

Outsourcing Strategically for Sustainable Competitive Advantage



A Joint Research Study by CAPS Research and A.T. Kearney, Inc.

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EXECUTIVE SUMMARY

BACKGROUND TO THE RESEARCH

Outsourcing has grabbed headlines in the past few years. Some proclaim it as a necessary, effective, and inevitable strategy to reduce costs, focus on the core business, maintain competitiveness, and obtain needed capabilities. Others see outsourcing as a threat to jobs, companies, industries, and whole economies. And numerous studies point to significant growth in outsourcing in the next few years, further fuelling the debate.

Barring a substantial reversal of current trends, outsourcing is here to stay. With that in mind, CAPS Research and A.T. Kearney, Inc. undertook a research study to understand the trends in outsourcing, how outsourcing decisions are made, and most importantly, how companies can be more successful in achieving their goals for outsourcing. The research team gathered survey data from 165 procurement executives or their functional peers across 24 industries globally and supplemented the surveys with select participant interviews.

KEY FINDINGS

The survey shows that companies use outsourcing broadly across many activities, but when viewed in terms of the amount of each activity outsourced, it appears that outsourcing is generally not being done very deeply. Activities with the greatest current level of outsourcing include information technology, distribution/fulfillment, legal/regulatory, manufacturing/operations, engineering/detailed design, and call centers.

Cost and focus are the primary drivers of outsourcing, with more than 80 percent of respondents indicating that cost reduction (in operating cost and capital investment) and the need to focus on the core business led them to outsource. While companies report that they are generally meeting or exceeding their cost goals for outsourcing activity, revenue goals are not being met.

The research further revealed that the approaches used to manage outsourcing influence company performance against outsourcing goals. The research defined a three-phase prescriptive model — strategy planning and analysis, contracting and relationship development, and implementation — and analyzed statistical responses, verbatim comments, and interviews with survey respondents to identify strategies and practices that affected performance levels.

The research also explored the role of the procurement organization in outsourcing decision-making and management. Procurement's involvement in outsourcing has been highest in other operational areas of the business (e.g., manufacturing, distribution, and fulfillment) and far less in outsourcing of administrative activities, demand-side activities such as sales and marketing, and research and technology. When procurement is involved in the process, however, there is a clear link with greater success. The research also pointed to an increase in outsourcing of procurement itself, particularly related to transaction processing and to the management of categories that are not directly related to the company's product.

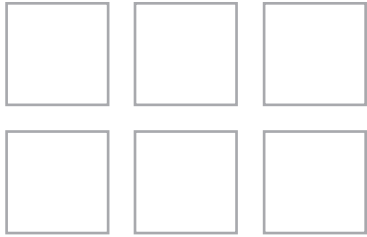
GUIDANCE FOR SENIOR MANAGEMENT

Although the research found that outsourcing is currently a common tactic used by many companies, we did not see widespread evidence of companies thinking strategically about outsourcing as a way to fundamentally rewrite the rules for competing. To this end, the research team married its analysis of the survey and interviews with its considerable academic and management consulting experience to offer perspectives on how companies *can* use strategic outsourcing as a competitive weapon. This report describes how tomorrow's environment for outsourcing may be different, provides examples of approaches that could create new opportunities, discusses a set of factors that companies should consider in selecting options, and highlights some of the execution issues that must be addressed.

RECOMMENDATIONS FOR FUTURE RESEARCH INTO STRATEGIC OUTSOURCING

The research summarized in this report establishes a baseline for current and planned levels of outsourcing and offers a three-phase process model and a framework for strategic outsourcing. The research also identifies several questions that future research in this area could address, thereby expanding and deepening the knowledge base on managerial issues in strategic outsourcing:

- How has the level of outsourcing changed since this survey? What factors contributed to greater or lesser growth than forecast?
- What are the country - and region - specific patterns and trends in domestic versus offshore outsourcing?
- What strategies and processes do companies employ for “insourcing” new work and work already outsourced?
- How prevalent will procurement outsourcing be? What will the dominant operating models be by the end of this decade?
- What additional factors and considerations are related to long-term strategic outsourcing?
- To what extent are companies using tradition or history to define core competencies? Could improved definitions and evaluation techniques potentially increase the scope of activities considered for outsourcing?
- Under what conditions could outsourcing lead to the demise of a company? What counteractions can executives take to prevent this?



CHAPTER 1: INTRODUCTION

Outsourcing has been a key business strategy used by companies in many industries for more than a quarter of a century. Automotive companies have been outsourcing manufacturing operations, business services, and even entire lines of business since the early 1980s. More recently, the contract manufacturing sector has developed with considerable outsourcing by electronic industry original equipment manufacturers (OEMs). Business processes such as information technology, logistics, human resources management, payroll, and certain elements of procurement have also been outsourced.

Across the globe, competitive pressures and the need for quarter-to-quarter financial performance improvement are driving an increase in the magnitude of outsourcing across industries worldwide. Companies are establishing and executing outsourcing plans in order to:

1. Match competitors in their outsourcing endeavors
2. Improve non-competitive cost structures
3. Focus on core competencies and reduce capital investment and overall fixed costs
4. Achieve cost competitive growth in the supply base for goods, services, and technologies in a company's value chain
5. Establish a future sales footprint in a low-cost country by outsourcing simple goods or business processes

These factors are forcing companies to fully evaluate their outsourcing models to determine their viability in today's highly competitive world. Effective outsourcing requires established processes to help determine:

- What to outsource and why
- How to find the suppliers that align best with future plans
- How to establish relationships and define contracts, execute the transition plan and measure results, and take corrective actions as necessary

OUTSOURCING DEFINED

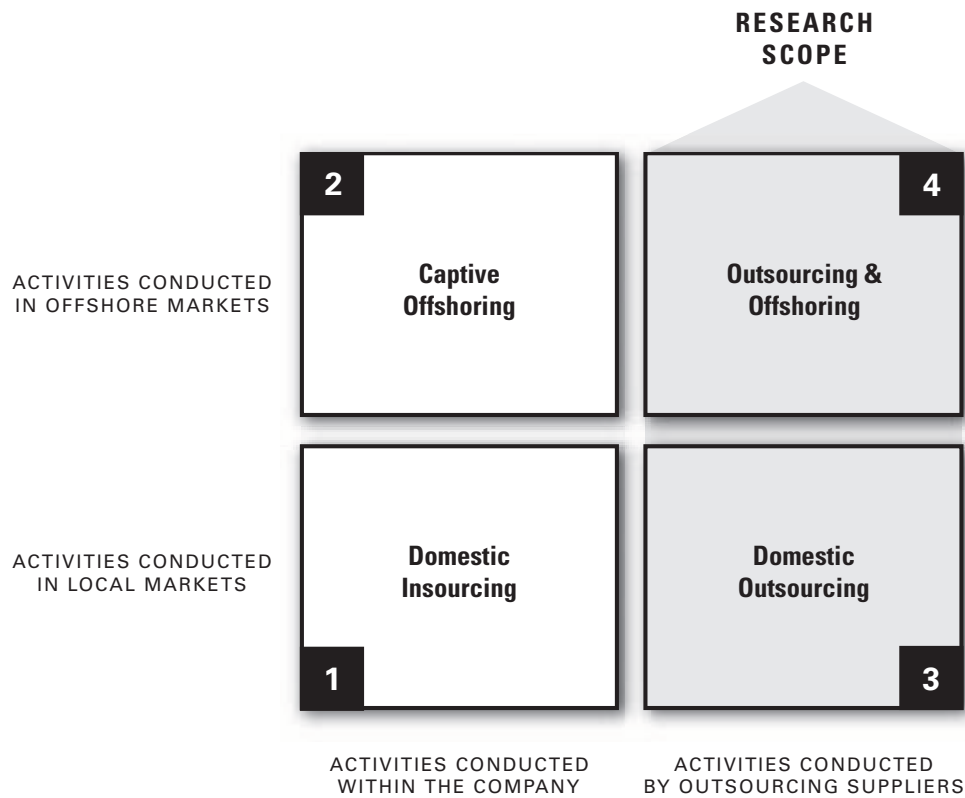
There is a clear distinction to be made between two oft-confused approaches: outsourcing and offshoring. The Institute for Supply Management defines the two terms as follows:

Outsourcing: "A version of the make-or-buy decision in which an organization elects to purchase an item that previously was made or a service that was performed in-house; often utilized for services. It involves sourcing and using a supplier that provides the completed item or service rather than buying the components and manufacturing them in-house."

Offshoring: "Being located or operating outside a country's boundaries."

Outsourcing and offshoring are somewhat similar in that they involve the transfer of work activities away from a company's domestic operations. The two approaches can also overlap, as Figure 1.1 illustrates.

FIGURE 1.1: RELATIONSHIP OF OUTSOURCING AND OFFSHORING



In looking at Figure 1.1, quadrant 1 represents the traditional model for insourcing, which keeps work in-house and onshore. Ford's River Rouge, Michigan, plant is a classic example of a domestic insourced operation. In its time, it was the largest industrial complex in the world. The automotive assembly operation was fed by an on-site steel mill, foundry, machine tool fabrication, and safety glass and tire manufacturing operations. Raw materials — chiefly iron ore, coal, sand, and rubber — entered the plant, and finished automobiles exited it.

Across many industries, a significant shift came in the early 1980s, when manufacturing work began to migrate to areas that offered lower labor costs. Initially, this was done on a regional basis, as happened within the United States when manufacturing moved from expensive urban areas to rural locations that offered cheaper land, tax incentives, and employees willing to work for lower wages. More recently, firms have moved their internal manufacturing and operations to lower cost countries, represented by quadrant 2. Large companies like General Electric and Dell have moved select service functions (such as call centers and back-office processes) to lower-cost countries while keeping them in-house as company-run operations. This movement is not solely motivated by the pursuit of low-cost labor sources, but also by the desire to be closer to and gain improved access to foreign markets. Consider, for example, that Japanese and German automakers have established “offshore” manufacturing sites in the United States.

During that same period, companies started to outsource non-core activities to local or regional suppliers that provided specialized expertise and lower costs, as shown by quadrant 3. The rise in the IT outsourcing, contract manufacturing, and third-party logistics industries characterize this activity.

Most recently, companies have moved to the activity depicted by quadrant 4, in which work is simultaneously offshored and outsourced. Although the work being transferred to India- and China-based suppliers has received the majority of the headlines, countries such as the Philippines, Brazil, Russia, Ireland, and the Czech Republic are also significant locations for offshoring.

Improved financial performance is the most frequently cited benefit to be obtained from the outsourcing of goods, services, and business processes. But for the uninitiated, the process is also fraught with potential difficulties around the decision-making process, loss of critical capabilities, cultural issues, union problems, and underperformance from new suppliers. A clear, well-thought-out strategy is key to maximizing outsourcing's benefits while avoiding its pitfalls.

Companies must establish a viable and well-understood outsourcing strategy upfront that includes a careful consideration of what goods and services — and possibly whole lines of business — are most suited to this approach. They need to establish current and future expectations for outsourced suppliers, and perform due diligence *vis a vis* the capabilities of the chosen suppliers. The company must also be able to execute the outsourcing and transition of work. Finally, supplier performance must be closely tracked, accompanied by any corrective actions required in tandem with ongoing management and development of the new supply base.

OBJECTIVES AND FOCUS OF THIS RESEARCH

In late 2003, a research team from CAPS Research and A.T. Kearney began a global research study that had three primary objectives:

1. Understand how companies plan for and manage their strategic outsourcing relationships.
2. Determine which strategic outsourcing management approaches are the most effective for achieving superior results.
3. Help clarify the current state of procurement outsourcing.

The scope of this research is mostly limited to **outsourcing** — quadrants 3 and 4 in Figure 1.1 — where work has been transferred to an outside supplier, either locally based or in an offshore location. In addition, strategic outsourcing goes far beyond make/buy decisions. The focus of strategic outsourcing decisions can include core competency analyses, lines-of-business, and any product or service worldwide. The overarching goal of our study was to gather and share insights from leading companies about their experiences with outsourcing in order to help businesses think through the complexity of their own strategies and achieve greater success from their outsourcing endeavors.

RESEARCH APPROACH

As our main source of primary data, the team developed a survey (see Appendix B) that profiled each respondent company's current and future levels of outsourcing, its reasons for and against outsourcing, levels of performance against outsourcing goals, and degree of influence that certain factors had on performance levels. The survey also asked respondents to identify the business activities with which they had experienced their most positive and negative outsourcing results, and to describe the factors that contributed to these levels of performance.

