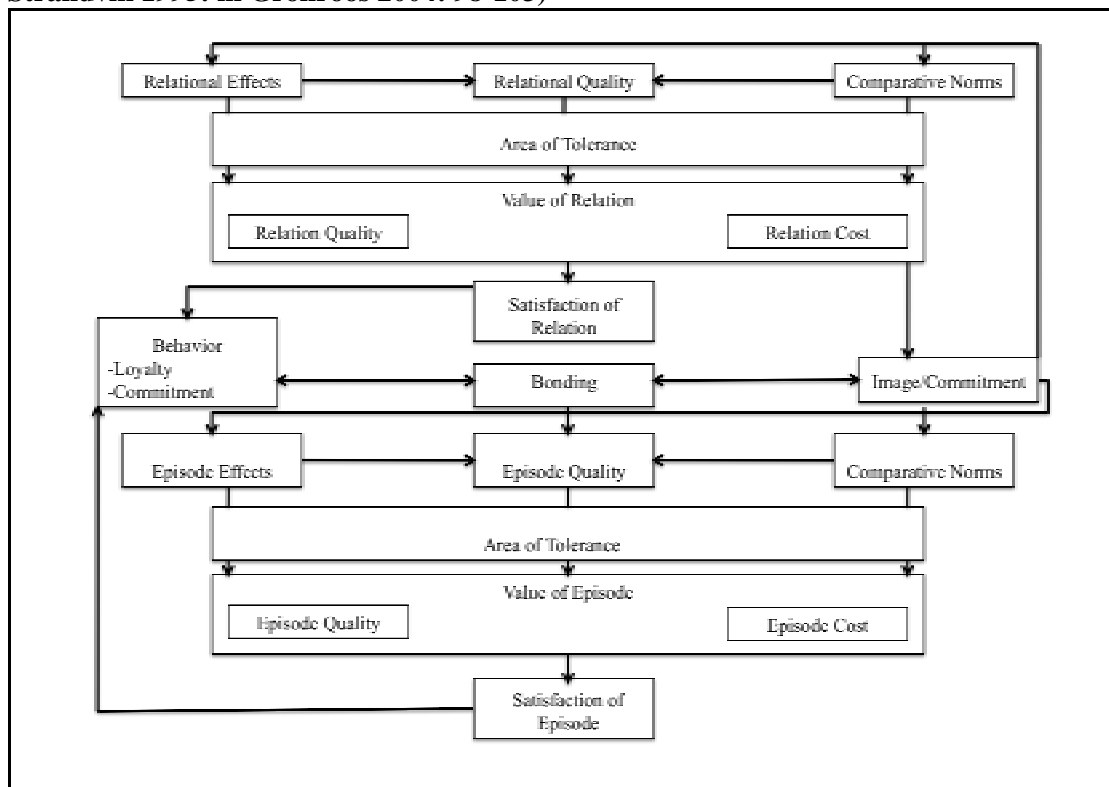
Reviewing the measurements of the outsourcing outcome both from a service quality and relational quality perspective the conceptualization of outsourcing success, as means of satisfaction is sufficient. However, this more complex model has been disregarded within research of outsourcing satisfaction within inter-organizational relationships. This is mainly referred to the research conducted by Wullenweber *et al.* (2008) and Blumenberg *et al.* (2009). Their research is conducted through scales of service quality and not relational quality, which means that episode quality is measured instead of longitude measurements that represents relational quality more accurate.

3.6 Mitigation of Outsourcing Risk through Relational Dimensions

Resent research show that relational processes can create risks that are critical for the outcome of outsourcing initiatives. This is an important factor for companies when deciding on BPO engagements. Previously stated, the concept of risk management has become a key issue within inter-organizational relationships, due to the degree of

involvement from external providers. In this thesis the broad definition of risk will be used meaning that: 'risk is understood as the potential for a negative outcome due to uncertainty about future developments, that has a known or estimated probability of occurrence' (Wullenweber *et al*. 2008: 2). Many researchers suggest that relational dimensions between a client and vendor are vital to outsourcing success, which also can mitigate the risks and keep contracts mutually beneficial. These risks can either be categorized as *financial risk* or *performance risk*. According to Wullenweber *et al*. (2008) financial- and performance risk is mitigated through four relational dimensions. It is supposed that high level of *trust* diminishes the financial risk of the outsourcing engagement. To mitigate performance risk *conflict resolution*, *communication*, and *cooperation* are significant factors, but are not equally important when mitigating the risk in matter. Conflict resolution is particularly vital to performance risk mitigation (Wullenweber *et al*. 2008: 4-6). When mitigating outsourcing risk (financial and performance) through relational dimensions, it is believed that a higher level of satisfaction will be perceived and experienced by the client (see figure 3.7).

Figure 3.7. Relational Risk Mitigation (Retrieved and customized from Wullenweber *et al*. 2008: 6)
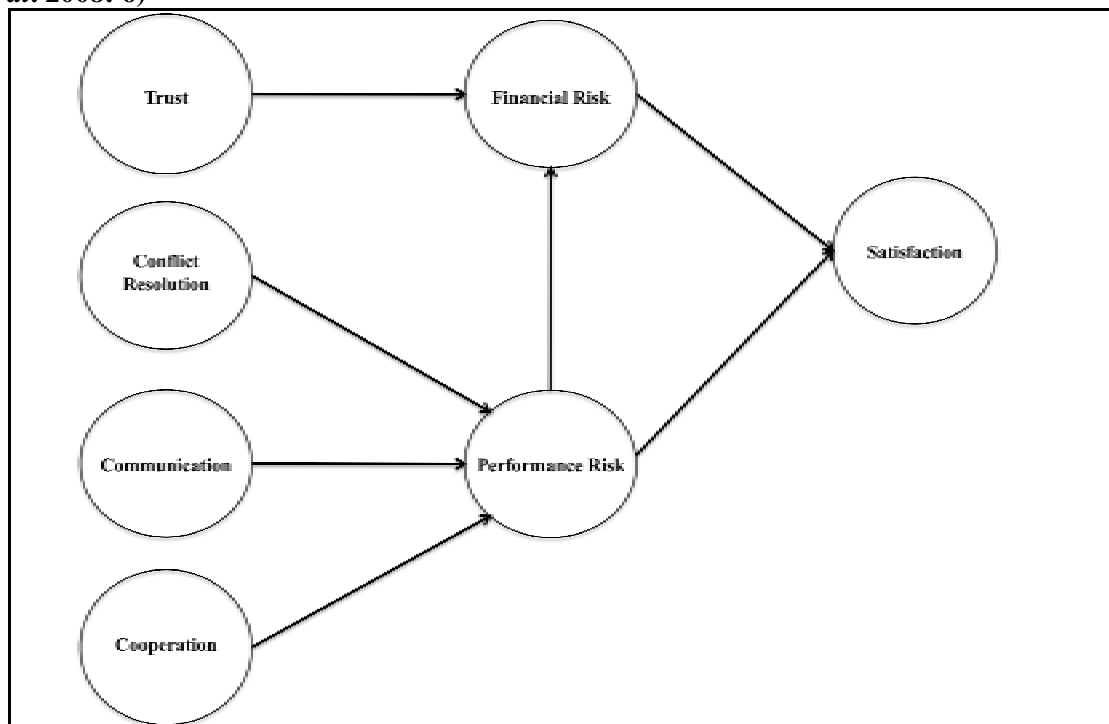
However, according to Van der Meer-Kooistra and Vosselman (2000) parties should share risks by making joint investments to prevent opportunistic behavior during a cooperation in which companies have a close relationship to each other. Companies may also find ways to share gain or loss of any improvement or deterioration of the transaction and so reduce the risks of opportunistic behavior (Van der Meer-Kooistra & Vosselman 2000: 55) that affects the degree of financial risk and performance risk.

3.7 Issues of BPO Optimization

It is therefore alleged that assessing BPO-engagements that both consider pre-contractual governance and post-contractual (relational) governance is essential if satisfaction is a desired outcome of an effort. Therefore efforts that diminish outsourcing risk will result into reduced complications when engaging in an inter-organizational relationship. However, this does not mean that diminished risk results into an optimal outsourcing outcome. If outsourcing optimization is a desired result, an outsourcing relationship should go beyond satisfaction measurements and also focus on management control and strategic fit.

Management control systems (MCS) will enable performance efficiency and activity monitoring, which helps organizations to achieve their objectives. Control is some what described as: 'Application of policies and procedures for directing, regulating and coordinating production, administration and other business activities in a way to achieve the objective of the enterprise' (Otley & Berry 1980: 232). With MCS the ability to adapt to external changes; face the increased complexity within the organization; minimize the fallibility of organizational members; and filling managements need to delegate authority. However, there are some common attributes that an effective MCS should demonstrate. These factors are demonstrated in figure 3.8. Designing a superior management control systems that is aligned to business processes will result into effectiveness (Hoque 2003: 50-2; Anthony & Govindarajan 2007: 98-104). Meaning that *operational effectiveness* can be achieved through superiority in performance, such as being able to utilize its resources better than rivals (Porter 1996: 61).