Additionally, the survey examined outsourcing from a procurement-centric perspective. First, we asked respondents to identify the level of involvement of the procurement organization in the strategic outsourcing process for the corporation. Second, we inquired about the level of outsourcing for procurement activities themselves.

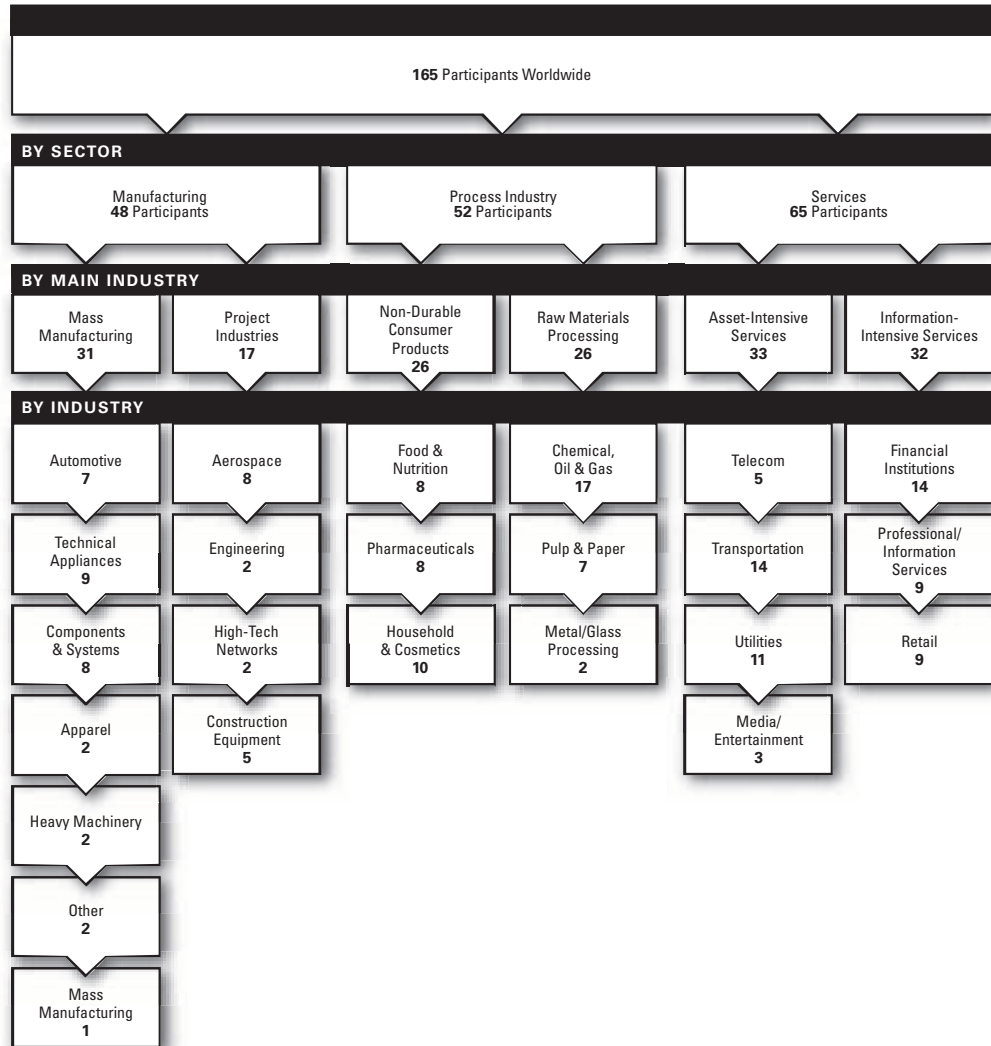
PARTICIPANT DEMOGRAPHICS

Approximately 1,000 companies were invited to participate in the survey. Solicited companies included CAPS Research member companies, members of the Institute for Supply Management and equivalent organizations in other countries, and previous participants in A.T. Kearney's global *Assessment of Excellence in Procurement* research studies. Invitations were sent to procurement executives where possible, or to related functional executives (e.g., finance and administration) in cases where the procurement executive could not be identified. Responses were received from 165 companies (a 16.5 percent response rate), who completed the survey online between October 2003 and January 2004.

The research also included interviews with 15 companies that were specifically chosen based on their responses to the survey. These interviews provided a deeper understanding of the approaches currently being used to manage the strategic outsourcing process.

The survey respondents represented 24 industries. For analysis purposes, the research team grouped these companies into six main industry types, then further grouped them into three sectors, as shown in Figure 1.2.

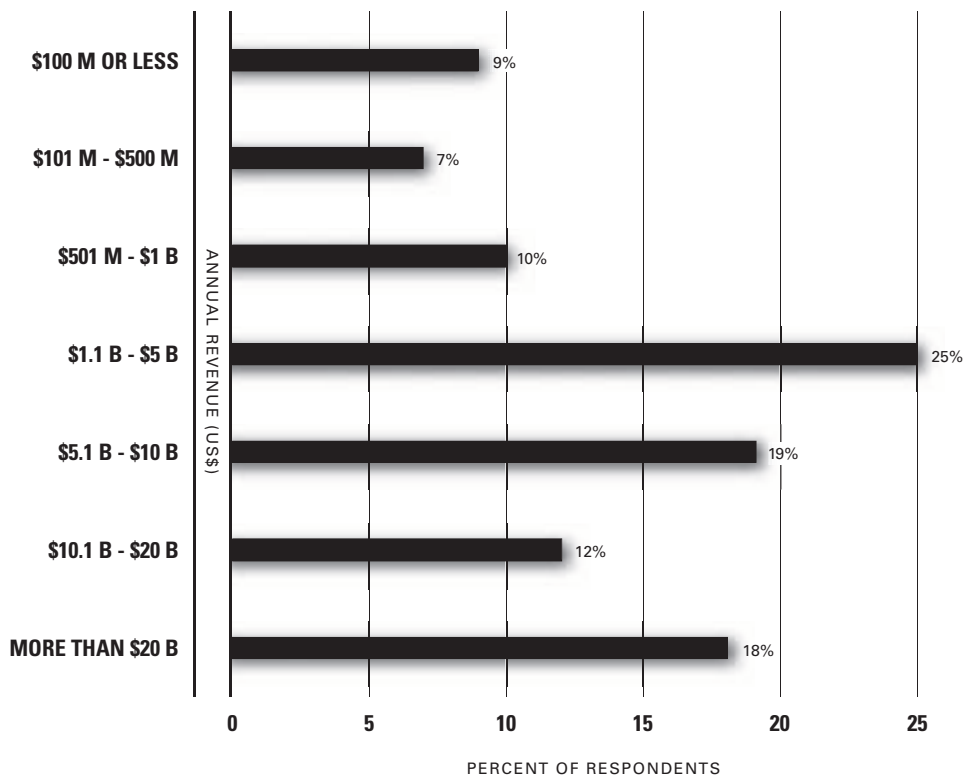
FIGURE 1.2: INDUSTRY PROFILE OF PARTICIPANTS



Source: Strategic Outsourcing Survey, 2004, Primary Industry

Participants ranged in size from just under US\$100 million in revenues to more than US\$20 billion, although most were at US\$1 billion or more (see Figure 1.3).

FIGURE 1.3: COMPANY SIZE OF STUDY PARTICIPANTS BY ANNUAL REVENUES



Source: Strategic Outsourcing Survey, 2004, Primary Industry

Participating companies represented a broad geographic footprint. Although 65 percent of these companies have their primary bases of operations in five or fewer regions or countries (most notably North America, Western Europe, and China), 44 percent go to market in 12 or more countries or regions.

REPORT STRUCTURE

The remainder of this document explores the topics below and provides answers to the following questions:

Chapter 2 — The State of Outsourcing Today

- How widely used is outsourcing?
- How deeply has outsourcing penetrated company value chains?
- What is being outsourced and why?
- What growth is expected for outsourcing?

Chapter 3 — A Prescriptive Model for Strategic Outsourcing

- What process should be followed to increase the likelihood of outsourcing effectiveness?
- What factors drive positive outsourcing results?
- What goals do companies have for outsourcing, and what results have they achieved?
- What have companies learned from their outsourcing initiatives?
- What are some examples of effective and ineffective outsourcing practices?

Chapter 4 — A Closer Look at Procurement

- What role does procurement play in the strategic outsourcing process?
- Why and to what extent is procurement itself being outsourced?

Chapter 5 — Thinking Strategically about Outsourcing

- How might tomorrow's economic, social, political, and business environments influence outsourcing decisions?
- What opportunities and possibilities exist for companies using strategic outsourcing?
- How should executives think about outsourcing in a changing environment?
- What are the executional issues to consider?

Appendices

- Appendix A — Management Considerations for Outsourcing Procurement Activities
- Appendix B — Survey Questionnaire
- Appendix C — Description of Statistical Analysis Methodology

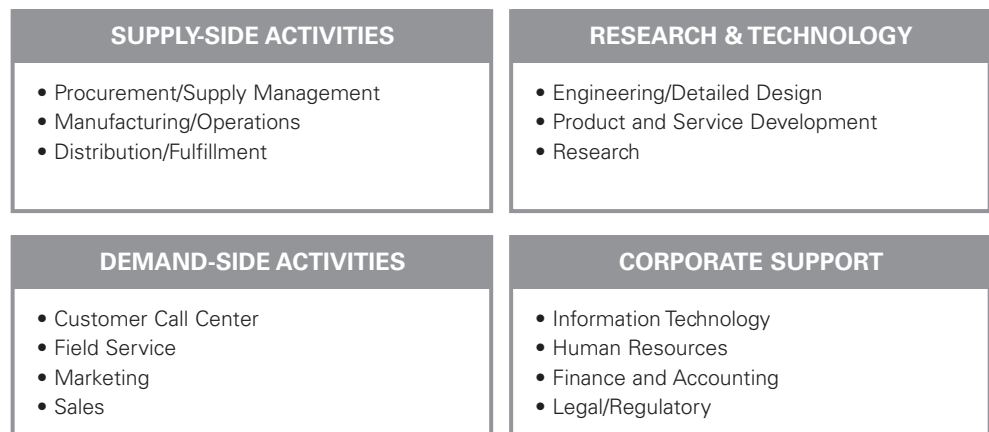


CHAPTER 2: THE STATE OF OUTSOURCING TODAY

CURRENT PATTERNS OF OUTSOURCING

The survey asked respondents to consider 14 distinct business activities and identify both their current levels of outsourcing and their planned levels of outsourcing over the next 18 months in these areas. To aid in subsequent analysis, these activities were divided into four types: supply-side activities, demand-side activities, research and technology, and corporate support (see Figure 2.1).

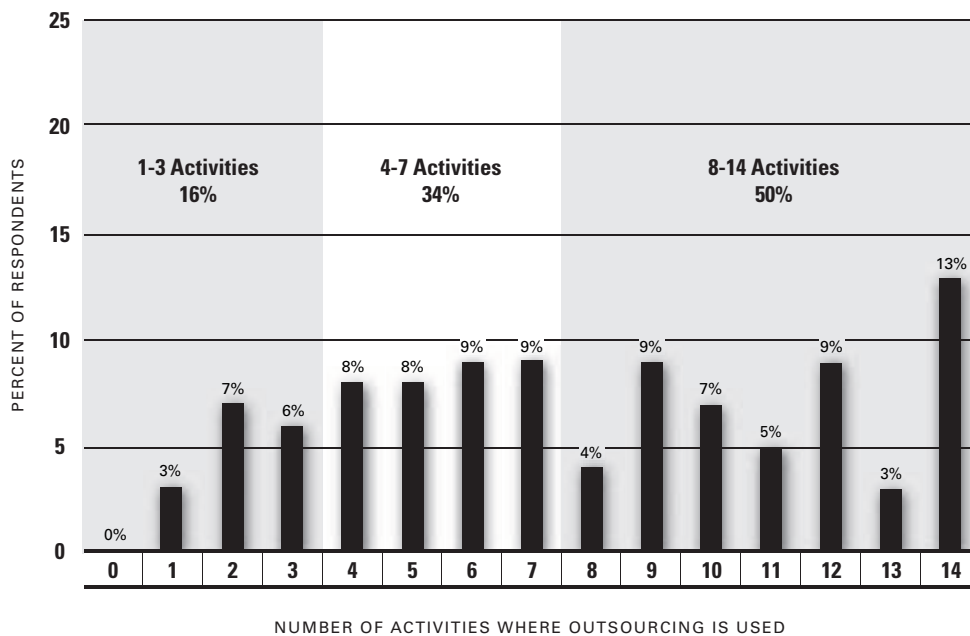
FIGURE 2.1: BUSINESS ACTIVITIES EXAMINED IN THE RESEARCH



We looked at levels of outsourcing in two ways. First, did the company outsource any part of an activity? Second, what amount of each activity did it outsource?