Figure 3.8. Effectiveness of Management Control Systems (Retrieved and developed from Hoque 2003: 50-1)
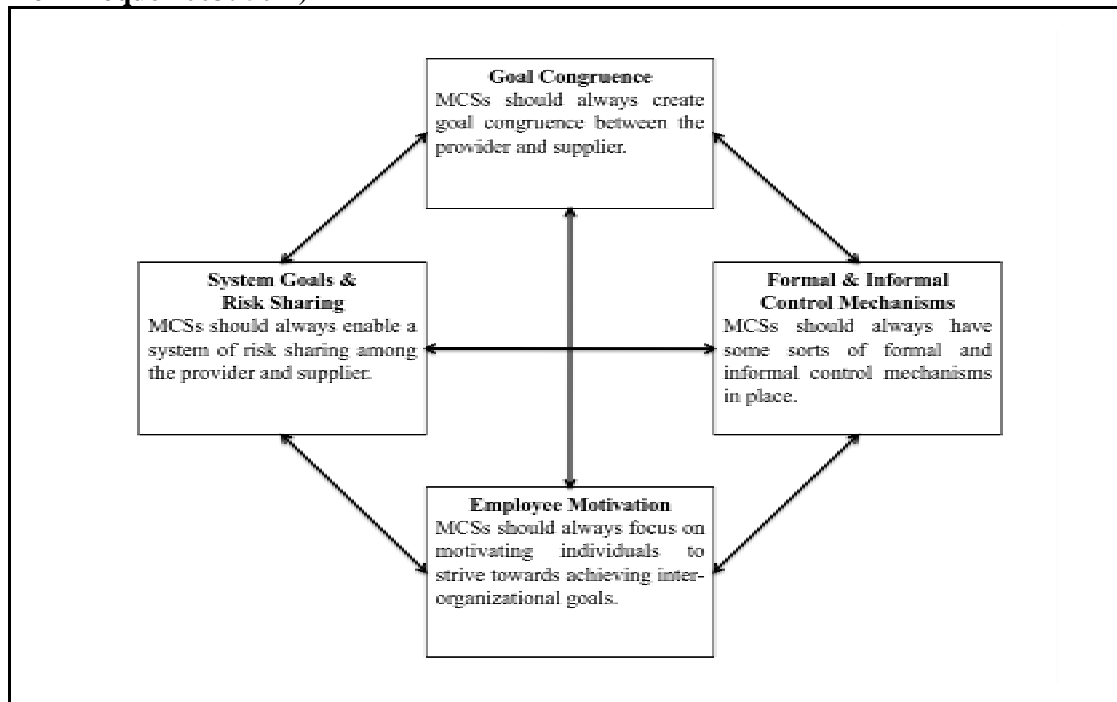
According to Porter (1996) operational effectiveness can only improve the performance of organizations while generating and sustaining *competitive advantage* will only result from superior strategy formulation and position (Porter 1996: 61-4). Strategy means performing core activities differently than its rivals or performing similar activities in different processes: 'Competitive strategy is about being different. It means deliberately choosing a different set of activities to deliver a unique mix of value' (Porter 1996: 64). However, for a strategy to be successful the internal environment of a firm (goal and values, resources and capabilities, and structure and systems) must be consistent with the firm's external environment. This brings us to the notion of *strategic fit* and *the basic framework for strategy*, which is a link between the firm and its external environment, e.g. including suppliers, providers and much more (Grant 2008: 13). Strategically companies that engage in an inter-organizational relationship with a external outsourcing provider can gain advantages, such as: aligning with an expert provider that outperforms the special task; adaptation and flexibility towards shifts in customer needs; and most importantly concentrating on value creating activities that are critical to sustaining competitive advantage (David 2007: 201).

As mentioned in the first chapter strategy should not only determine which activities to perform and how they are configured, but should also determine how activities are fit together.

Table 3.3. Strategic Fit Drives Both Competitive Advantage and Sustainability (Retrieved from Porter 1996: 70-2)

	Strategic Fit	
First-Order Fit	∗	Business activities and processes that are *consistent* among each other within a value-chain.
Second-Order Fit	∗	Business activities and processes that are *reinforced* among each other within a value-chain.
Third-Order Fit	∗	Business activities and processes that are *optimized* among each other within a value-chain.

This is because *strategic fit* drives both competitive advantage and sustainability. However, it can only be achieved when rivals have a complex system of interlocked activities to match. A position that is built on systems of activities becomes harder for rivals to outmatch when the system rests on activities that are *consistent*, *reinforcing* and activities where efforts are jointly *optimized* (see table 3.3). For instance, having a high coordination and information exchange effort with external suppliers and providers can also eliminate the risks of unsuccessful outcome (Porter 1996: 70-4), within an inter-organizational relationship.

The interpretation is that sustained competitive advantage, operational effectiveness, and satisfaction collectively is the optimal outsourcing success. Instead of solely focusing on relational risk mitigations and pre-contractual governance, both outsourcing parties should include satisfaction but also look beyond it. This means that outsourcing success should incorporate three dimensions instead of only one, which is illustrated in figure 3.9.

Figure 3.9. The Three Dimensions of Outsourcing Success
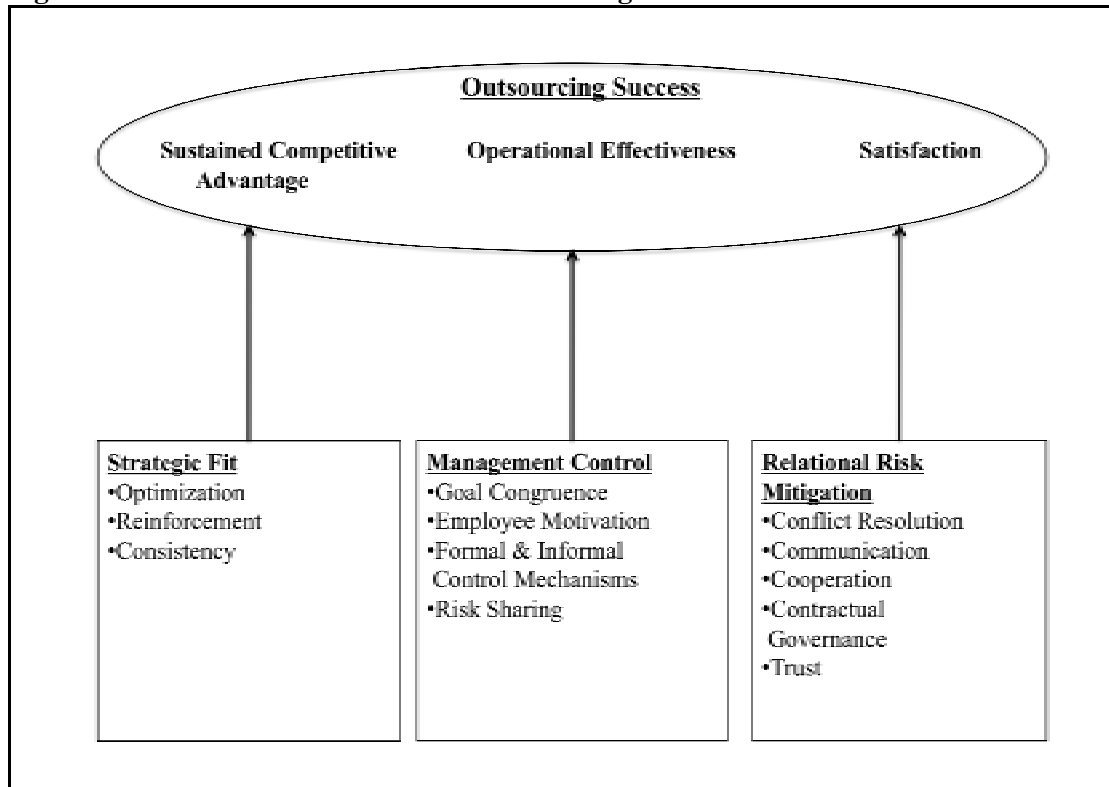
IV. Optimization of Business Process Outsourcing

In this chapter we will look deeper into the different outsourcing perspectives of selected outsourcing theory. This is related to the empirical data retrieved through conducted case studies of advisor, client, and provider perspectives. The combined perceptions are intended to triangulate the issues of BPO optimization and outsourcing success.

4.1 Motives for Outsourcing

'(…) many organizations attempt to actively inject new perspectives by bringing the outside in' (Hargadon 2003: 84)

According to McIvor (2009) motives for outsourcing – bringing the inside out – can be evaluated through two influential theories within the academic field of economics and management. The theories referred to are *transaction cost economics* (TCE) and *resource based view* (RBV). As mentioned earlier these theories can in some instances become contradicting and in other instances become complimentary. For clarification purposes these different situations are illustrated in table 4.1.

Table 4.1: Complementary and contradictory perceptions of the RBV and TCE in outsourcing decisions (Retrieved and customized from McIvor 2009: 60-1)

Resource Position	Potential for Opportunism	Differentiating results of outsourcing evaluation
Superior	*Lower*	* The RBV-approach would prefer to manage the activity internally whereas the TCE-approach would prefer to outsource the activity.
Weaker	*Higher*	* The RBV-approach would advocate outsourcing whereas the TCE-approach would advocate internal management of that specific activity.
Weaker	*Lower*	* Both the RBV- and TCE-approach would advocate outsourcing.
Superior	*Higher*	* Both the RBV- and TCE-approach would prefer internal management.

Advisor perspective: Company A distinguishes that the main reason for outsourcing is referred to as attempts of cost reduction. Through global research conducted by Company A, approximately *70 %* of companies are recognized as engaging in outsourcing solutions for cost reduction reasons. Another reason is to leverage a certain technology, thus being able to increase effectiveness and improve processes with more enhanced technologies, but also to standardize an activity or a business process across a corporate group, in an attempt to become more consistent or transparent. A last critical issue that is becoming increasingly apparent within outsourcing deals is that companies want to optimize their processes and create effectiveness within their operations (Outsourcing Advisor Representative 2009).

Client perspective: Company C has exercised outsourcing efforts differently in different divisions, some more than others, within the organization. Company C's representative states that outsourcing becomes an important issue if the external provider has superior capabilities compared to your in-house capabilities (Outsourcing Client Representative 2009).

Provider perspective: Company P recognizes several different reasons for companies when conducting outsourcing engagements. Most companies that engage in outsourcing efforts are looking at outsourcing as a solution for cost savings. Another reason for similar efforts in some cases is to gain control over a specific business process. Although this may initially seem like a paradox, the increase of control is caused by the larger number of levers you can pull in an outsourcing contract compared to internal leverage. Finally, outsourcing efforts can be engaged if the management of a client wants to focus attention on the core business activities (Outsourcing Provider Representative 2009).

Viewing the three different perspectives evidently acknowledges that outsourcing engagements becomes an effort if a company has a weaker resource position. This is mainly considered with the ambition of outsourcing attempts being motivated by leveraging a specific technology, rationalizing resource allocation, gain control, consistency, transparency or efforts of optimization, which is not achievable when doing it in-house. This means that a company who is considering outsourcing efforts is likely to engage if there are limited resources to perform that function or process effectively in-house. However, companies are not to forget issues regarding opportunism, if higher resource positions are desired outcomes within an outsourcing deal. This will be discussed later on in the chapter.

Being the case that outsourcing efforts are conducted for different reasons they have similar perceptions. This will consequently result into a critical evaluation and assessment regarding the significance of the outsourcing provider's competencies, resources and capabilities. Regardless of the outsourcing provider's specific competencies they contain three main key areas, such as *delivery*, *transformation*, and *relationship* (Feeny *et al*. 2005: 42). For clarification purposes these different competency areas are illustrated in table 4.2.

Table 4.2: Competencies of Outsourcing Providers (Retrieved and customized from Feeny *et al*. 2005: 42)

Competency	Key Area of Competency
Delivery Competency	∗ The level of the outsourcing provider responsiveness to outsourcing client's demand. Exposing their service scope and service complexity.
Transformation Competency	∗ The level of the provider's responsiveness to the client's anticipation that the processes they outsource will advance and help improve their operational effectiveness.
Relationship Competency	∗ The outsourcing provider's willingness to maintain a good relationship that creates mutual beneficial pre-contractual agreements where the bargaining power is higher for the outsourcing client.