In the first case, the survey data shows that companies use outsourcing broadly across many activities. For example, half of the respondents use outsourcing for eight or more of the activities surveyed (see Figure 2.2). Another one-third of respondents outsource elements of between four and seven activities.

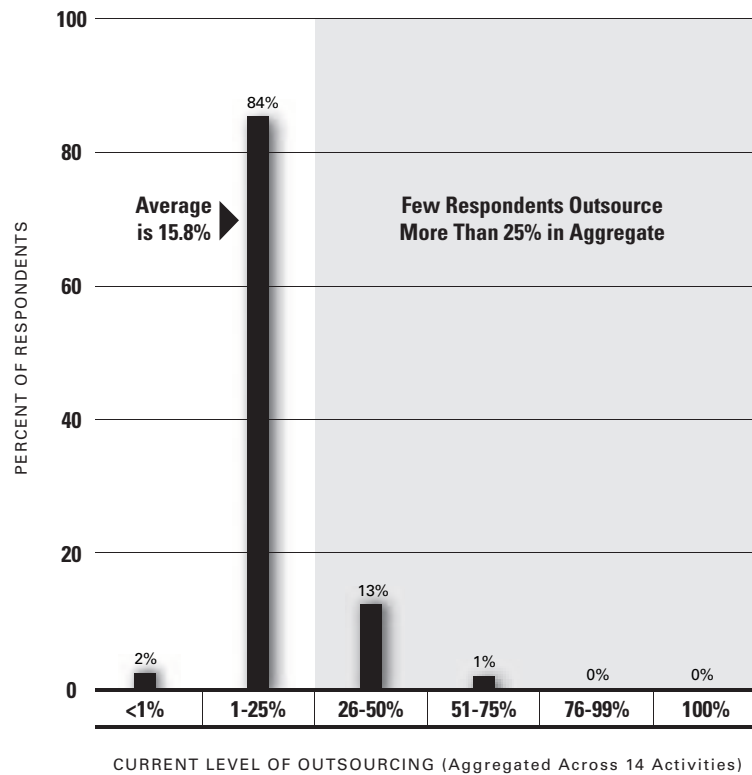
FIGURE 2.2: BREADTH OF OUTSOURCING ACROSS 14 ACTIVITIES



Source: Strategic Outsourcing Survey, 2004, Question 1

However, when viewed in terms of the amount of each activity outsourced, outsourcing is generally not being done very deeply — the typical portion of any given activity that is being outsourced is relatively low. Even for information technology, the activity with the deepest level of outsourcing penetration, only 14 percent of respondents indicated that they outsource more than 25 percent of that activity (see Figure 2.3).

FIGURE 2.3: OUTSOURCING PENETRATION LEVEL

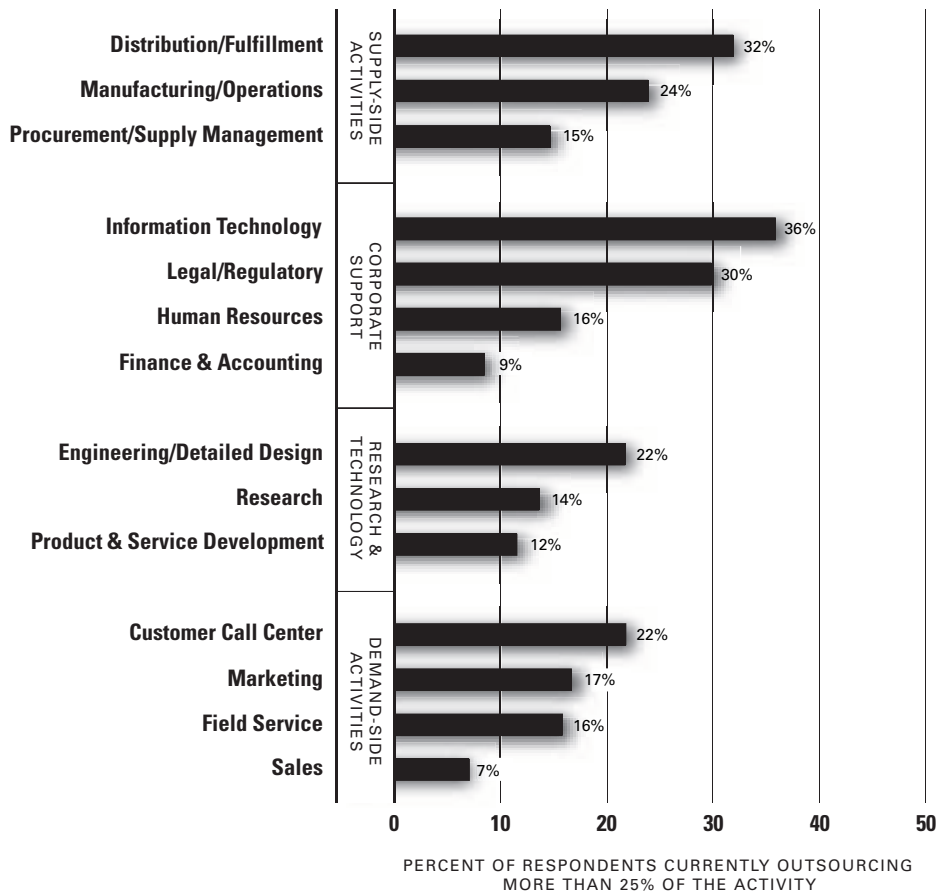


Source: Strategic Outsourcing Survey, 2004, Question 1

This reflects the fact that many activities can be broken down into sub-activities that companies can then outsource without sending the full activity outside. For example, in the IT area, a company might choose to outsource desktop support but not Web hosting, or applications maintenance but not applications development. In fact, across all 14 activities, the average level of outsourcing penetration is 15.8 percent as shown in Figure 2.3.

For the purposes of our study, 25 percent penetration constitutes the threshold for “significant outsourcing” of an activity. Reflecting this threshold, Figure 2.4 shows the current levels of significant outsourcing for all 14 activities across the respondents. In addition to information technology, activities with the greatest current level of outsourcing include distribution/fulfillment, legal/regulatory, manufacturing/operations, engineering/detailed design, and call centers.

FIGURE 2.4: LEVEL OF “SIGNIFICANT” (25 PERCENT OR MORE OF AN ACTIVITY) OUTSOURCING BY ACTIVITY

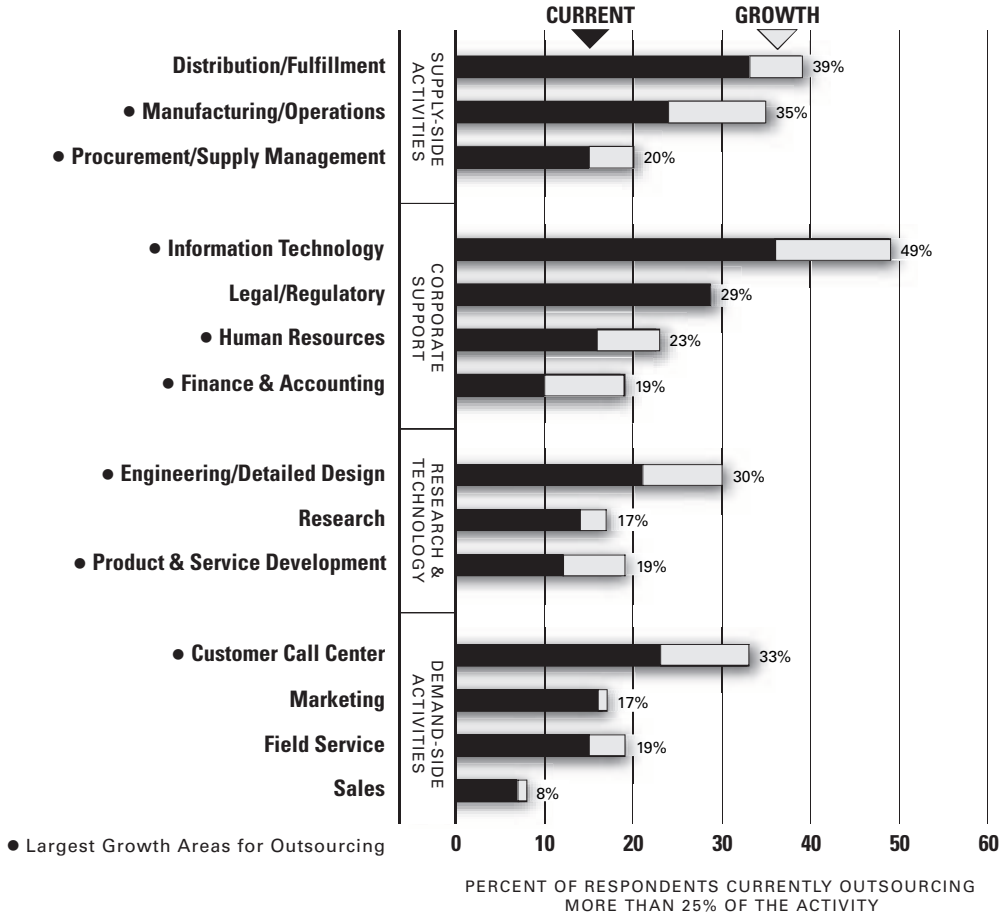


Source: Strategic Outsourcing Survey, 2004, Question 1

PROJECTED GROWTH IN OUTSOURCING

Figure 2.5 builds on Figure 2.4 by adding projected growth over the next 18 months. Looking ahead, the greatest growth areas are expected to be information technology, manufacturing and operations, procurement and supply management, human resources, finance and accounting, engineering and detailed design, product and service development, and call centers.

FIGURE 2.5: ANTICIPATED FUTURE OUTSOURCING LEVELS BY ACTIVITY

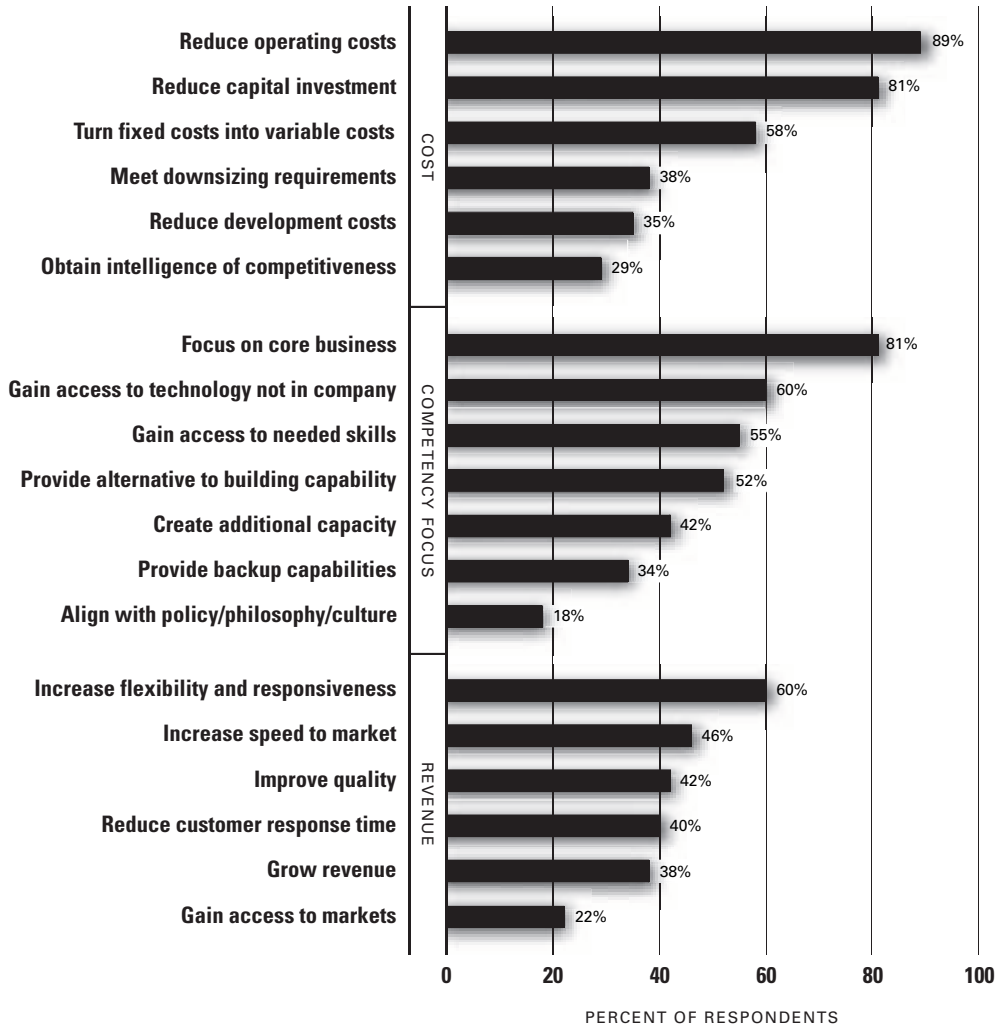


Source: Strategic Outsourcing Survey, 2004, Question 1

PRIMARY REASONS TO OUTSOURCE OR NOT OUTSOURCE

Companies have been pursuing outsourcing for a variety of reasons that can be grouped into cost, competency focus, and revenue considerations (see Figure 2.6).