Advisor perspective: Company A's representative acknowledges that companies with the desire of optimizing outcomes when considering outsourcing engagements are interested in the transformation competencies of the external provider. This means that issues of continuous improvements become more scrutinized when evaluating an outsourcing alternative. Nevertheless, delivery competencies are also discussed as an important factor to some extent of an outsourcing outcome (Outsourcing Advisor Representative 2009). This perspective portrays the provider's responsiveness to the client's anticipation that the process they outsource will advance and helps improve client's operational effectiveness. In this case we can find that transformation competencies are of greater significance when evaluating outsourcing providers.

Client perspective: Company C advocates that the evaluation of outsourcing initiatives and outsourcing outcomes should be aligned with the increase in competitiveness an external provider can generate for the company. The client

representative advocates that inspection and scrutiny of the providers' capabilities regarding their quality control systems is in order (Outsourcing Client Representative 2009). From Company C's point of view it is important to focus on the provider's service scope and service complexity. This indicates that the delivery competencies are crucial factors when evaluating an outsourcing provider, from a client perspective.

Provider perspective: When asked what the main differentiators of Company P were, the representative responded by focusing on the delivery competency of their organization (Outsourcing Provider Representative 2009). Both exposing their service scope and service complexity distinguished the outsourcing provider representative's point of view. What has also been discussed is the client awareness regarding the transition period. During the initial phase of an outsourcing relationship the attention needed in that transformation is critical (Outsourcing Provider Representative 2009).

Bundled together in different ways these capabilities will result in a provider's competency that is specifically relevant to the client. Screening the perceptions from the representatives gives the interpretation that delivery and transformation competencies are those that are evaluated when putting outsourcing providers under scrutiny. The motives for outsourcing that are conducted by means of generating competitiveness and business value is achieved through a higher resource position. This is enabled through outsourcing provider's competencies and ability to infuse external perspectives and innovative knowledge into the client's business processes. There are several enablers within an outsourcing engagement and are grouped in *client-*, *provider-*, and *relationship* enablers (Weeks & Feeny 2008: 130-5). Therefore it becomes a crucial issue to understand the key enablers of business value as an outsourcing outcome.

What is of importance is that the company representatives that are presented in this thesis tend to focus less on the significance of relational competencies when evaluating outsourcing providers. This gives evidence to limiting relational enablers within outsourcing engagements. However, all of the representatives acknowledge the importance of a healthy relationship between client and provider. The propositions on how competitiveness and the optimal outsourcing success are achieved in an outsourcing relationship are still required for understanding the reality of BPO. This will be portrayed next when the dimensions of outsourcing success are investigated.

4.2 Three Dimensions of Outsourcing success

Contemporary research that has been mentioned in previous chapters has the tendency to solely use cliental satisfaction as a dependant when evaluating outsourcing success. Dealing with the risk factor in an outsourcing agreement can be a quite cumbersome matter. One of the biggest drawbacks of letting someone else conduct ones business is that the client to some extent loses control over it. It therefore becomes a risk factor that now is harder to monitor and influence, which becomes a financial concern. There is also an increased opportunism and probability of performance risk, such as the provider not performing the way that was anticipated by the client. Outsourcing contracts are written in general terms, but carried out in detail, and in the process misinterpretations and mistakes arise. In the startup process of an outsourcing agreement differences in expectations can surface and there can be complications regarding responsibilities. As previously mentioned, Blumenberg *et al*. (2009) and Wullenweber *et al*. (2008) advocate that to mitigate financial- and performance risk, factors such as contractual governance, conflict resolution, communication and cooperation are important factors for the outsourcing success and the degree of cliental satisfaction.

However, this is not sufficient if long-term optimization is a desired outcome of an outsourcing engagement. Diminished risk does not result into an optimal outsourcing outcome. Rather relational risk mitigation can be used to prompt client satisfaction. In the remaining parts of this chapter we will look closer on the significance of relational risk mitigation and the optimal outsourcing success. We believe that if outsourcing optimization would be a desired outcome, an outsourcing relationship should have to go beyond satisfaction and also direct attention towards other dimensions of outsourcing success. Only then can outsourcing efforts become optimized. This will be presented in a model that illustrates outsourcing optimization and outsourcing success.

4.2.1 Dimension I – Satisfaction

Satisfaction is, according to Parasuraman *et al.* (1994), measured by the service that is *desired*: 'the level of service representing a blend of what customers believe "can be" and "should be" provided', and the *adequate* service: 'the minimum level of service customers are willing to accept' that is expected. In this *zone of tolerance* lies the performance that a client or customer would consider satisfactory (Parasuraman *et al.* 1994: 202). Going one step further they suggest that satisfaction through service quality should be measured through five major parameters of quality, such as reliability, responsiveness, assurance, empathy and tangibles. These criteria have fulfilled the representation of outsourcing success within the latest research in that field. However, there are more elaborative quality measures that focus on relational quality developed by others, such as Liljander and Strandvik (1995). But these more complex models have been disregarded within research of outsourcing success as satisfaction within relational dimension. The common denominator for these two models is that outsourcing success is aligned to only cliental satisfaction. Meaning that any other desired outcome of outsourcing efforts is not achievable. We follow this argument by investigating the perceptions of the respondents in our thesis, regarding outsourcing success.

Advisor perspective: According to the representative of Company A, non-satisfactory outcomes mainly originate from the negligence of creating a clear picture on the service level that is required. Providers are also required to participate with the client to be able to achieve a specific and desired service level. The representative also discusses that withholding information regarding strategy and objectives of the outsourcing initiative between the provider and the client can be catastrophic: 'If so this situation can create unevenness, meaning that either party withholds information that is important to the outsourcing outcome, which then results into experiences of lower service quality or higher costs for basic services from the clients point of view' (Translated from Outsourcing Advisor Representative 2009).

Client perspective: Company C's representative acknowledges the issue of unevenness and certain loss of control when outsourcing can in different instances be viewed both positively and negatively. Nevertheless, the issue of openness is regarded as precarious: 'That's the big risk with suppliers, if you don't keep them under control, they can possibly take off with your knowledge. This is due to the vast amount of knowledge they gain by doing business with you' (Translated from Outsourcing Client Representative

2009). Company C therefore recognizes one of the main disadvantages of letting someone else conduct ones business, which is the loss of control.

Provider perspective: Company P's representative states that their organizational culture is very service-oriented that always tries to assure cliental satisfaction. When Company P engages in outsourcing efforts with a client it is necessary to realize that it is more than a provider and client relationship. Therefore we attempt to execute our outsourcing services that allow both organizations to have whole and common sets of interests, which solve various issues and challenges in an outsourcing relationship. The representative illustrates this by stating: 'If a client finds ways to do things cheaper or save money, if both supplier and the customer have a share in any profitability gains you have from streamlining the process, that has a huge benefit, it really means a lot in the amount of effort the vendor makes to do things in a better way or make it in a cheaper way' (Outsourcing Provider Representative 2009).

Assessing the different perceptions of the representatives one can distinguish concerns regarding the openness within an outsourcing relationship. What is of great significance is to have a balance between the provider and client. Meaning that information regarding strategy and objectives of the outsourcing initiative between the provider and the client can be catastrophic if withheld. However, this is often a crucial issue for the client because openness is regarded as a precarious factor. The key factor from a provider perspective is to have common interests when initiating outsourcing engagements, which is key parameter when solving challenges within an outsourcing relationship. Similarities to goal sharing, goal congruence and related management tools are distinguished when reviewing the respondent's perceptions of outsourcing success. Therefore parties that engage in outsourcing initiatives should share risks by making joint investments to prevent or reduce opportunistic behavior by sharing gain or loss of any improvement or deterioration of the transaction (Van der Meer-kooistra & Vosselman 2000: 55). Obviously this confirms that solely relying on relational risk mitigation is not sufficient to optimize BPO. Therefore we can reject H0. and confirm H1. Thus, it is alleged that assessing BPO-engagements that only consider pre-contractual governance and post-contractual (relational) risk mitigation is sufficient if satisfaction is a desired outcome of an outsourcing engagement. This assumption is confirmed due to the fact that diminished risk does not result into an optimal outsourcing outcome, but rather that relational risk mitigation can be used to prompt client satisfaction.

4.2.2 Dimension II – Operational Effectiveness

'(…) group of individuals committed to a common goal, offers a powerful

way to overcome (…)' (Hargadon 2003: 104)

Operational Effectiveness is another dimension of outsourcing success and according to Porter (1996) it is realized when experiencing superior performance of similar activities compared to a company's rivals. Operational effectiveness enables companies to utilize its resources better (Porter 1996: 61). Companies that outsource parts of their operations can gain operational effectiveness through: less expensive business process solutions; resources that can be allocated to core business processes, and superiority and effective performance (David 2007: 201).

According to Anthony & Govindarajan (2007) effectiveness is achieved when the outcomes are aligned with organizational objectives. Reversely, an organization whose outcome fails to contribute sufficiently to the realization of the organization's goals is not effective (Anthony & Govindarajan 2007: 131). To enable performance efficiency and effective activity monitoring between two parties that helps organizations to achieve their goals and objectives requires the implementation of an effective management control system. Management control systems that increase effectiveness should always be built upon goal congruence, have some sort of formal and informal control mechanisms in place, focus on motivating individuals to strive towards achieving goals and enable a system of risk sharing between the provider and client (Hoque 2003: 50-1). We follow these arguments by investigating the perceptions of the respondents in our thesis, regarding outsourcing success through operational effectiveness.

Advisor perspective: Company A's representative acknowledges that it is crucial to be open with the client by making them aware of the risks that can arise. Afterwards governance becomes a main concern, which is achieved through a control model that incorporates a structure and process that controls the relation with the outsourcing provider. The control system should be designed according to measurable service levels that have been agreed upon by both parties. The advisor representative states: 'It is therefore essential not to neglect the commitment and involvement of the preparatory work with the outsourcing provider to implement an effective control system within the vendor relationship' (Translated from Outsourcing Advisor Representative 2009).

Client perspective: As previously mentioned Company C's representative stated that: '(…) if you don't keep them under control, they can possibly take off with your knowledge (Translated from Outsourcing Client Representative 2009). This acknowledges that a control mechanism is an important factor. Other factors that are essential for outsourcing success are from the client representative point of view: clear goals, thorough information on the provider, keeping technology to yourself if applicable and conducting quality control internally (Outsourcing Client Representative 2009).

Provider perspective: According to Company P's representative it is crucial to implement incentives for cooperation. This is not only necessary on the operational level. Even on the management level a significance of good cooperation between the senior leaders from both organizations is crucial. The provider representative also mentioned the importance of informal control mechanisms by stating the following: 'I think the other key to work on is to understand each other's culture (…) Do they have some sort of core value inherited from the founder of the company a hundred years ago?' (Outsourcing Client Representative 2009).