FIGURE 2.6: REASONS CITED FOR OUTSOURCING AN ACTIVITY

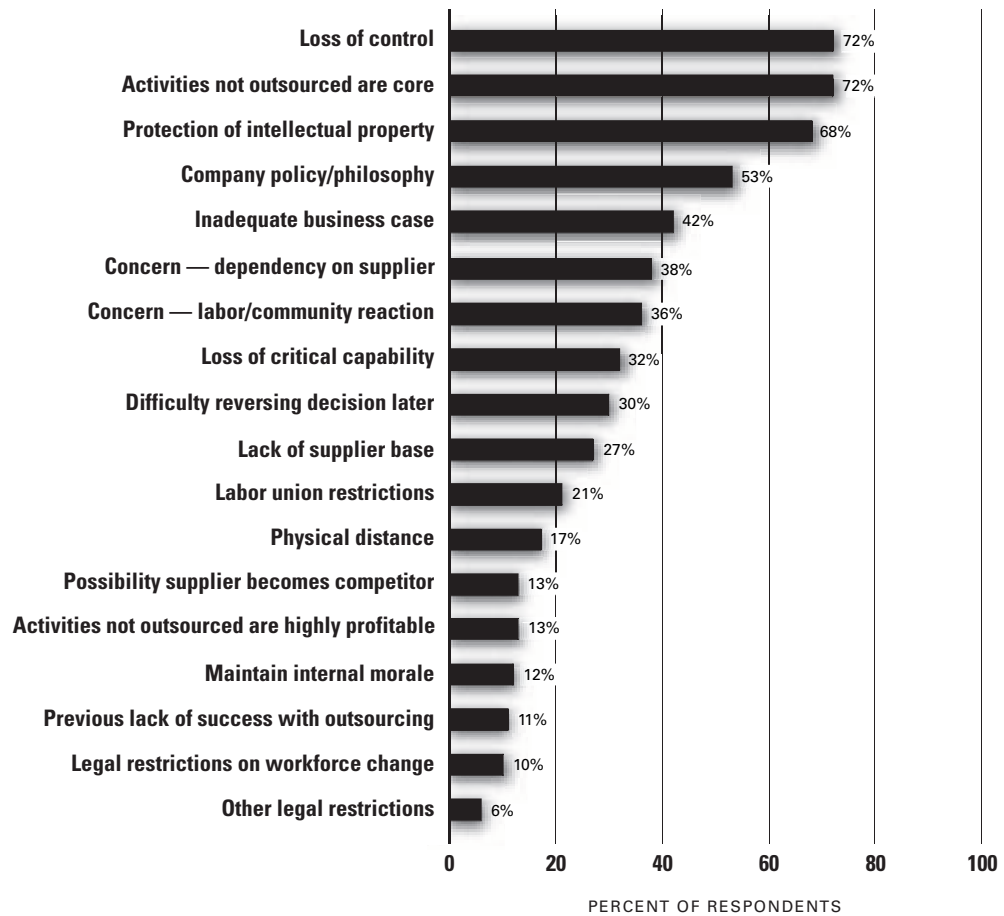


Source: Strategic Outsourcing Survey, 2004, Question 3

One message is clear: at this time, cost and focus are the primary drivers of outsourcing, with more than 80 percent of respondents indicating that cost reduction (operating cost and capital investment) and the need to focus on the core business led them to outsource. Generally, fewer than half of the respondents cited revenue-growth-related reasons for outsourcing.

Among the primary reasons companies chose not to outsource were concerns over loss of control, the individual company's belief that the remaining in-house activities were core, and protection of intellectual property. As shown in Figure 2.7, more than half of the respondents also noted that outsourcing is contrary to their company policy or philosophy.

FIGURE 2.7: REASONS CITED FOR CHOOSING NOT TO OUTSOURCE AN ACTIVITY

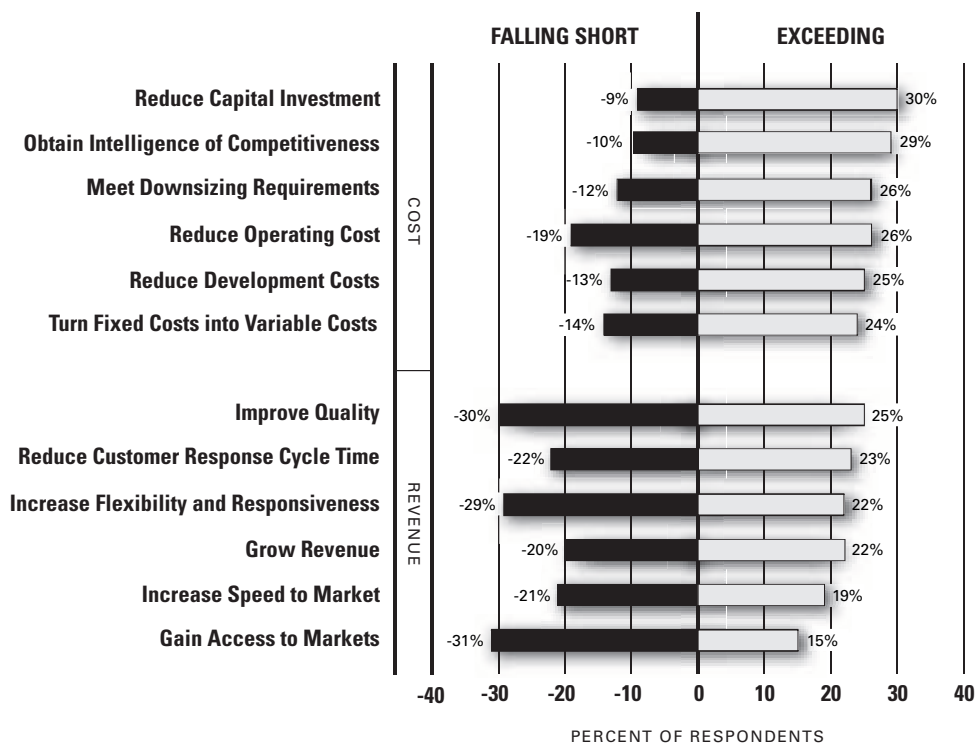


Source: Strategic Outsourcing Survey, 2004, Question 4

GOAL ACHIEVEMENT FROM OUTSOURCING

While companies report that they are generally meeting or exceeding their cost goals for outsourcing activities, revenue goals are not being met. Figure 2.8 compares the percent of companies exceeding goals with the percent falling short for each activity (for clarity, the percent meeting goals is not shown). The majority of companies with cost-related goals for outsourcing met or exceeded their goals, while those with revenue-related goals had less success, with more companies falling short of goals than exceeding them.

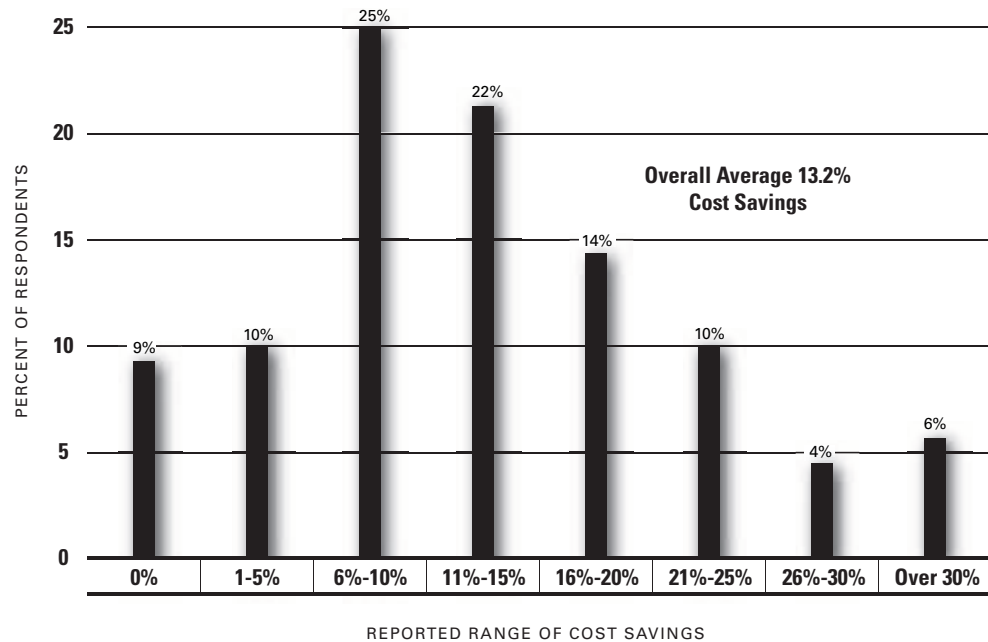
FIGURE 2.8: PERCENT OF RESPONDENTS EXCEEDING AND FALLING SHORT OF OUTSOURCING GOALS



Note: Sample sizes range from 40-118 companies citing individual goals
 Source: Strategic Outsourcing Survey, 2004, Question 5

Respondents were asked specifically about the level of cost savings achieved through outsourcing and the speed to realize savings. As Figure 2.9 illustrates, the overall cost savings reported by respondents averaged 13.2 percent. More than one-third of respondents reported cost savings in excess of 15 percent, while only 9 percent reported no savings from outsourcing.

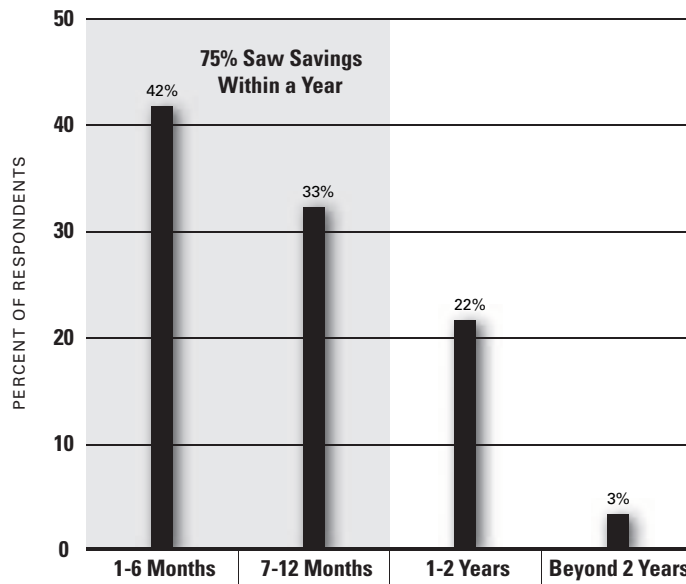
FIGURE 2.9: PERCENT OF RESPONDENTS BY REPORTED RANGE OF COST SAVINGS



Source: Strategic Outsourcing Survey, 2004, Question 6

Figure 2.10 displays the time to savings. Three-quarters of the respondents realized savings within a year of implementing outsourcing, while just 3 percent had to wait beyond two years to see savings.

FIGURE 2.10: REPORTED TIME TO REALIZE SAVINGS FROM OUTSOURCING



Source: Strategic Outsourcing Survey, 2004, Question 7

Given that cost reduction is the primary short-term outsourcing goal, we believe companies are initially focusing on projects with a fairly narrow focus and higher savings potential that are easier to implement and that do not affect core business strategies. This helps to explain why 75 percent of companies saw savings in the first year.

More complex strategies involving many functions in the organization and possible development of a supply base will be required for companies to achieve significant longer-term cost reductions. For example, the outsourcing of the complete design, development, manufacturing, and distribution of a product line will require executive management, technology, manufacturing, supply chain, and marketing alignment, collectively increasing decision-making complexity. In addition, the increased cost of managing the transition will require higher overall financial returns. Finally, the supply base may require development to execute the complete design-to-customer order-fulfillment process.