Evaluating the representative's perspective regarding operational effectiveness the importance of implementing an effective management control system becomes apparent. The reasoning and concerns of collaboratively implementing an effective control system that incorporates both formal and informal control mechanisms, goal and risk sharing, and so on confirm this. However, there are still some concerns regarding the openness from the client perspective as being a precautious issue relating to strategic knowledge that is essential to the competitiveness. This is also of concern to the future existence of the company if imitated and replicated. It is in these instances that *strategic fit* can function as a solution that enables outsourcing initiatives to sustain competitive advantage. Accordingly, BPO-engagements become able to achieve outcomes that go beyond satisfaction and operational effectiveness.

4.2.3 Dimension III – Sustained Competitive Advantage

Sustained Competitive Advantage is according to Porter (1996) by no means the result of effective management tools. Management tools that increase operational effectiveness can only improve the performance of organizations while generating and sustaining *competitive advantage* will only result from superior strategy formulation and positioning (Porter 1996: 61-4). Strategy means performing core activities differently than its rivals or performing similar activities in different processes: 'Competitive strategy is about being different. It means deliberately choosing a different set of activities to deliver a unique mix of value' (Porter 1996: 64).

'Thinking Different, Together' (Hargadon 2003: 104)

Naturally the ability to be open within an outsourcing relationship, issues such as trust must be in place, which is mentioned by Weeks & Feeny (2008). However, relational factors do not mean that financial risk and performance risk are mitigated to a greater extent. To eliminate risks that threatens the competitiveness and future existence of a company when outsourcing, requires a complex system of interlocked activities that are *consistent*, *reinforcing* and activities where efforts are jointly *optimized*. Only then does a position become harder for rivals to outmatch if it rests on a set of outsourced activities that are integrated. To achieve a strategic fit between two sets of activities or two sets of business processes requires that decisions and actions become integrated across these independent subunits (Porter 1996: 74). We follow these arguments by investigating the perceptions of the respondents in our thesis, regarding outsourcing success through sustained competitive advantage.

Advisor perspective: The representative of Company A consistently recapitulate the factors of outsourcing success by mentioning openness, collaboration, and changing attitudes that withhold this kind of behavior. This is of crucial importance when conducting the preparatory work with the outsourcing provider (Outsourcing Advisor Representative 2009). The representative clarifies this perception by stating: 'Those who experience outsourcing success have a strong belief in openness. They share their objectives and goals with each other and know what they expect from each other' (Translated from Outsourcing Advisor Representative 2009).

Client perspective: The risk of not sustaining competitive advantage is a vital concern for Company C. The client representative also acknowledges the importance of solely profiting from an outsourced party. The representative perception is derived from the following statement: 'If you keep ample capability yourself or the supplier has more capability than you, then this can also result in an increase of competitiveness, provided that you are the sole company profiting from this' (Translated from Outsourcing Client Representative 2009)

Provider perspective: Company P's execution of outsourcing services enables clients to share common sets of interests that solve various issues and challenges in an outsourcing relationship. The provider representative acknowledges the need of integrating decisions and actions by stating the alternative of opportunism which: '(…) is where they create incentives where the parties start pulling in different directions from one another (…) So you have contradicting goals' (Outsourcing Provider Representative 2009).

Integrating the decisions and actions to achieve a strategic fit between business processes will enable outsourcing efforts to sustain competitive advantage. This is also confirmed when interpreting the representative's perspective regarding concerns of openness, threat of losing their competitive edge when being open with an outsourcing provider, and moving to different directions within an outsourcing engagement. It is only when a significant level of integration is achieved that opportunistic behavior is eliminated, which is damaging within an outsourcing initiative. This means that these concerns of losing competitiveness within an outsourcing relationship can only be eliminated if strategic fit is realized. From a client perspective it is necessary to be integrated with an outsource provider, due to the fact that this disables any possibility of loss of control and that knowledge can not be transferred to other clients that are doing business with the same provider. This means that it will become harder for rivals to replicate or imitate a specific position if it rests on a set of activities that are jointly fit together. It is in these instances that *strategic fit* can function as a solution that enables outsourcing initiatives to sustain competitive advantage. However, this requires that companies conduct their outsourcing efforts with their providers in order to prevent contradicting goals, which enable them to work together and integrate decisions and actions.

For an outsourcing outcome to be optimized and reach a higher level of outsourcing success requires that decisions and actions be integrated within an outsourcing relationship. Through openness outsourcing parties are able to integrate their independent activities and business processes. Consequently this will result into strategic fit that enables outsourcing efforts to sustain competitive advantage.

4.3 BPO OPTIMIZATION

Collectively viewing sustained competitive advantage, operational effectiveness, and satisfaction as the optimal outsourcing success means that outsourcing initiatives cannot solely focus on relational risk mitigation and contractual governance. Therefore looking beyond relational risk mitigation and contractual governance, and including integrated management control systems and strategic fit will result into a higher level of outsourcing success. This means that outsourcing outcomes should incorporate three dimensions of outsourcing success instead of only one. Consequently, a higher application of each of the three aspects results into a superior outcome. Thus, in order to reach the highest level of outsourcing success one needs to incorporate all three dimensions as depicted in figure 4.1.

Figure 4.1: Outsourcing Optimization and Outsourcing Success
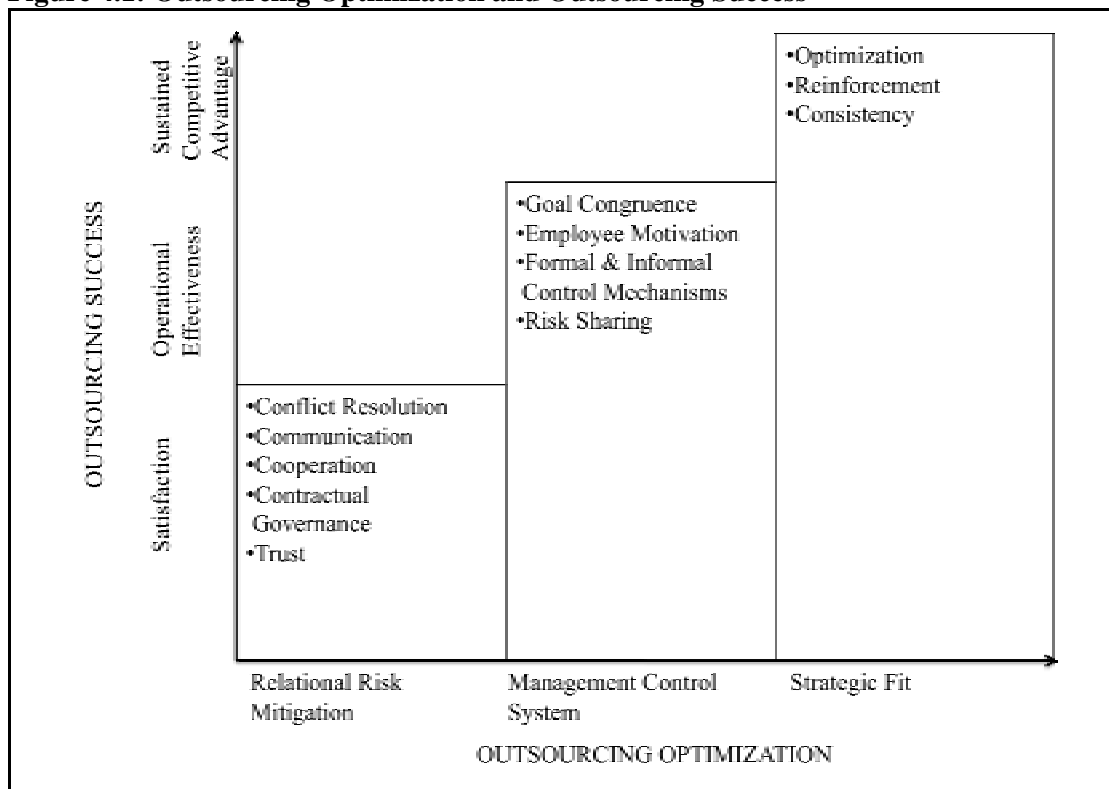
V. The Reality of Business Process Outsourcing Optimization

This chapter will present the thesis' final conclusions regarding the reality of business process outsourcing by stressing the purpose of this thesis. Our findings have illustrated the significance of cliental satisfaction and how to optimize business process outsourcing, which will be presented here.

5.1 Significance of Satisfaction as a Dimension of outsourcing Success

> ∗ Is solely relying on relational risk mitigation sufficient when optimizing business process outsourcing?

The above research question has been approached by emphasizing the outcome of outsourcing efforts, where the main focus has been to identify outsourcing success from different intervening dimensions and how these levels of success are achieved within an inter-organizational relationship. The very purpose of initiating outsourcing efforts may differ from company to company, nonetheless it has proven to be an important factor for understanding the optimization of BPO engagements. The case company representatives that have been presented in this thesis provide valuable insights to this problem. The three different perspectives evidently acknowledge that outsourcing engagements becomes worthwhile if a company has a weaker resource position. Meaning that outsourcing becomes an attractive alternative where a company cannot utilize its inputs more efficiently to achieve organizational goals than an external provider. Meaning that a company who is considering outsourcing efforts is likely to engage in outsourcing if there are limited resources to perform that function or process effectively in-house.

What is of great importance is that organizations, which desire an outsourcing engagement should result into the optimal outsourcing outcome tend to focus less on relational competencies and enablers when evaluating an outsourcing initiative, and more on transformation and delivery competencies. Meaning that factors, such as: exposing the service scope and service complexity of the outsourcing provider; and the outsourcing providers responsiveness to advance and help improve the clients

operational effectiveness becomes more important. It is only when a significant level of integration and sharing is achieved that opportunistic behavior is dramatically reduced, which mitigates risks that are damaging for an outsourcing engagement. Goal sharing, goal congruence and other related management tools are distinguished when moving towards other dimensions that portray outsourcing success more realistically. Clearly this confirms that solely relying on relational risk mitigation is not sufficient to BPO optimization, which resulted into the rejection of H0. and confirmation of H1. This also gives evidence for limiting the importance of the relational competencies when evaluating outsourcing providers, which also limits the relational enablers within outsourcing engagement even if a healthy relationship between client and provider is significant to some extent. This assumption is confirmed due to the fact that diminished risk does not result into an optimal outsourcing outcome. Rather relational risk mitigation can be used to prompt client satisfaction as a dimension of outsourcing success.

5.2 How to Optimize BPO Efforts

✱ How is business process outsourcing efforts optimized?

When analyzing other dimensions beside *satisfaction*, such as *operational effectiveness* and *sustained competitive advantage* it becomes apparent that implementing an effective management control system and achieving a strategic fit is crucial. Collectively viewing these three dimensions as the optimal outsourcing success means that outsourcing initiatives cannot solely focus on relational risk mitigation. Therefore looking beyond relational risk mitigation, and including integrated management control systems and strategic fit will consequently result into a higher level of outsourcing outcome. The case company representatives confirmed this through their reasoning and concerns of collaboratively implementing an effective control system.

From a client perspective the issue of openness becomes a threatening matter if the risk of opportunistic behavior is high. Therefore it is important to have a strategic fit that enables outsourcing initiatives to sustain competitive advantage. This is achieved by integrating the decisions and actions to form a strategic fit between two sets of activities or two sets of business processes. Only when a significant level of

integration is achieved opportunistic behavior that are damaging will be reduced. Concerns of losing competitiveness can only be eliminated if strategic fit is realized. Another issue is that the integration between an outsourcing client and an outsourcing provider disables any possibility of loss of control. Meaning that knowledge is not transferable to other clients that are doing business with the same provider if it rests on a complex system of interlocked activities. Optimizing outsourcing outcomes and reaching a higher level of outsourcing success, such as sustained competitive advantage, operational effectiveness and satisfaction, requires that decisions and actions become integrated within an inter-organizational relationship.

5.3 Knowledge Contribution

The contribution of this thesis to the studies and the academic field of inter-organizational relationships and governance is that outsourcing success should not solely be evaluated and measured through satisfaction. This is because measurements of satisfaction are often focused on episodes within an inter-organizational relationship and not on the outcome of the whole relationship. Therefore, when measuring or evaluating outsourcing success based on relational quality it should incorporate longitude measurements instead of quality that only represents a specific episode in time.

To optimize BPO efforts, outsourcing relationships must go beyond evaluating satisfaction and not solely acting upon it through relational risk mitigation. It is not intended to marginalize relational risk mitigation as a management tool to create a significant level of outsourcing success, rather that it is not sufficient when solely used to optimize BPO efforts. Therefore we have developed a conceptual framework and model that portrays BPO optimization and outsourcing success in a more truthful matter (see figure 4.1).

5.4 Future Research and Limitations

Further research on the subject of BPO could include an analysis of the contracts that are written between the customer and supplier: how they are made to support, reprimand unwanted behavior and to align their goals and what actions the different types of contracts results in. Future research within the field of inter-organizational governance should also examine the difference between local suppliers and

multinational / offshore suppliers in their *modus operandi* to measure any tendency of cultural differences that are critical to outsourcing success. Another crucial factor is that research similar to Wullenweber et al. (2008) and Blumenberg et al. (2009) on relational quality should incorporate longitude measurements instead of quality that only represents a specific episode within an outsourcing relationship.

The limitations of our research consist of the inability to generalize our model with only three case companies. However, the different perspectives that are presented in this thesis derive from various outsourcing experiences in multiple industries and sectors. Therefore, some significance of generalization is achieved, thus could be applicable to future outsourcing efforts.

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Appendix 1.

Case I: The Advisor Perspective

The advisor case company (Company A) is an organization of 70 associate firms that has a global reach and is operating in nearly 150 countries. Company A provides a broad range of professional services including audit, tax, consulting and financial advisory services. The company provides its services to all major sectors and targets national and middle market enterprises, public institutions, privately owned companies and public sector organizations. The consulting division is engaged in providing services to clients across the world within strategy, operations, technology, human resources and outsourcing consulting services.

Company A's representative that was interviewed (2009-05-07) is a *Senior Manager* within the company's subsidiary that is located in Stockholm, Sweden. The representative has been a consultant for 10 years, where the representative has worked with *shared services*, *outsourcing advisory*, *change issues* and *transformation challenges* regarding finance functions and with some focus on other business processes. This expert representative has been chosen to facilitate the advisor perspective regarding outsourcing and BPO issues. Before working as a consultant the representative worked within finance related functions, such as a controller and other operational functions for major international companies. However, the representative has been with Company A since 2002.

1. Background

1.1 What is your current position and what are your work tasks?

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
I am part of *Company A* with a position as a *Senior Manager* and have been a consultant for 10 years. In my career I have worked with change issues and transformation challenges regarding finance functions with some focus on business processes also. The last 10 years I have focused on *Shared Services* and *Outsourcing Advisory*. Company C consulting division is divided into *CFO Services*, *Operation Excellence*, and *IT*. *CFO Services* focuses on the CFOs responsibilities and the support during a transition period or changes within that part of businesses. *Operation Excellence* work with business procurement, lean

management, sourcing issues, cost reduction and so on. The *IT* group focuses on IT strategy and implementation.

1.2 What outsourcing services does Company A offer?

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
In our group it is *Outsourcing Advisory*, which is also very much related to *Shared Services* offers. Because effectiveness within *F&A activities* can in some instances resulted from outsourcing solutions. We also have an *Integrated Performance Management* service where financial management and business control is evaluated as regards for executing the strategy. This incorporates performance management, budgeting, control, and evaluation, which are more a holistic approach to financial management and management control. So we do not offer outsourcing services, rather we advise on outsourcing issues and evaluate companies if this is necessary. However, we do have a *BPO business* within *Company A* in Östersund, which is more locally facilitated and not offered in the rest of the country. We also have larger BPO businesses in USA and other European countries that target global companies, which have subsidiaries around the world can take part in.

1.3 How long have you been in the business?

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
Before working as a consultant I worked within finance related functions, such as a controller and other operational functions for major international companies. However, I have been at my current position at *Company A* since 2002.

2. Motives

2.1 What motives for outsourcing does BPO clients have?

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
The main reason for outsourcing that we consider is cost reduction. We have some global studies that 70 % are engaging outsourcing solutions for cost reduction reasons. However, we also see some need for leveraging technology, such as gain effective and better processes with more enhanced technologies. This is something that outsourcing providers can offer, but also clients are after some sorts of standardization of *F&A activities* across a corporate group, an attempt for being more consistent.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
We also see more and more companies want to optimize their processes and create effectiveness in their way of work, which we advocate when advising on outsourcing solutions. This is often a major issue for some outsourcing clients when choosing an outsourcing provider.

2.2 What are your competitive advantages as a service advisor?

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
Our main differentiation factor is that we are neutral and independent. We don't strive to gain the mega deals in such ways that the providers do. This position is very appealing to clients that are considering outsourcing approaches. Another advantage is that we have a global network and the competencies to deliver outsourcing solutions to large corporations who consider outsourcing. A third advantage is that we facilitate a good *Vendor Relation Program* with the major BPO providers. The providers that are included in this *Vendor Relation Program* know that we are independent are aware of that we have the knowledge of their strength and weaknesses. These outsourcing providers that are included are evaluated on a European level that amount to more than 10 providers and depends on different markets. For the outsourcing clients we can therefore offer various potential vendors that are most advantageous for their solution. However, the main factor is that we are independent advisors in these outsourcing efforts.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
Within smaller outsourcing deals, which often is an issues of *Shared Services*

where we in Sweden identify as transition period of the *F&A activities* if outsourced. In those situations we can offer the choice of potential outsourcing providers and help them with the process to until the choice is done. We can then help with the evaluation and identification of the specific processes and the startup process of the outsourcing engagement.

2.3 In what way do you work with continuous improvements?

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
Outsourcing clients that base their choice regarding outsourcing provider on optimization are interested in what way outsourcing providers' work with continuous improvements. Major outsourcing providers often promote this expertise when they meet outsourcing clients. One could say that the continuous improvement of our work is through the different resources and capabilities of the provider. The greater effectiveness of processes and continuous process improvements are becoming more and more important in these crucial times for outsourcing clients.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
It is also important to be aware of the small a more local based outsourcing providers that can facilitate these minor and more specific outsourcing deals. Therefore we have to go both ways, because some major corporations don't even consider some outsourcing providers if they cant deliver more than a specific level of capacity. Its not sufficient to only have a relation to large outsourcing providers we have to meet the outsourcing clients different preferences and needs.

3. Risks

3.1 Have you identified any risks (for the customer) associated with outsourcing? How do you work to prevent those risks?

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
The main risk is that the outsourcing client undermines the importance of viewing the outsourcing issue as a case prior to striking the deal, which can result into companies experience unexpected cost during the transformation. Engaging an evaluative business case with outsourcing providers and advisors regarding the costs of these initiatives often prevents this from happening. This should then be related to the motives of outsourcing a business process. We therefore recommend a thorough financial evaluation before going through the deal. After the decision has been made risks such as risk loosing the staffs and the skilled workers prior knowledge of running that specific business process during the transition period. If the skills and knowledge is not transferred the outsourcing provider may experience major challenges during the changes.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
Another risk is that the outsourcing client do not experience a good service and are not satisfied with the delivery of the services, which is mainly related to negligence or a clear picture of which service is required at first. There should be a clear picture on the service level that is required. Vice versa providers also have requirements on the outsourcing client to be able to achieve a specific and desired service level.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
A risk that is also relevant to prevent is the non-openness regarding strategy and objectives of the outsourcing initiative between the provider and the client, which we advise on. If so this situation can create unevenness, meaning that either party withholds information that is important to the outsourcing outcome, which then results into experiences of lower service quality or higher costs for basic services from the clients point of view. There are different conduct levels between the outsourcing clients regarding the view on service agreements. The problem often derives from the clients' inability to transform from a provider mentality to a client mentality, which the results into poor identification of a desired service level. It is often more focus on what is to be delivered, not enough focus on how the service is to be delivered and under what timeframe or quality it is to be delivered. This is often related to how much the client is ready to pay for

outsourcing services. This is an area were we have to advise our clients that don't have any previous outsourcing experiences.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
Our participation in any outsourcing solution is mainly based on evaluating different alternatives, which overlap to the transition period. It is very rare that we have any presence after this period. What we can do is post-evaluations, and measures the service quality and the vendor relationship. However, our focus is during the evaluations and the transition period. In these periods we can help with change issues.

3.1 One of the main issues with outsourcing is that customers, even if they still have insight in their economy, risk loosing control over the company.

3.1.1 What is you view on that?

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
We are aware of the unrest with the lost of control, which is discussed with companies. However, in some instances this change and lost of control can create a higher level of transparency when organizational politics cant disrupt or manipulate F&A activities within a corporate group. The awareness of having transparency within F&A activities can mitigate the unease of losing control.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
One counteraction is implementing a good governance system that incorporates continuous evaluations and measurements regarding delivery and so on. So it does not have to be viewed as lost of control rather greater transparency. However, it requires preparatory work with the outsourcing provider to implement an effective control system when F&A activities are transferred to the outsourcing provider. Often this results into changes within the control system. If the importance of preparatory work and implementing

effective control systems is undermined one could risk losing control.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:

We therefore advise that setting aside time for preparatory work with the outsourcing provider to implement an effective control system is a solution that prevent a possible loss of control. It is not the outsourcing provider that is responsible for the performance, because they only facilitate the transactions. They take fore granted that the outsourcing client have responsible controllers that are involved in the F&A activities. Larger corporations that are public companies must apply different policies, codes and laws, such as Sarbanes Oxley Act. This often result into a strict internal control culture. Obviously clients don't engage in outsourcing efforts if these standards are not encountered, which are an important element in the change and the transformation.