FIGURE 2.11: DECISION-MAKING MODEL FOR EVALUATING OUTSOURCING OPPORTUNITIES

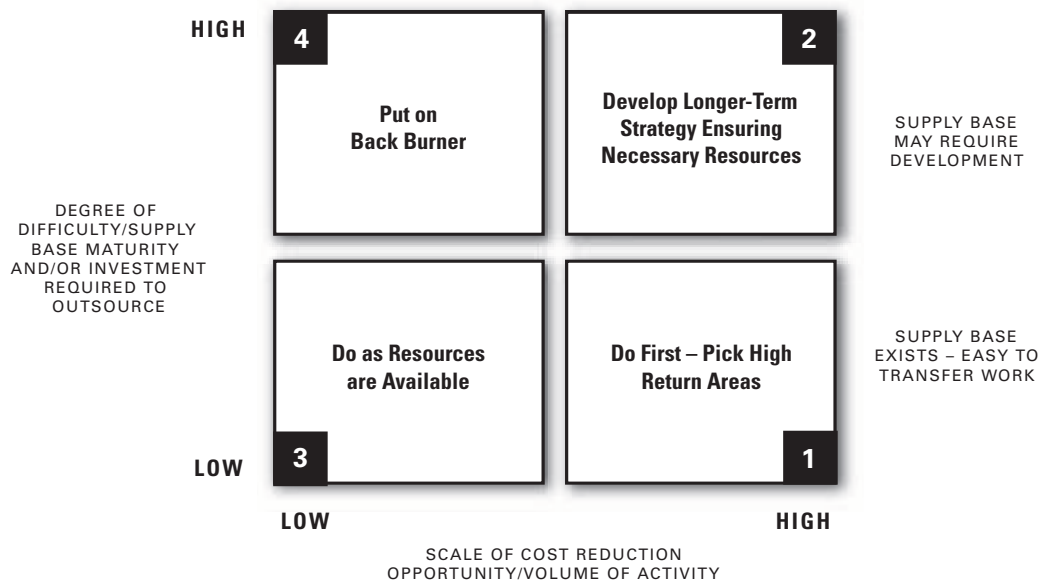
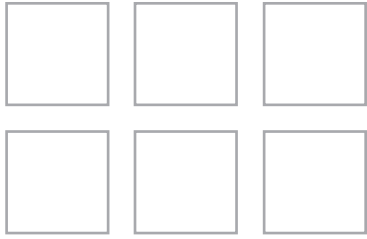


Figure 2.11 is a descriptive decision-making model for evaluating outsourcing opportunities in terms of both the size of opportunity and degree of difficulty. Examples of outsourcing in quadrant 1 include the early outsourcing of “board stuffing” in electronics and call center services by many firms. Quadrant 2 examples include seat design, engineering, and manufacturing in the auto industry and structural component/system outsourcing in aerospace. An example of quadrant 3 might be cafeteria services or facilities maintenance, where the complexity of outsourcing is relatively low, but the returns are low as well. Finally, in quadrant 4, the low size of the opportunity coupled with internal constraints (e.g., potential labor disruption) or the lack of a mature external supply base may preclude a current outsourcing action.



CHAPTER 3: A PRESCRIPTIVE MODEL FOR STRATEGIC OUTSOURCING

DEVELOPING A PRESCRIPTIVE MODEL

As a core part of the research, we undertook the development of a prescriptive model to help guide companies toward superior results through strategic outsourcing. Based on our prior experience, we began the research with the five-phase model shown in Figure 3.1. This model guided the development of the overall research questionnaire in Appendix B.

FIGURE 3.1: INITIAL FIVE-PHASE MODEL OF THE STRATEGIC OUTSOURCING PROCESS



Using the model, we identified 24 factors (shown in Figure 3.3) related to the process of outsourcing and connected these to the five phases. These activities were viewed as critical to achieving positive outsourcing results, and they formed the basis for a series of questions in which respondents were asked to specifically rate the degree to which each activity contributed to the level of performance against outsourcing goals.

Through the statistical analyses described in Appendix C, we developed two important findings regarding the model:

1. Our original assignment of the factors among the five-phases model was statistically valid.
2. The factors could be reassigned into a simpler three-phase model that had even higher statistical validity, as shown in Figure 3.2.

FIGURE 3.2: REFINED THREE-PHASE STRATEGIC OUTSOURCING MODEL



The new, three-phase model combines the first two phases from the original model (“strategy and planning” and “analysis and decision-making”) into a new first phase that we titled “strategy planning and analysis.” The majority of activities in the original middle phase remained in place, making a new phase that we titled as “contracting and relationship development.” The new three-phase model combined the last two phases from the original model (“transitioning and implementing” and “ongoing management and measurement”) into a new third phase titled “implementation.” The 24 identified factors were re-categorized in the new three-phase model and are shown in Figure 3.3.

FIGURE 3.3: MAPPING OF FACTORS AGAINST THE REFINED THREE-PHASE MODEL

STRATEGY PLANNING AND ANALYSIS	CONTRACTING AND RELATIONSHIP DEVELOPMENT	IMPEMENTATION
<ul style="list-style-type: none"> • Executive consensus about the appropriateness of outsourcing this activity • Clear directional business case and rationale to justify outsourcing this activity • Systematic processes to identify candidate activities for outsourcing based on competitive analysis • Formal process to establish requirements and select the outsourcing supplier for this activity • Formalized financial and situational analysis processes to decide whether to outsource this activity • Formal governance process and project plan to guide and manage the transition to the outsourced model • Cross-functional decision-making and agreement to outsource this activity 	<ul style="list-style-type: none"> • Formal contract and service level agreement • Formal contingency/exit strategy • Systematic process to determine what information to share with each other • High degree of trust • Clear roles and responsibilities for managing the execution of the contract • Formalized and clear intellectual property rights and ownership agreement with the supplier • Pre-established and agreed-upon business and technical goals for the relationship, including performance metrics 	<ul style="list-style-type: none"> • Mechanisms to track and report performance versus goals • Formal process to take corrective action • Formal joint problem resolution process • Accurate and valid performance metrics • Clear assignment of responsibilities to the correct people, from both parties, to manage the relationship • Accurate and effective bilateral information flow to execute the requirements of the contract and service level agreement • Clear accountability for transition management • Joint education and training for affected activities and processes • Formal governance process and project plan to guide and manage the transition to the outsourced model • Formal plan to maintain motivation of outsourced or displaced staff during the transition process

The significance of the second finding is that the factors making up a phase are all highly interrelated and can and should be managed as an integrated group (i.e., to be successful, companies should not attempt to “cherry-pick” from the lists).

A company’s performance in all three phases significantly impacts its level of performance against the 19 specific goals shown earlier in Figure 2.6. The most significant impact on goal achievement was performance in the implementation phase, followed by contracting and relationship development, and then strategy planning and analysis.

Although all factors in the three phases play a role in performance against the aforementioned 19 goals, Figure 3.4 shows the factors that had the highest contribution to performance, listed in order of relative degree of influence. Companies should give these factors special attention to ensure that they are resourced and managed effectively.

FIGURE 3.4: MOST IMPORTANT FACTORS AFFECTING PERFORMANCE

STRATEGY PLANNING AND ANALYSIS
<ul style="list-style-type: none"> • Executive consensus about the appropriateness of outsourcing this activity • Clear directional business case and rationale to justify outsourcing this activity • Systematic processes to identify candidate activities for outsourcing based on competitive analysis • Formal process to establish requirements and select the outsourcing supplier for this activity
CONTRACTING AND RELATIONSHIP DEVELOPMENT
<ul style="list-style-type: none"> • Formal contract and service level agreement • Formal contingency/exit strategy • Systematic process to determine what information to share with each other • High degree of trust • Clear roles and responsibilities for managing the execution of the contract
IMPLEMENTATION
<ul style="list-style-type: none"> • Mechanisms to track and report performance versus goals • Formal process to take corrective action • Formal joint program resolution process • Accurate and valid performance metrics • Clear assignment of responsibilities to the correct people, from both parties, to manage the relationship

USING THE MODEL TO PREDICT PERFORMANCE

An important consideration for executives is whether effectiveness in the three-phase model overall and by individual phase can help answer these questions:

- Does performance in any of the three phases help predict benefits (magnitude of cost savings achieved and time to achieve savings)?

- Do certain types of outsourcing goals help predict benefits (magnitude of cost savings achieved and time to achieve savings)?

Does performance by phase help predict benefits? Our analysis, using regression analysis techniques, showed that the performance in the overall three-phase model was statistically significant (significance level of <0.0001) and positively influenced the magnitude of cost savings. Additionally, we found that there was a statistically significant and positive relationship between two of the phases — “implementation” and “contracting and relationship development” — and the magnitude of cost savings.

However, when a similar regression analysis was performed on “time to savings” for each of the phases, we found no significant predictive capability. Enhanced performance within the phases did not predict a decrease — or an increase — in the time to savings. One explanation is that the factors in each phase were not schedule or time-driven in content. There may be other variables that more specifically impact time to savings.

Do certain types of outsourcing goals help predict benefits? Respondents were asked to rate their degree of accomplishment against goals for the 19 performance areas related to outsourcing listed in Figure 2.6. To help analyze their responses to the question, we used a statistical technique called exploratory factor analysis (see Appendix C). This technique identified three underlying types of goals — cost and capacity, growth and speed, and access to skills and technology — into which the performance areas could be grouped. Figure 3.5 shows the most important goals within each group.

FIGURE 3.5: MOST IMPORTANT FACTORS FOR EACH GOAL CLUSTER

GOAL CLUSTER 1 (COST AND CAPACITY)
<ul style="list-style-type: none"> • Reduce operating cost • Turn fixed costs into variable costs • Create additional capacity • Increase flexibility and responsiveness • Focus on core business
GOAL CLUSTER 2 (GROWTH AND SPEED)
<ul style="list-style-type: none"> • Increase speed to market • Grow revenue • Improve quality • Increase flexibility and responsiveness
GOAL CLUSTER 3 (ACCESS TO SKILLS AND TECHNOLOGY)
<ul style="list-style-type: none"> • Gain access to technology not resident in our company • Gain access to needed skills • Reduce capital investment

Using respondent's performance on these three types of goals, regression analyses were performed to determine the ability to predict time to savings (question 7 in the questionnaire). The "cost and capacity"-oriented strategy was significantly associated (0.01 level) with a faster time to savings. The "growth and speed" and "access to skills and technology" goals did not significantly impact time to savings.

"Level of savings" was also analyzed versus performance on the three types of goals. "Access to skills and technology" was positive and significant (0.01 level), indicating that a strategy focused on acquiring external skills and technology and reducing capital investments is related to an increase in the relative magnitude of savings attained through outsourcing. "Cost and capacity" and "growth and speed" did not significantly impact magnitude of savings. We also applied the above analyses to size of company (revenue) and type of industry (manufacturing, process industries, and services) and found no major differences with the overall findings.

These analyses suggest two different strategies at work. Companies seeking "quick" savings focus on finding less expensive alternatives to operating today's business. Companies focused on *tomorrow's* business needs may find more significant savings over the longer term by leveraging skills, technologies, and scale offered by the marketplace to dramatically reduce the cost of their value chain, rather than attempting to develop these capabilities themselves.

IDENTIFYING GOOD OUTSOURCING STRATEGIES AND PRACTICES

For each of the phases in the three-phase model, respondents were also asked to identify their best- and worst-case outsourcing experiences and to provide a description, in their own words, of the most significant reasons for each.

The outsourced activities most frequently cited for having the best results were manufacturing and operations, information technology, and procurement and supply management. The activities associated with the worst results were information technology, engineering and design, and distribution and fulfillment. The fact that information technology appears on both of these lists indicates that the approaches used to manage the outsourcing process can have a significant impact on results.