3.1.2   *How do you work to prevent possible loss of control? What measures are taken?*

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:

Other preventive action for loss of control then effective governance and control systems is the possibility to conduct in-house audits. In this case the company can follow up the control of the F&A activities that are outsourced. The transparency and the availability of the transactions enable outsourcing clients to facilitate in-house audits and control if it is desired. However, this should not be the case if there is collaborative preparatory work with the outsourcing provider.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:

Another method is to be open with the outsourcing provider and vice versa,

regarding the objectives and strategy to be able to analyze how the outsourcing efforts can be coordinated accordingly. The ability to understand each other's corporate cultures is also a crucial factor. Those who experience outsourcing success have a strong belief in openness.

3.1.3   *If the control is passed from the customer to the provider, do you think that it could have any positive / negative effects for the customer, if so, which?*

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:

'We are aware of the unrest with the lost of control, which is discussed with companies. However, in some instances this change and lost of control can create a higher level of transparency when organizational politics cant disrupt or manipulate F&A activities within a corporate group. The awareness of having transparency within F&A activities can mitigate the unease of losing control' (Translated from Interview with Outsourcing Advisor Representative 2009-05-07: 3.1.1).

3.2 How do you handle confidential material? (So it won't reach other clients) Do mistakes happen, like sending material to wrong person?

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
There are different alternative to this problem. It could be through the usage of different systems for different users. Larger and more global deals often rely on one outsourcing provider that is prohibited from working with other clients, but this is also often an issue of how much an outsourcing client is ready to spend on control mechanisms and to physically set apart or disconnect a specific part or division within the F&A activities, instead of just having technological mechanisms such as authorization, firewalls and so on. There are multiple methods to this problem. The more a company moves from paper usage towards electronic usage this problem becomes easier to handle and prevented from coming into wrong hands. However, even for larger or smaller outsourcing deals it is often a criterion that a group of employees only facilitate outsourcing services

to one corporation as their representatives.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
For smaller outsourcing providers that facilitate services more locally do often represent multiple clients at the same time. In these case it often results into technological mechanisms such as authorization, firewalls and so on. Depending on the resources, capacity and capabilities of the outsourcing provider these mechanisms of controlling information can vary, even if there always is some sort of client confidentiality agreements.

4. Relationship

4.1 How do you treat problems arising in the cooperation with the customer?

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
When we engage a client we are very open with possible risks that can arise. The first thing we do is to develop a governance and control model that incorporates a structure and process that controls the relation with the outsourcing provider. The control system should be designed according to measurable service levels that have been agreed upon by both parties. These systems should include processes that handle any type of escalations that is experienced. This can be how an escalation on the operational level is channeled to a supervisory level where corrective actions can take place.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
Again what are most important are openness, collaboration, and changing attitudes that withhold this kind of behavior. It is therefore essential not to neglect the commitment and involvement of the preparatory work with the outsourcing provider to implement an effective control system within the vendor relationship. It is not easy to transform a client profile from a provider mentality to a client mentality regarding F&A activities. This is something that we often work with.

4.2 How important do you consider a close relation / good communication with the client is, and the client trusting the provider?

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
I think that this question is already answered. Obviously this is really important. Those who experience outsourcing success have a strong belief in openness. They share their objectives and goals with each other and know what they expect from each other.

5. Conclusion

5.1 What is your view of the outlooks for your company and the outsourcing business industry?

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
There is an increase in interest with regards to today's recession for cost reduction and outsourcing as a possible alternative solution for this kind of efforts. What we also see in the Scandinavian market is that we are far behind other countries. Overall companies are very suspicious and more careful regarding outsourcing. This maybe is due to cultural differences. However, we have identified some changes regarding the attitude of outsourcing. Meaning that more and more companies are becoming stable and are more mature in this endeavor to outsource.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
Both locally and globally this awareness of outsourcing is changing. In Nordic countries more and more corporate groups are considering outsourcing as an alternative. There is also many different kinds of outsourcing that are developing, which is very important to be aware of when looking at outsourcing alternatives. In Sweden e.g. outsourcing IT and HR is quite common, but not as mature in other types of business processes. However, companies also look for other parts and functions within their organizations to outsource. It has become essential for outsourcing providers to become more professional and focused in some specific areas, which becomes their niche that becomes a competitive advantage.

5.2 What advise would you give to a company considering outsourcing a business function?

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
The first thing is to treat the outsourcing alternative as a business case through comprehensive evaluations. The evaluation should be based on both financial and qualitative measures. These evaluations are somewhat important for benchmarking purposes when comparing previous and future performances during the outsourcing delivery.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
Secondly, one can't neglect or undermine the necessary investments that are required during a transition and change period. There should be considerations to support this transformation and change process. Unwillingly there will be experiences of set backs, nevertheless it is important to be aware of them and to be able to recover from them.

Translated from Interview with Outsourcing Advisor Representative 2009-05-07:
Finally, having a clear insight and understanding of what to outsource and for what reason one is considering outsourcing alternatives.

Appendix 2.

Case II: The Client Perspective

The client case company (Company C) is the holding company for one of the world's largest electronics companies and has subsidiaries in over 60 countries across Europe, Africa, North America and Asia Pacific. The company's business is separated into three major segments, which are consumer electronics, medical systems, and lighting. Company C has also joint ventures and alliances with various companies around the world. The company was established in 1891 where the founder started manufacturing incandescent lamps and other electrical products.

Company C's representative that was interviewed (2009-05-12) is a *member of the executive management board*, which is located in the Amsterdam, Netherlands. The representative joined Company C in 1973 and has worked for the company around the world in a number of key management positions. This expert representative has been chosen to facilitate the client perspective regarding outsourcing and BPO issues. The client representative entered the position in 2006, but is currently retired.

1. Background

1.1 Could you briefly describe Company C and what is the core of the organization?

Translated from Interview with Outsourcing Client Representative 2009-05-12:
Company C is a multinational company operating in various fields of electronics in over 60 countries, employing over 180.000 people. The core of the business is divided into three main categories, such as *Consumer Electronics*, *Medical Systems* and *Consumer Lifestyle Electronics*.

1.2 *What is your function within Company C?*

Translated from Interview with Outsourcing Client Representative 2009-05-12:
I was a member of the Board of Management, but I am retired now. I entered this position in 2006. However, I joined *Company C* in 1973 and have worked within the company around the world in a number of key management positions.

1.3 What functions/parts have been outsourced in your Company?

Translated from Interview with Outsourcing Client Representative 2009-05-12:
Several big pieces have been outsourced within the company. There are different sorts of outsourcing in different divisions. In the *Consumer Lifestyle Electronics* division for example we have outsourced almost all the actual production of products, Televisions VCRs and similar products have all been outsourced. When we look at the Lighting division most of the products are still made within the company, only a couple of particular fields like Compact Fluorescent Lighting are outsourced. Medical Systems have outsourced sub-systems.

1.4 What "trends", outsource-wise, have you witnessed during the years?

Translated from Interview with Outsourcing Client Representative 2009-05-12:
When you want to reduce risk as a company you outsource big pieces. As such we have outsourced all the production for televisions a couple of years ago. But if you now look at the future there seems to be a more narrow focus on outsourcing deals.

1.5 *What are the reasons for choosing the current outsource providers?*

Translated from Interview with Outsourcing Client Representative 2009-05-12:
When outside parties have superior capabilities compared to your in-house capabilities you choose those partners to outsource to. There is however one drawback attached to this namely that you lose that capability.

2. Motives
2.1 What are the reasons and goals for outsourcing the previously named functions?

Translated from Interview with Outsourcing Client Representative 2009-05-12:
Mainly when an outside party can fulfill the designated function better than you.

Most of the times it's from a cost savings point of view but it can also been done due to a fluctuating business division. The changing in the volume of the production and thus by outsourcing this function improving the stability of Company C cause this fluctuation.

2.2 Is outsourcing viewed as a source of competitive advantage for Company C?

Translated from Interview with Outsourcing Client Representative 2009-05-12:
No.

2.3 Is there continues improvement in the current outsourcing deals? If yes, in what way and does this emanate from your company or from the provider?

Translated from Interview with Outsourcing Client Representative 2009-05-12:
Most of the times the improvement emanates from Company C as we learn what can go wrong during the process which is then corrected in the next contract. You first look at the performance of the supplier and what things went wrong; if the problems are solvable with the supplier you adjust the contract accordingly, if not you have to switch to another supplier.

3. Risks

3.1 What negative factors do you relate to outsourcing? Are those factors still currently present within the company?

Translated from Interview with Outsourcing Client Representative 2009-05-12:
It depends on how the outsourcing is organized. If you look at the Compact Fluorescent lighting for example, we have kept the development within Company C and outsourced the production. In that way we keep the capability of the design of new products. At Consumer Electronics, with televisions for example, they have outsourced too many of their capabilities in my eyes. Thereby lacking capabilities yourself and running the risk of competitors easily copying your products.

3.2 Do you have any experience that you lose control to some extent on outsourced business functions, if so do you see this as a positive or negative effect?

Translated from Interview with Outsourcing Client Representative 2009-05-12:

You always have a loss of control to some extent. If you have a capacity shortage and the supplier therefore has to invest, you have to look for different solutions. At Compact Fluorescent Lighting for example we now have 5 different suppliers due to the fact that those companies weren't financially strong enough to increase the capacity fast enough. Moreover you don't want to have only one supplier since that invokes the risk of being completely dependent on this supplier. In this case it would also mean that one company would produce 25% of the total world production of lamps, making it very powerful and also creating the opportunity for that company to supply the lamps in different ways for themselves. Thus there is ample reason for dividing the power and thereby retaining more control. You furthermore run the risk that the supplier gains sufficient capabilities that he can make the product himself and starts to supply it himself; we sometimes prevent this by gaining a minority stake in these companies. We did this with Compact Fluorescent Lighting for example to gain control over the company.

Translated from Interview with Outsourcing Client Representative 2009-05-12:

However certain loss of control due to outsourcing can be seen as either a positive or negative effect. When outsourcing for cost savings reasons you can incur lower costs and therefore increasing competitiveness. If you're outsourcing risk you can mitigate (a part of) the fluctuations thereby possibly also creating a competitive advantage. If you keep ample capability yourself or the supplier has more capability than you than this can also result in an increase of competitiveness, provided that you are the sole company profiting from this. That's the big risk with suppliers, if you don't keep them under control, they can possibly take off with your knowledge. This is due to the vast amount of knowledge they gain by doing business with you.