An analysis of the verbatim comments provided by respondents reveals a total of 70 positive and 83 negative observations, which we have classified according to the three phases of our prescriptive model. (Some observations were not classified due to limited information.) Review of the strategies and practices from the summarized verbatim responses shown in Figures 3.6, 3.7, and 3.8 suggest that to successfully implement outsourcing initiatives, firms must be effective in the following areas at each stage:

Strategy and planning stage

- Clearly established and communicated business case for outsourcing, based on fact-driven logic and internal alignment across functions and/or businesses
- Ongoing senior leadership at both buyer and supplier companies
- Clear scope of work, performance expectations, governance, and project plan
- Excellent suppliers with valid measures of performance

Contracting and supplier relationships

- Correct supplier selection with alignment between buyer/supplier cultures and philosophies
- Suppliers with proven current and future performance capabilities
- Clarity in roles, responsibilities, and measurements to track current and future productivity
- Excellent communication and trust

Implementation

- Effective change management
- Effective measurement, with both the outsourcing team and supplier accountable for results
- Clear customer project/transition plan
- Appropriate people from both organizations driving continuous improvement with high levels of communication

FIGURE 3.6: VERBATIM RESPONSE – PHASE 1: STRATEGY AND PLANNING

POSITIVE IMPACT STRATEGIES AND PRACTICES	NEGATIVE IMPACT STRATEGIES AND PRACTICES
<ul style="list-style-type: none"> • Establishment of a clear business case and requirements for outsourcing • Complementary knowledge and skills between core competencies of buyer and suppliers • Senior leadership engagement and support — at both buyer and supplier • Clear performance expectations within the business and of outsourced supplier established up front • Clearly defined project plan • Governance team implemented • Excellent suppliers identified and chosen • Cross-functional and business-aligned strategy • Outsourcing strategy broadly communicated 	<ul style="list-style-type: none"> • Poor supplier selection and service level agreement • Poor planning and limited internal commitment beyond a small group of people • Poor outsourcing decision processes • Scope of work poorly defined • Inability to measure against a baseline or critical success factors • Inadequate business case • Projected cost savings not achieved, thereby continued outsourcing not justified • Poor “exit” policy • Outsourcing of “near core competency” • Hand-off of a “problem” versus an “excellent process”

FIGURE 3.7: VERBATIM RESPONSES – PHASE 2: CONTRACTING AND RELATIONSHIP DEVELOPMENT

POSITIVE IMPACT STRATEGIES AND PRACTICES	NEGATIVE IMPACT STRATEGIES AND PRACTICES
<ul style="list-style-type: none"> • Solid statement of work and supplier expectations, including results sharing • Measurement of outsourced supplier performance and continuous improvement • Correct supplier selection, with buyer and supplier philosophies and cultural alignment • Clear roles and responsibilities in contract • High degree of trust • Good lines of communication 	<ul style="list-style-type: none"> • Poor communication • Overstated supplier capabilities • Poor fit of cultures • Lack of clarity regarding work responsibilities • Lack of alignment regarding priorities and their resetting impacting external customer satisfaction • Poor metrics and supplier performance measurement • Lack of trust

FIGURE 3.8: VERBATIM RESPONSES – PHASE 3: IMPLEMENTATION

POSITIVE IMPACT STRATEGIES AND PRACTICES	NEGATIVE IMPACT STRATEGIES AND PRACTICES
<ul style="list-style-type: none"> • Effective change management plans • Both outsourcing team and supplier held accountable for results to goals • Establishment of clear-cut cost targets for measurement of success • Clear project plan in contract • Building of good relationships with suppliers and ensuring the correct people are in meetings/problem solving sessions — always driving continuous improvement • Highly managed engagement with supplier(s), including executive reviews, defined governance with specific performance metrics reviewed • High levels of communication 	<ul style="list-style-type: none"> • Lack of supplier oversight • Lack of buy-in by key people resulting in project sabotage • Unplanned-for demand and volume shifts • Poor alignment of company philosophies and communications • Lack of measurement • Lack of a “transition” process • Unexpected costs • Culture and language issues • Cycle time gets longer due to distance • Lack of risk mitigation

SUMMARY

We believe that there is strong evidence that a company's performance on the factors included in the three-phase model directly affects the results it will achieve from outsourcing. This position is supported by the statistical analyses presented in this chapter, which demonstrate significant relationships between performance factors in the three-phase model and the level of results achieved, and reinforced by the survey respondents' experience, as documented in their own words.



CHAPTER 4: A CLOSER LOOK AT PROCUREMENT

Although the primary focus of this research is on management approaches toward outsourcing across a diverse range of business activities, the scope also includes a specific review of procurement. In this chapter, we explore the current role of the procurement organization in the company's strategic outsourcing process, the evolutionary forces that corporate procurement organizations face, and the outsourcing of activities within the procurement organization itself.

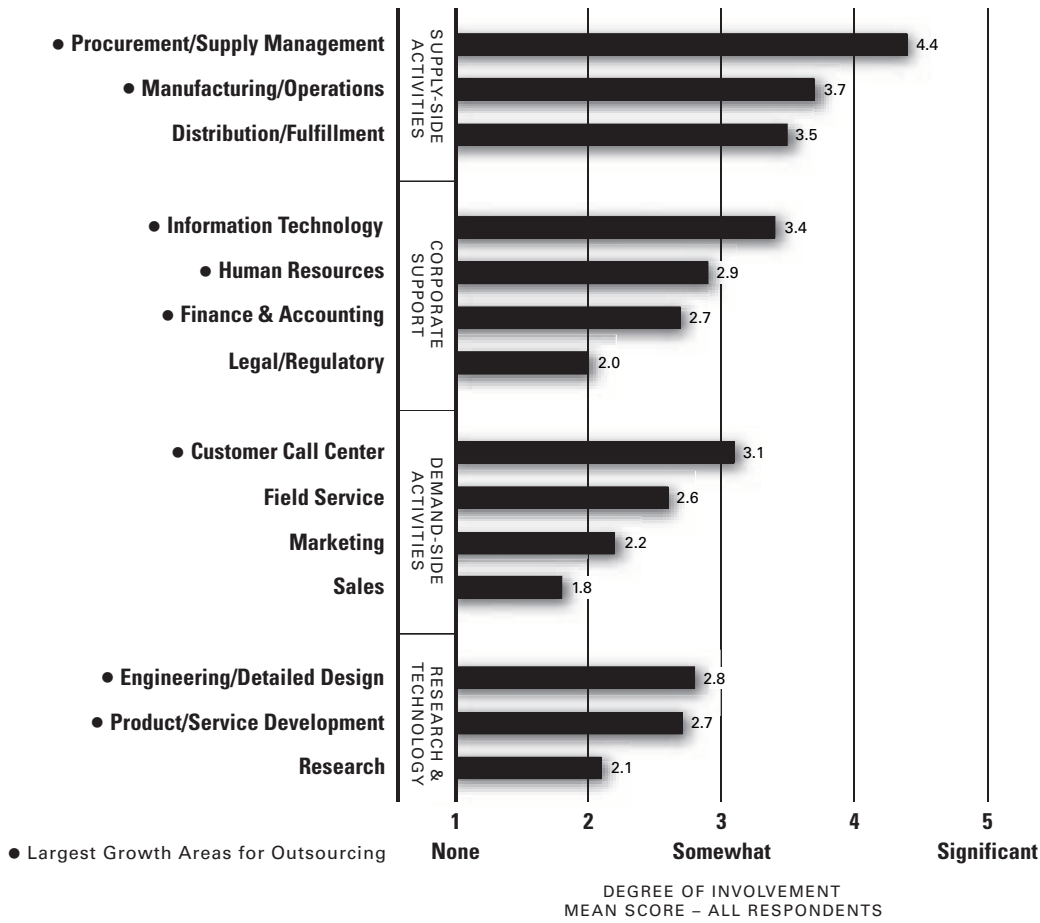
THE PROCUREMENT ORGANIZATION'S ROLE IN STRATEGIC OUTSOURCING

Our research explored the extent to which each participating company's procurement organization was involved in its strategic outsourcing process. The analysis probed:

- How deeply the procurement organization was involved in the outsourcing process for each of the 14 activities included in the survey
- How deeply the procurement organization was involved at each phase in the strategic outsourcing process
- The influence that procurement had on outsourcing success (comparing involvement level for the company's best and worst outsourcing experiences)

As shown in Figure 4.1, procurement organizations are most deeply involved in outsourcing decisions related to supply-side activities: procurement/supply management itself, manufacturing, and distribution/fulfillment. Procurement also has a moderate degree of involvement in decisions regarding the outsourcing of operations-related activities such as call centers, field service, product development, and engineering and detailed design, as well as corporate support activities such as human resources, information technology, finance, and accounting. Procurement's involvement is significantly lower in sales, marketing, research, and legal activities.

FIGURE 4.1: PROCUREMENT ORGANIZATION'S DEGREE OF INVOLVEMENT IN THE OUTSOURCING PROCESS, BY ACTIVITY

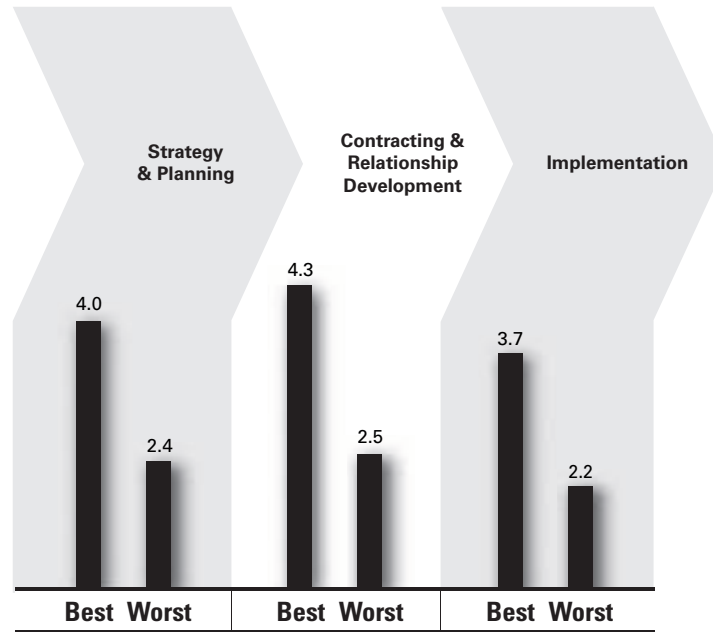


Source: Strategic Outsourcing Survey, 2004, Question 2

This pattern reflects the traditionally strong linkages between procurement and operations (especially in manufacturing-oriented companies), and leadership’s reluctance, until recent years, to include procurement in decisions surrounding external expenditures for research, legal, and marketing and sales.

Our survey respondents were asked to indicate the level of involvement by procurement in their company's best and worst outsourcing experiences. As Figure 4.2 indicates, there is a clear link between the level of procurement involvement in the outsourcing process and the degree of success achieved.

FIGURE 4.2: LEVEL OF PROCUREMENT ORGANIZATION INVOLVEMENT IN RESPONDENT'S BEST AND WORST OUTSOURCING EXPERIENCES

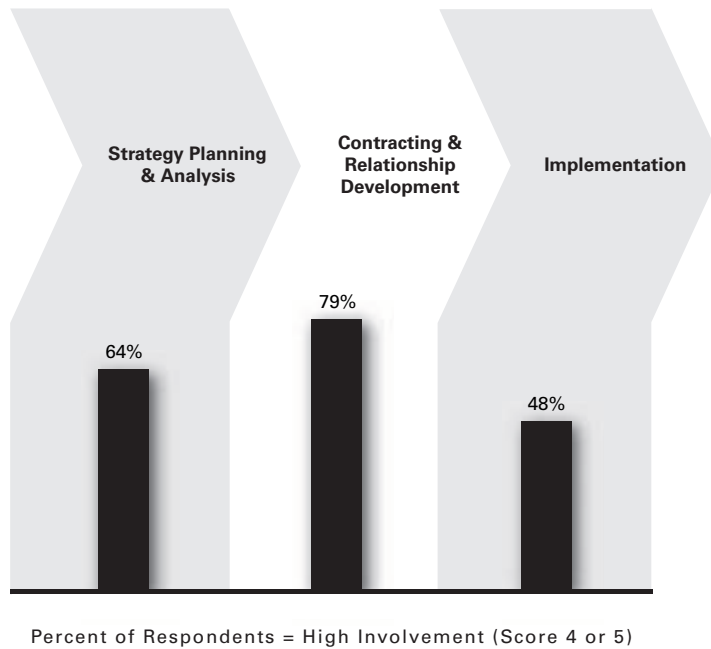


KEY: MEAN OF SCORE
 1 (No Involvement) | 5 (Significant Involvement)

Source: Strategic Outsourcing Survey, 2004, Question 12

Procurement organizations are most likely to be involved in the contracting and relationship-structuring phase of the strategic outsourcing process, as Figure 4.3 shows. Nearly 80 percent of survey respondents say that their procurement organizations have a high level of involvement in this phase, where the need for negotiating skills and experience provide a natural fit.