3.3 Do you have experience that information related to outsourcing is treated confidentially?

Translated from Interview with Outsourcing Client Representative 2009-05-12:
No, officially yes but in practice this doesn't hold as contracts are not infinite. As they will gain knowledge while doing business with you, which is inevitable. This isn't a bad thing if the product is in a dying phase, but when doing this with new products that have to guarantee your future I would strongly dissuade this. For the same reason I would never outsource certain lamps to China, you benefit from the arrangement for 5 years and then you see the same lights as competitors on the market. This sort of conduct does happen on a large scale, for some countries this is more severe than other. Especially in China your information is rarely safe, they copy everything. We therefore have an extensive list of technologies that may never be outsourced to China. It is therefore essential when dealing with outsourcing that you keep certain key components in your own hands.

4. Relationship

4.1 How do you experience your relation to the outsourcing vendor? Does it live up to your initial expectations?

Translated from Interview with Outsourcing Client Representative 2009-05-12:
As we're talking about a wide range of contracts the answer differs as well. At Compact Fluorescent Lighting we are very satisfied but even there we're not talking about one but five providers.

4.2 What qualifications should a supplier have?

Translated from Interview with Outsourcing Client Representative 2009-05-12:
It should have ample financial resources to be reliable in the long run as it cannot go bankrupt halfway the agreement. Thus there has to be kept an eye a close eye on the changes in their financial position. It should have clear quality control as well as quality systems and quality order systems, which are imperative. It should

also possess ample capability to achieve cost reduction themselves, as well as the knowledge on how to induce cost reduction.

5. Conclusion

5.1 What are the most essential features in your opinion for successful outsourcing?

Translated from Interview with Outsourcing Client Representative 2009-05-12:
It's important that you keep the design in your own hands and exercise the final quality control yourself, as you are still the one responsible for delivering the product to the customer; this is especially true in the early stages of a new product.

5.2 What advice would you give to a company, similar to your company, considering outsourcing a business function?

Translated from Interview with Outsourcing Client Representative 2009-05-12:
You first have to evaluate why you're doing it and what the resulting increase in competitiveness would be. Next you have to realize what technology you might lose, so you have to establish what technology to outsource and what not, because you are bound to lose some in the process. Then the partner has to possess proficient strength, financially as well as capabilities. For example if you're using their design capabilities then you need to check them. And you most certainly need to check their quality checking systems. And you furthermore cannot "drain the provider dry", because when a provider is very dependent on you it's extremely easy to squeeze them into bankruptcy. It is therefore important that you are on the same line with each other and both know what you're getting into. Demands like a five percent yearly reduction of the costs, since the market demands the same, should be checked whether this is in line with the capabilities of the provider. Otherwise you might run the risk of the provider upholding to the contract reducing the prices while not having the capability to reduce its costs resulting in his bankruptcy, which of course has negative consequences for you.

Translated from Interview with Outsourcing Client Representative 2009-05-12:

Summing up the essential factors that make outsourcing a success:

∗ Clear goals

∗ Thorough information on the provider, financially as well as its capabilities

∗ Keeping certain technology to yourself if applicable

∗ Ensuring your own quality checkup on products

Appendix 3.

Case III: The Provider Perspective

The provider case company (Company P) is one of the leading providers of consulting and outsourcing services through a global delivery network of over 53 centers in the world. The company's business is structured around five operating groups, which incorporates products, communications and high tech, financial services, resources, and public service. Company P has experience and capabilities across most of the industries, business functions and operates in more than 52 countries. Their offerings fall under three segments, such as consulting, systems integration and outsourcing.

Company P's representative that was interviewed (2009-04-27) is *Chief Operating Officer* for the System Integration and Technology organization at Company P's subsidiary located in Copenhagen, Denmark. The provider representative coordinate, assures project quality, and allocates resources to projects regarding IT consulting, application maintenance and application outsourcing issues. This expert representative has been chosen to facilitate the provider perspective regarding outsourcing and BPO issues.

1. Background

1.1 What is your current position and work tasks

Interview with Outsourcing Provider Representative 2009-04-27:
I'm Chief Operating Officer for system integration and technology, IT consulting. My work tasks involve coordinating a large number of things internally as well as ensuring the correct allocation of resources to projects. While keeping an eye on future needs as well as support for future sales. Furthermore keeping up competitiveness on all parameters is of high importance in our industry.

1.2 What kind of outsourcing services does Company P offer?

Interview with Outsourcing Provider Representative 2009-04-27:
We have a quite wide range of different thing, but you can break the key area down to IT. For example application maintenance, application outsourcing where

rather than having their own people to maintain IT systems they outsource it to us so we then have the responsibility to maintain systems and reporting error corrections whatever that might involve. Related to that there is infrastructure outsourcing, keeping all the services in the air and ensuring that server operations get carried out in time. And the other type we do a lot of is BPO, much more administrative tasks, HR, purchasing functions, all those types of services.

1.2.1   *Are these different types increasing integrating now?*

Interview with Outsourcing Provider Representative 2009-04-27:
No I wouldn't see it that way. If you go back some years there was a tendency towards some sort of huge outsourcing mega deals and quite a few companies around the world have burned their fingers a little bit on those deals because it's so hard to coordinate all the different activities. Now there is more of a tendency towards slightly more focused outsourcing deals with a particular function. It can be that they are the same companies that are providing both types of services but typically the individual outsourcing deal is focused on a particular function. At another time when a company has the necessary focus and energy it can take on a new outsourcing deal to address a different function of the company.

1.2.2   *Would that be to remain having control from customer point of view by instead of outsourcing the whole thing doing it stepwise?*

Interview with Outsourcing Provider Representative 2009-04-27:
The thing is that outsourcing is extremely difficult to do well. So it actually requires, at least during the startup phase, a lot more management attention than if the function would stay within the company. And that being the case, if you start outsourcing too many things at once then you don't have the management then you don't have the capability to cope with all of these things. Because there is a huge number of areas which you need to critically evaluate in the process of outsourcing. Who is going to respond to what areas,

what things you want to measure quality wise, how do you solve the problems during the startup phase as there are always going to be a lot of those. So if you only have a limited numbers of leaders in your company and then suddenly they are running around trying to fix a lot of problems related to a massive outsourcing deal then they don't have the time and energy to run the business. I think this is one of the reasons why people have started to scale down on the size of the outsourcing deals towards more focused outsourcing deals.

1.3 What kind of business model does your company utilize?

Interview with Outsourcing Provider Representative 2009-04-27:
Typically it involves some sort of partnership with the customer whereby we take over a set of functions and then the specifics of the deal are very much dependent on the customer, what it is that they want to achieve. But it most of the times comes down to typically a multiple number of years, it's not a short term thing. So we're talking about a number of years constructed in such a way that benefits both parties. As there is always a big overhead in the startup of the outsourcing we always need a certain amount of time before it starts to pay off in doing it for both parties. We furthermore don't really have any specifics concerning our business model.

1.3.1   *What differentiates Company P from other outsourcing companies?*

Interview with Outsourcing Provider Representative 2009-04-27:
The biggest differentiator is that we have a huge offshore compartment, so we have tens of thousands of people in India and the Philippines for example and other locations around the world. So when we're delivering a lot of outsourcing deals we're able to utilize both. We have people on shore to formulate and create the interface to the customer and fronting functionality and then we have a large number of people offshore performing, in many cases, the bulk of the work. That holds the costs down but at the same time

still gives people the opportunity to have a local interface and interact with a local organization. So that would be a typical situation that we have with a significant offshore component as part of the outsourcing model.

1.3.2 *How much of the BPO can you do offshore?*

Interview with Outsourcing Provider Representative 2009-04-27:

It depends quite a bit on what the business process is and also how complex the individual customer's organization is. If the individual customer doesn't have a very streamlined process that's well defined it's much harder to push those things to a different part of the world. There is also an issue with language, whether you want to communicate in English or another language and find people offshore who also communicate in that language. So there isn't really any fixed number for that, there are some situations where you can push 90% of the work offshore and some at most 30%.

2. Motives

2.1 What motives for outsourcing do your customers usually have?

Interview with Outsourcing Provider Representative 2009-04-27:

For business process outsourcing there are a few different reasons why people do outsourcing. If you look at most of the surveys internationally, maybe two thirds of them are looking at outsourcing for the sake of saving money, that's at least one of the justifications of doing it. But another reason for doing it can sometimes be to gain control over the area, which may seem like a bit of a paradox. But the reason is when you have a department in your organization, the numbers of levers you can pull or buttons you can press to increase the service or make sure that they hit their budgets or what other possible reason are actually sometimes quite limited depending on the historical structure of the organization. You don't have a contract with them, you don't necessarily have all that much you can enforce. Whereas you can have an outsourcing contract where you have some very clear service level agreements, you perhaps have some contract penalties for non-

delivery of services. So in that way you can to a large extent increase the motivation level of the supplier organization to provide the right service on time. Other things can just be to free out management attention, give them the time to focus on the core of their business. That's fine as long as they understand that for a period of time during the transition they actually need to pay more attention to that function than before. On the long term they of course do have less time allocation to that function.

2.2 What seems to be apparent from some of the research on BPO outsourcing is that the reasons of outsourcing, initially mainly cost savings, will expand during the contract. Is this also true in your experience? And what other advantages do they then gain or realize?

Interview with Outsourcing Provider Representative 2009-04-27:
Yes. I think one of the others for at least dealing with a company like us, where we have 180.000 people worldwide, that you're actually able to draw on a number of skills that you wouldn't get if you were engaged in a contract with a small local outsourcing agency. If you're faced with some 2 week or 2 month problem it's sometimes hard to solve those with the local available expertise, but if you're connected to a global network of experts enabling you to pull in the necessary skills much more easily. That would be one of the key benefits they would experience later on.

2.2.1 How often is there the opportunity for customers to re-negotiate the contract?

Interview with Outsourcing Provider Representative 2009-04-27:
Again there is no real one answer to this question as we're dealing with a wide variety of different contracts. It's very much dependent on the individual deal, how long is it for in the first place and a lot of different things regarding, pricing, flexibility, size, all of those things.

2.2.2   Are you as a big provider more standardized than smaller ones?

Interview with Outsourcing Provider Representative 2009-04-27:

Yes, it's maybe somewhat more standardized but it's not like we're talking about hundreds of these deals each year in a local country. So a lot of them are actually quite complex as they need to meet the fit of the individual customer and their organization and perhaps they want to transfer a few hundred people out of their organization and into the outsourcing company that is set up. So there are a huge number of factors that actually need to be tailored to the individual deal, especially in the case where employees are part of it so they're actually transferred from the customer to the outsourcing deal. As such there are a lot of things you need to take into account.

2.2.3   Is that how it is usually done, when you take the existing staff and transfer them into an outsourcing company you create in the deal?