FIGURE 4.3: PERCENTAGE OF COMPANIES WITH HIGH PROCUREMENT ORGANIZATION INVOLVEMENT IN STRATEGIC OUTSOURCING PROCESS



Source: Strategic Outsourcing Survey, 2004, Question 9

About two-thirds of the respondents indicate that procurement has a high level of involvement in the outsourcing strategy planning and analysis phase. Reasons that companies typically include procurement at this phase include:

- Knowledge of supply market alternatives
- Insight into the dynamics of existing and potential supply markets, such as opportunities and risks, including road-mapping of supplier technology trends
- Knowledge and ability to help benchmark internal activities against external providers
- Experience in helping users define expectations of external providers, including future investment requirements

Involvement in the implementation phases — the transition as well as the ongoing relationship management and measurement — is significantly lower for procurement, with just under half of the respondents reporting high involvement by procurement in this phase.

When procurement organizations are involved in implementation, reasons include:

- Experience in transitioning activities from incumbents (in this case, the host company itself) to new suppliers (e.g., establishing and guiding the testing, ramp-up, and cut-over processes)
- Expertise in establishing supplier performance management programs (defining measures and goals, setting-up measurement and reporting systems, and creating processes to drive continuous improvement or trigger corrective action)

Where procurement has a lower level of involvement during implementation, reasons can include resistance to its involvement by other departments by the previous activity “owner” or procurement’s lack of specific expertise. However, such a situation may also reflect a legitimate need for other organizational units to take the lead in transitioning and managing the outsourced activity. For example, if a portion of an activity is outsourced (such as one manufacturing plant within a network), the executive responsible for the area (e.g., the vice president of manufacturing) may wish to retain primary control over the relationship so as to improve integration of the outsourced plant into the overall network.

However, even if procurement does *not* have the lead role in managing the relationship, the principles of effective supplier management must be embedded within the lead function. (The importance of this focus on implementation was borne out in Chapter 3, which demonstrated the link between implementation and results.)

PROCUREMENT AT A TURNING POINT?

Clearly, there is no uniform manner in which companies use their procurement organizations to support strategic outsourcing. For some, there is deep involvement across the complete strategic outsourcing process; for others, the role is more limited and focused mainly on the transaction itself. Many companies use the procurement organization in traditional, familiar areas; far fewer involve them in emerging areas for outsourcing. These patterns are indicators of a larger movement affecting procurement.

Many procurement organizations are approaching a turning point, similar to the situation faced by information technology departments several decades ago, in which some key questions will come to be addressed. What procurement-related activities are truly strategic to the business and should be kept in-house, strengthened, and built-upon? Conversely, what activities add little strategic value and are better accomplished by outsourcing specialist companies that are able to leverage their skills, expertise, and scale in ways that a single enterprise cannot?

Although outsourcing of procurement is not yet widespread, this and other research projects indicate that it is growing (as described later in this chapter). While most companies may ultimately choose to outsource some portion of their procurement activities, the procurement organization’s leadership should have a strong say in these and many other outsourcing decisions. How might this evolve? The experience over the last 40 years in IT outsourcing provides some lessons learned.

In the 1970s and early 1980s, the broad availability of computing power seemed to hold great promise even as it created enormous competitive risks. At the time, IT was viewed as a significant competitive weapon, but time has proven that this was not the case for all companies.

The popular view of IT diverged rapidly circa 1985, with three different paths or models evolving for this function:

- develop into a strategic weapon;
- become an internal utility; or
- transition to an outsourced service.

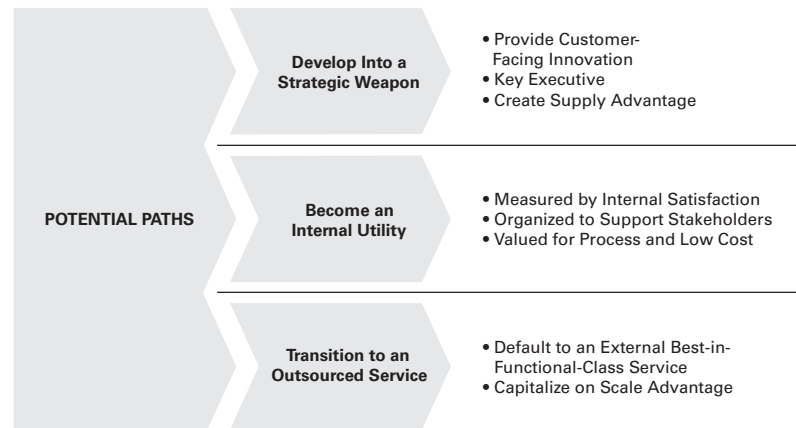
A combination of factors led different companies to pursue one of these paths, but the IT executives generally had a strong influence on their enterprises' decision-making processes based on their ability to demonstrate value and articulate a strategic role for the future. Similarly, today's chief procurement officers will play a major role in determining the fate of their organizations.

For information technology, the trigger for change was the personal computer, as small-scale computing came to strip away much of the traditional mystique from data processing. For procurement, this trigger has yet to be identified. The escalating availability and power of Internet tools, rising volume of information about supply needs and options, and increasingly transparent market economics all may well be the trigger. Alternatively, the trigger could come about as a result of companies reaching a "tipping point" in their value chain structure. As a greater percentage of the value chain is outsourced, companies will be forced to rethink how they need to manage their portfolio of external supplier relationships going forward.

Consider that until recently, the supply market was a realm that could only be accessed by diligent practitioners working in offices stacked floor to ceiling with supplier catalogs. Now, the supply marketplace has an online, global electronic billboard, making supply markets visible to *everyone*, not just the purchasing agent. Companies can now employ auction tools and end-user ordering systems to help ensure that virtually all of the goods and services they rely on are sourced effectively, managed well, and purchased efficiently.

What will the procurement organization look like in this new world? A model similar to IT will likely apply over the coming years, as shown in Figure 4.4. The procurement organization could take on a "strategic weapon" role, combing the supply market for sources of customer-facing innovation and revenue generation, thereby creating strategic cost advantage. Providing both strategic insight and technical capabilities to support the corporation's overall outsourcing decisions will be key terms in this equation.

FIGURE 4.4: POTENTIAL EVOLUTIONARY PATHS FOR PROCUREMENT ORGANIZATIONS



For activities without a strategic impact (transaction processing or managing categories that have little influence on overall cost or customer satisfaction), the company could leverage a utility or shared-services approach that manages for optimal efficiency and cost. In such a situation the company still keeps the activities in-house and relies on internal scale and scope to drive internal procurement effectiveness versus what might be available from procurement outsourcing providers.

Finally, for areas where the procurement organization adds no strategic value or where the company lacks internal scale to operate at high levels of procurement effectiveness, transitioning to an outsourced procurement service is the logical outcome.

OUTSOURCING PROCUREMENT ITSELF

The survey asked respondents to provide additional detail on the level of outsourcing for procurement and supply management across six main categories of expenditures: direct materials, MRO (maintenance, repair, and operating supplies), indirect purchases, capital expenditures, services, and goods for resale.

For each, respondents were asked to indicate their company's current levels of procurement outsourcing, and the expected levels within 18 months for three types of activities:

- Strategic procurement (supplier selection and category and commodity strategy)
- Supplier management (supplier assessment and evaluation, supplier development, and supplier certification)
- Transaction processing (ordering, replenishment, payment and settlement, coding and catalog management, and procurement information systems management)

Procurement outsourcing is not yet widespread, as Figures 4.5 and 4.6 illustrate. Consider that MRO transaction processing is currently the most prevalent area for procurement outsourcing, yet only 20 percent of companies are outsourcing this activity today — a figure that is projected to rise to only 33 percent 18 months out.

The fraction of companies outsourcing procurement activities drops off significantly for categories tied more closely to the core of the business (e.g., revenue linkages for direct materials and goods for resale, and business infrastructure for capital expenditures) and for strategic procurement and supplier management.

It is important to note, however, that a subtle form of procurement outsourcing for direct materials can take place when a company turns over manufacturing responsibility for systems and modules to a first-tier supplier. Often, the very procurement of raw materials and component parts is outsourced to that first-tier supplier, separating the company from knowledge and influence over buying decisions for these items. Some companies retain a level of control, however, by stipulating that first-tier suppliers buy from designated suppliers.

FIGURE 4.5: CURRENT USE OF PROCUREMENT OUTSOURCING

TYPE OF PURCHASE	PERCENT OF RESPONDENTS CURRENTLY OUTSOURCING PROCUREMENT ACTIVITIES		
	STRATEGY	SUPPLIER MANAGEMENT	TRANSACTION PROCESSING
Direct Materials	4%	7%	9%
MRO	9%	13%	20%
Indirects	11%	12%	17%
CapEx	4%	7%	9%
Services	15%	13%	19%
Goods for Resale ¹	5%	8%	11%

¹Forty-five percent of the respondents purchase goods for resale

Source: Strategic Outsourcing Survey, 2004, Question 13-19

FIGURE 4.6: PLANNED USE OF PROCUREMENT OUTSOURCING

TYPE OF PURCHASE	PERCENT OF RESPONDENTS PLANNING TO OUTSOURCE PROCUREMENT ACTIVITIES		
	STRATEGY	SUPPLIER MANAGEMENT	TRANSACTION PROCESSING
Direct Materials	5%	8%	15%
MRO	13%	17%	33%
Indirects	15%	14%	28%
CapEx	4%	8%	13%
Services	16%	16%	25%
Goods for Resale ¹	7%	11%	18%

¹Forty-five percent of the respondents purchase goods for resale

Source: Strategic Outsourcing Survey, 2004, Question 13-19

Companies that have outsourced procurement activities have done so for a variety of reasons, including the need or desire to:

- Focus the procurement organization on important categories and higher value-added activities
- Reduce costs of transaction processing
- Tap into external category expertise and use the market leverage of the outsourcing provider
- Reduce cycle time and improve efficiency of sourcing efforts
- Gain access to information technology tools without major investment
- Establish and develop minority suppliers

Reasons that companies have chosen *not* to outsource procurement include:

- The belief that procurement is already performing at the same levels as or better than supply market alternatives
- The fear that procurement is being under-managed internally, and that giving the “mess” to someone else can only compound the problem
- The belief that procurement/supply management is a core competency
- The fear of the risks involved in losing expertise/knowledge about second—and third-tier supply markets
- The lack of capable outsourcing providers
- The unwillingness to give up control of (or gains from) future productivity initiatives in procurement

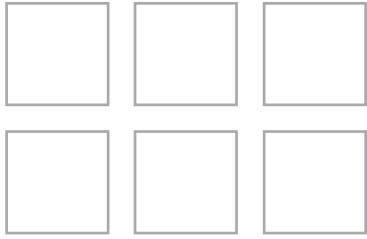
EVALUATING THE PROCUREMENT OUTSOURCING OPTION

There is no single right answer to the question of whether to outsource procurement, in part because there are so many different questions around this subject and each company is so unique. What competencies are core? Which are non-core? Should the company retain functions such as sourcing, supplier relationship management, and transaction processing? Or should it outsource them? If it is determined that outsourcing is the answer, a new question is posed: should the business be outsourced to a category-specific service provider, or a broad-based service provider that might be able to provide scale or other advantages?

Executive management in each company needs to assess the procurement organization and its activities against the broader company’s own needs and situation. Key questions to be asked include:

- What is the current value contribution of procurement to the firm? What additional impact could it have if world-class practices were used? How does this differ by category of purchase?
- What is it costing to deliver that value? What could it cost if efficiency improved? What would it cost to attain world-class levels?
- In what areas could other companies provide procurement services at a lower cost while increasing the value contribution over time?
- What are the risks of outsourcing procurement, and how can they be mitigated?
- Will the company lose competitive advantage and a core competency if procurement is outsourced?

Appendix A provides executives with perspectives on the procurement options available and some of the approaches that can be used to evaluate them.



CHAPTER 5: THINKING STRATEGICALLY ABOUT OUTSOURCING

As our research shows, outsourcing is a widespread practice in business today, and it will continue to grow. The reasons for and approaches toward outsourcing by individual companies vary greatly. Some are doing so because of tactical considerations, such as outsourcing specific functions (e.g., accounts payable) to reduce cost. Others have made strategic decisions, including the outsourcing of whole activities to fuel growth without adding capital, as Procter & Gamble did in outsourcing manufacturing for some product lines to suppliers that already had the product and process capabilities to improve the product over time. Even more ambitious is the outsourcing of whole parts of the value chain to generate capital and create new options, as General Motors and Ford did by spinning off Delphi and Visteon, respectively.