Interview with Outsourcing Provider Representative 2009-04-27:

We've seen a number of deals like that but I wouldn't say that it's standard practice. It's one of the solutions, it depends very much on what it is and how much people inside are needed to perform those functions and the customers organization. You can imagine some situations where was a fairly simple and standardized function that was being performed by customers and there isn't a need to have access to all those people in the new organization. On the other hand when you look at very complex task it will be very difficult for a new organization without any of those old employees to fulfill the same function. It varies a lot on the individual area again.

2.3 In what way do you work with continues improvements?

Interview with Outsourcing Provider Representative 2009-04-27:

We have a fairly rigid set of methods or methodology which we try to employ on all of the projects. What usually happens is that you have a fairly unstable period

in the beginning during the whole mobilization at the startup of the project. Then it's very much about closing all of the gaps and holes that you identify over time.

2.3.1 *How long does this period traditionally last?*

Interview with Outsourcing Provider Representative 2009-04-27:

I don't think again that there is any one answer for that but I think it would be very difficult to stabilize any outsourcing deal within half a year. We're talking about a fairly long period of time and of course you can discuss how unstable is it after six months but you would still be able to notice that there are some issues popping up. Some who used to be able to ring down to Jeanette on the third floor and get something done quickly, now Jeanette isn't working here anymore, she part of an outsourcing organization or maybe someone else has taken over that role in India or China. So how to make that communication work and ensure that the right person gets the status report on how it is going with that task. There are a huge number of those things, almost impossible to identify all of them up front. So it's about nailing them down and slowly fine tuning the organization so everything runs smoothly.

3. Risks

2.1 What risks can you identify for the customer when outsourcing and how do you work to prevent those?

Interview with Outsourcing Provider Representative 2009-04-27:

One of the biggest risks for the customer is that they come from an organization as I mentioned before that is fairly dynamic where they are used to be able to contact individual persons to get something done. And now they are subject to a contract, depending on how rigid the contract the customer has chosen to engage in, and of course rigidity is also a determining thing for price. The more the price goes down probably to some extent the more inflexible the contract will be. Then there is the risk that you will also have this situation where you can't get things done quickly anymore or at least the communication involves also is this part of the standard

service or do we need to do something different here. So that is one risk. Another as I see is that the customer will perhaps get into a situation where they lose control of some key area that they perhaps need to change in the longer term. So if your business is in the progress of changing over time because it is growing quite fast then it may be that you have a need for that function later on. It can be that your business contacts for your operations changes so you can actually regret that you have outsourced. You can imagine a situation like that but having that said we haven't really seen that happen so far, locally at least. I think the main one which I see happening often is that either the customer hasn't communicated things very clearly out to their people. It's part of the outsourcing process that when someone mentions they are considering outsourcing a particular function that can obviously be quite demoralizing or concerning for the people who are in that function. They will wonder if they are going to keep their jobs and who is it that they are going to be working for if they're being transferred out of the company. And of course then there is the risk that you lose some of those people and they perhaps have some key knowledge. Of course there are a bunch of different things you can do there but most important is to actually communicate early and honestly as possible. I mean of course you can't always communicate with certainty in the beginning you just started to look at the options but at least give people the opportunity to understand, ok this is how the world looks at the moment and these are the things that we are discussing. There is always the balance of confidentiality in negotiating with different suppliers. I think that the mistake some people make is that they start to communicate once they have the full answer and that day never comes because there is always a degree of uncertainty.

3.1.1   Do customers have unrealistic expectations? Is it common?

Interview with Outsourcing Provider Representative 2009-04-27:
That's of course possible. It depends on the scale you measure it on, if the customer has unrealistic expectations then that will become apparent during the negotiations. If we take that discussion from a bit earlier, the more you drive down the price of something. It's like buying a car, if you buy the absolute cheapest model then you can't at the same time expect that it got the

adjustable mirrors, the sunroof, air conditioning and the V8 engine. I think it's important to realize that there is a tradeoff between the flexibility and the price. In negotiating with us we try to be open and honest about that, I'm also talking about this in a more general context for outsourcing it's not specific to any customer. It's a general view that if you gone into a deal for saving money that you also need to balance that off against the other consequences of the low pricing.

3.1.2 *How does the process of choosing a provider normally look like? Do they normally negotiate with other companies as well?*

Interview with Outsourcing Provider Representative 2009-04-27:
That can really vary a lot again. Do we have a long standing engagement with them, do we have a very strong trust relationship with the customer, that´s one factor. Typically though, for larger firms of course, most companies or organizations would issue some sort of a tender or a request for proposals for different outsourcing companies to come with their offer and how they would solve the problem and an indication of the costs.

3.2 *One of the main issues with outsourcing is that customers, even if they still have insight in their economy, risk loosing control over the company. What is you view on that? How do you work to prevent possible loss of control? What measures are taken? If the control is passed from the customer to you, do you think that it could have any positive / negative effects for the customer, if so, which?*

Interview with Outsourcing Provider Representative 2009-04-27:
Of course there is always going to be a concern for any senior business person that they don't have control of a function in the same way as before. It's a matter of building in some sort of service level agreement for that function. You can of course measure the level of service you have in a lot of different ways, the least complex level is the number of errors that get fixed per month or something similar. But it can also be the slightly softer values that you also try to measure

in some way, the satisfaction amongst your own employees by the service provided by that function.

3.3   How do you handle your customers' confidential materials?

Interview with Outsourcing Provider Representative 2009-04-27:
We have an extremely tight set of rules for how we handle all data. There are numerous legal operation laws we need to fulfill in the countries we operate in, and also extensive internal policies. It has enormous consequences if we don't do things right. You need to look at; who is it that you want to communicate with, there are fairly clear rules on which you are allowed to send to. What data they can send, and to whom. Also, if they're outside the closed network, it needs to be encrypted. They don't use any sort of private mails or anything. We have clear policies about that.

Interview with Outsourcing Provider Representative 2009-04-27:
If you don't do it right, the consequences are catastrophic.

4.   Relationship

4.1 Have any additions ways of treating problems arising with customers?

Interview with Outsourcing Provider Representative 2009-04-27:
We have, I guess in our culture, we always try to make sure the customer is satisfied; it is fairly service-oriented company. The reason for the problems, they can be quite varied, specific to the way the customer works. Ultimately, one of the most important things to realize is that we have something closer to a partnership, than to a customer / supplier relationship. If you find practice, which allows both organizations to have whole set of interests, you solve a lot of big issues. Give an example: If a client find ways to do thing cheaper or save money, if both supplier and the customer have a share in any profitability gains you have from streamlining the process, that has a huge benefit, it really means a lot in the amount of effort the vendor makes to do things in a better way or make it in a

cheaper way.

Translated from Interview with Outsourcing Provider Representative 2009-04-27:
The alternative is where they create incentives where the parties start pulling in different directions from one another. Supplier has the interest of making their work as profitable as possible, and the customer wants it as cheaply as possible. So you have contradicting goals.

4.1.1 *And then risk the relationship; this would be one of the key factors to have an effective partnership?*

Interview with Outsourcing Provider Representative 2009-04-27:
There is always going to be some sort of difference, because of course there is the price factor. If you find some sort of reasonable level, where you can give both parties incentive to co-operate, that also comes down to the bottom level, the guys out there, working together, they will experience it as a far more harmonious outsourcing relationship if it is like that. Every time they get some little things done, and they feel they need to get some budget allocation, or fill out 3 or 4 forms to get it approved, before they could just call someone up and have him do it.

4.2 *How important do you consider a close relation / good communication with the customer is, and you gaining their trust?*

Interview with Outsourcing Provider Representative 2009-04-27:
You also need to have the top level a very good co-operation between the senior leaders from both organizations, they need to feel they trust one another, if there are any issues, they get it fixed. And this is in both directions. I think the other key to work on is to understand each other's culture. Just because the company has some way of doing things. So it's important to spend some time, especially for the supplier for understanding the way that the customer works. The People that they have employed there and the underlying culture of the organization, especially large value of doing things in a way. Do they have some sort of core value

inherited from the founder of the company a hundred years ago?

4.2.1 *So there is always research connected to the outsourcing relationship?*

Interview with Outsourcing Provider Representative 2009-04-27:
Not so much research, just as much as talking to one another and maybe training also, working with this outsourcing customer so making sure they understand the context they're working in. It is not just a generic line from an excel sheet, it is a company with a specific set of values that they are.

4.2.2 *Do you on a regular basis measure the satisfaction?*

Interview with Outsourcing Provider Representative 2009-04-27:
Yes, we do. But that is general for all our projects.

5. Conclusion

4.1 What is your view on the outlooks of the outsourcing industry? Will it continue on a more focused path in the future?

Interview with Outsourcing Provider Representative 2009-04-27:
I can't see any reasons for these mega deals you saw a couple of years ago. A number of companies have maybe burnt their fingers, and have become wiser. I think we will slightly smaller deals.

5.1.1 *But isn't there an advantage with having big IT platforms, wouldn't that give an incentive to merge more functions into one supplier?*

Interview with Outsourcing Provider Representative 2009-04-27:
In a lot of cases there are locally applicable accounting rules. You can't send anywhere in the world without thinking actively about it. Most companies already have a fairly well integrated IT, that can handle all these back office,

and nearly everybody have some sort of (ja ve)? Systems as they call it, which performs key financial salary functions. I think that's already been in place for the last couple of years.

Interview with Outsourcing Provider Representative 2009-04-27:
I still think it's a series of smaller deals, it can be with the same vendor, but it will still be done in pieces, so you take one function, and get it under control, then you take another function a year later and get that under control.

Interview with Outsourcing Provider Representative 2009-04-27:
I think we are more likely to see smaller deals, for the reasons I have mentioned before.

5.1.2   *The outsourcing deals can be big in that way, but you take it piece by piece?*

Interview with Outsourcing Provider Representative 2009-04-27:
Yes, but it is made in a chain of smaller deals. The result can still be large, but one massive outsourcing deal, instead of specific deals which have their own set of six step parameters and performance indicators.

5.1.3   *Can you see more and more of those portfolio-type companies, where almost all functions have been outsourced?*

Interview with Outsourcing Provider Representative 2009-04-27:
I haven't seen it myself. You could imagine where there will be more often and almost only have the brand left. That would kind of be the extreme case. Where you only keep the one or two aspects of the company that makes you special, and push everything else off. But I think we are still some way of that from happening

5.2 What advise would you give to a company considering outsourcing a business function?

Interview with Outsourcing Provider Representative 2009-04-27:

I think as a first step, what they're trying to achieve by outsourcing? Are they just trying to save money, to enhance their flexibility so they perhaps can handle the swings or are they trying to get access to specific set of skills they don't have internally.

Interview with Outsourcing Provider Representative 2009-04-27:

When they included that it is the right thing to do, then they should look very carefully at what the trade-offs are; between flexibility and costs for example. And keep those in mind when selecting the vendor. And also think very much about the idea of having a partnership rather than a pure customer / supplier relationship.

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