While tactical outsourcing will continue to generate benefits, we believe that the future will belong to companies that think and act strategically in the outsourcing arena. Tactical outsourcing is a follow-the-leader approach, not a road to competitive advantage. Strategic outsourcing can create new ways to compete, and possibly rewrite the rules for whole industries.

This chapter offers our perspectives on the context, issues, and approaches that companies can employ in pursuing strategic outsourcing. We explore four topics to consider when thinking strategically about outsourcing:

- Understanding how tomorrow's environment may be different
- Imagining the opportunities and possibilities for strategic outsourcing
- Exploring the range of strategic outsourcing options to gain advantage for your corporation
- Addressing the executional issues

UNDERSTANDING THE FUTURE BUSINESS ENVIRONMENT

Given the changes to business, technology, and world affairs since the early 1990s, business strategies developed then seem almost naïve in today's world. Similarly, a decade from now, today's strategies could seem equally naïve, unless companies anticipate and plan for potential upsets to the tenuous economic, social, and political conditions of today.

Before thinking strategically about outsourcing, executives should consider how changes to the business environment can significantly impact companies and the industries they compete in, and how those changes could alter future strategic outsourcing options, risks, and management approaches. In one view of the future, Paul A. Laudicina¹ has identified five critical drivers of change that are creating challenges for leaders.

1. Globalization
2. Demographics
3. The new consumer
4. Natural resources and the environment
5. Regulation and activism

For each, Laudicina identifies underlying trends and proposes scenarios on how each driver might play out. He then combines scenarios into different views of the world 10 years out. While it is not the intent of this report to dive deeply into each driver and scenario, we offer here some highlights and interpretations of what they could mean for decisions about strategic outsourcing.

Globalization

Global economic integration is making it easier to raise and allocate capital across borders. Suppliers in emerging markets are building technologies and capabilities rapidly, providing a richer rationale for outsourcing than just pursuing low cost. Advances in information technology and logistics services make offshoring and global sourcing more accessible and practical. This is creating a fertile environment for even greater outsourcing, especially outside the home country. Gaining entry and access to fast-growing markets may require a greater degree of offshore outsourcing in order to enable companies to achieve scale quickly and meet local governmental requirements.

At the same time, globalization introduces new risks. Outsourcing to low-wage countries exposes companies to political and social backlash from governments, workers, and consumers at home. Distant locations with less well-developed infrastructures and supply chains stretched around the globe add to business continuity risks from natural disasters, disease (e.g., SARS), or manmade acts of disruption (e.g., terrorist acts in both the physical and “cyber” worlds). Companies need to think about and plan for such contingencies as they develop strategies for outsourcing.

Demographics

Both the workforce and the consuming public in the developed world are aging, bringing about a shrinking labor pool and the attendant loss of experience, a shift in buying habits, and new funding requirements for retirement and healthcare. At the same time, the developing economies are seeing a population boom that is creating millions of ambitious young people. It is uncertain whether the developed countries will promote immigration of workers or allow increased export of jobs as a remedy to their situation. Likewise, as standards of living increase in developing countries, it is difficult to predict whether workers will have better opportunities by migrating, or by helping to build their own economies.

¹*World Out of Balance: Navigating Global Risks to Seize Competitive Advantage*, McGraw-Hill, 2004

One thing that appears certain, however, is that as these economies strengthen and grow, today's relative cost advantages versus developed countries will shrink, and the capital-to-labor ratios and quality of the supporting infrastructure in these countries will rise. One implication is that companies making offshore outsourcing decisions need to look beyond short-term cost benefits and take a longer-term strategic view of the economics and build in flexibility. On the domestic front, perhaps they should also consider a different kind of outsourcing for certain activities, where retired employees, working on a reduced schedule, "supply" their skills and experience to their former employers.

The New Consumer

In many developed countries, consumer markets are flooded with choice and saturated by consumption. To attract new consumer purchases, companies need innovative products and services that cut through the clutter and *create* demand rather than merely satisfying it. At the same time, a growing consumer class in emerging economies is generating a different kind of demand for products and services, tuned to local needs and customs. Together, these trends are creating millions — *billions* in some cases — of micro-markets that require a steady stream of new and exciting products and services, and require creative ways to deliver them.

From an outsourcing strategy standpoint, this means that companies need to look beyond today's offerings and channels and focus also on the capabilities they and their strategic outsourcing partners will need to serve these diverse markets. Companies should explore nontraditional sources of ideas and capabilities for product design, selling, marketing, manufacturing, and distribution.

Natural Resources and the Environment

Projections of shortages in oil, clean water, and quality air are offshoots of those studies that predict increased global economic development. Although many of the dire scenarios are projected to take place decades from now, spot shortages are showing up already in prices — witness the late-2004 rise in oil prices, to US\$55 per barrel.

Companies should consider how shortages could impact location decisions and logistical considerations related to outsourcing, and especially offshoring. What would the implications be on those decisions if shortages affect business economics and sustainability? What precautions should firms consider to dampen the effects of losing direct control over the availability and use of scarce resources?

Regulation and Activism

Since the start of the decade, both the governmental and public mood has shifted from liberalization and deregulation of businesses, toward much greater oversight and scrutiny. Corporate scandals, deregulation efforts with dubious success, and heightened security concerns sparked this increased attention, and the emergence of activist groups has added to it. The Sarbanes-Oxley Corporate Reform Act in the United States is just one example of tougher scrutiny on the decisions corporations make — and, by extension, on the decisions their outsourcing partners make. Additional risks from the secondhand effects of an outsourcing supplier violating corporate standards for the environment, releasing private customer data, or using child labor also expose corporations to criticism, embarrassment, or liability.

At a minimum, companies should assess how outsourcing increases their exposure, and plan accordingly. This may include raising the bar for making the outsourcing decision in the first place (i.e., are the risks from loss of control worth the potential gains?), and building in additional safeguards to the selection and management of the outsourcing partner.

As events of the past decade have shown, straight-line projections of today's trends create a poor basis for strategic decision-making. Before developing and determining strategic outsourcing options, companies should consider the implications of fundamental business, social, and environmental drivers such as those discussed above.

IMAGINING THE OPPORTUNITIES

Thinking strategically about outsourcing means stretching the imagination beyond today's reality. Applied strategically, outsourcing has the potential to restructure whole value chains. In a book entitled *Rebuilding the Corporate Genome*², authors Johan Aurik, Gillis Jonk, and Bob Willen provide a vision of tomorrow's ultra-competitive corporation, built around the "capability-driven" organization. In this vision, companies will focus only on those capabilities crucial to their strategy and mission as an enterprise, and outsource or spin off other capabilities.

At the same time, companies will pursue new relationships with existing and potential partners along the value chain. The aim will be to recombine capabilities across companies to increase the joint competitiveness of all parties. The intent? To transcend the traditional practice of maximizing the returns from a single capability — "taking a larger slice of the pie" — and to instead make the pie itself bigger, thereby increasing the size of each individual slice.

What could this mean for industry structures? Far less vertical integration within traditional players, shifts in responsibilities and requirements of suppliers (exemplified by tiered physical value chains and networked knowledge and transaction value chains), brand-new competitors and channels, and a growth in specialized niche providers are among the possibilities. Future work will be positioned at the place in the value chain where scale, intellectual property, and capabilities are best leveraged.

Consider some examples already in place:

- In several instances across a range of industries, bundling of products and services has allowed companies to shift full responsibility for availability and performance to suppliers. An early version of this is systems suppliers in the automotive industry that provide pre-assembled systems and modules, bundling products (their own components and those of others) with the assembly service. General Electric offers "power by the hour" contracts to its commercial airline customers, where GE sells an hour of engine use, and handles maintenance and repair.
- The U.S. Navy is implementing a "performance-based logistics" concept with several of its suppliers. Here, suppliers take over full provisioning and support responsibilities, providing the Navy with guaranteed availability and reliability of items ranging from tires to sophisticated weapons systems. In addition to order processing and materials distribution, the suppliers handle engineering and technical services, repair-overhaul-replace decisions, and obsolescence management.

²*Rebuilding the Corporate Genome: Unlocking the Real Value of Your Business*, John Wiley and Sons, Inc, 2003

- Limited income and distribution constraints in emerging-market countries can require nontraditional solutions. In India, Hindustan Lever Limited (a subsidiary of Unilever PLC) has set up manufacturing and distribution for single-serve packs of personal care products priced at the equivalent of a single American penny. Also in India, Arvind Mills sells ready-to-sew kits of blue jeans components distributed through a network of thousands of local tailors. Significantly lower costs and widespread distribution has made Arvind a market leader.
- Virtual companies, providing goods and services to transient, fast-changing markets, may emerge. This follows the model of the entertainment industry, in which movies, compact discs, and other media are created by quickly bringing together various performers and experts and then swiftly disbanding them.
- FedEx and UPS are providing outsourcing supply chain solutions to companies such as Cisco, Hewlett-Packard, Philips, and Nikon. These and many other companies have outsourced order processing, transportation, distribution management, information systems, repacking, kitting for specific customers, and final assembly.
- Contract manufacturers in the electronics industry are taking on more design work for OEMs, enabling the OEMs to focus on their absolute core competencies instead of peripheral areas.

Looking ahead, even greater restructuring is possible. For example, a consumer packaged goods company might turn over much of its manufacturing and distribution to a company with the scale and expertise to set up and operate a world-class physical value chain. This would free up the company to focus on product innovation and development, branding/consumer market development, and new consumer services — perhaps in combination with other companies offering complementary products.

Another example might be the ongoing restructuring of the automobile industry. Already, OEMs have outsourced responsibility for both the design and assembly of certain models to first-tier suppliers. Increased automobile reliability (resulting in reduced maintenance and thus reduced revenue for dealers), increased sophistication, and the increased use of electronics in automobiles are changing other assumptions about the industry's structure. Add to this the potential for fundamental design changes in the not-too-distant future, as with GM's Autonomy fuel-cell concept car that would feature a "skateboard" chassis independent from the body that will allow a single vehicle to use separate bodies for different purposes, from a utilitarian station wagon during the workweek to a sporty sedan for a weekend getaway.

With design and assembly skills available from systems integrators, and some potentially game-changing economic and technological dynamics, it is not too hard to imagine a marquee brand name like Sony, Virgin, or Wal-Mart creating a radically different value chain for the industry.

EXPLORING STRATEGIC OUTSOURCING OPTIONS

After understanding the future business environment and the strategic opportunities for outsourcing, a company is better able to explore the strategic options that are right for its unique situation. These options depend on several factors, including:

- The company’s maturity and experience in outsourcing
- Strategic intent for outsourcing
- Maturity of the outsourcing market
- Commitment to the current business model
- Readiness and capacity for change

Maturity and Experience in Outsourcing

Inspired by the seemingly endless possibilities and opportunities it offers, many companies may take aim to transform their business (and their industry with it) via outsourcing. However, not all companies are ready for transformational outsourcing. It requires sufficiently mature strategies and processes for outsourcing to achieve such goals. Figures 5.1 and 5.2 illustrate a four-stage model of how companies mature in these two areas. Each stage builds a base of experience and competency that allows a company to evolve to the next stage.

FIGURE 5.1: A.T. KEARNEY STAGES OF EXCELLENCESM – OUTSOURCING STRATEGY AND GOALS

ELEMENT	STAGE			
	I	II	III	IV
STRATEGIC OBJECTIVE FOR OUTSOURCING	<ul style="list-style-type: none"> • Change the cost structure 	<ul style="list-style-type: none"> • Rationalize the asset base 	<ul style="list-style-type: none"> • Enhance capabilities 	<ul style="list-style-type: none"> • Reposition the business
STRATEGIC OUTSOURCING ROADMAP	<ul style="list-style-type: none"> • No apparent outsourcing strategy or roadmap 	<ul style="list-style-type: none"> • Outsourcing strategy based on financial considerations 	<ul style="list-style-type: none"> • Outsourcing strategy combines financial objectives and forward-looking assessments of needed capabilities 	<ul style="list-style-type: none"> • Outsourcing strategy is fully integrated into the business strategy
EXAMPLE GOALS FOR OUTSOURCING	<ul style="list-style-type: none"> • Seek lower cost alternatives to performing current activities internally • Meet downsizing requirements 	<ul style="list-style-type: none"> • Increase capacity without investment • Turn fixed costs into variable costs • Provide back-up capabilities 	<ul style="list-style-type: none"> • Gain access to needed capabilities not currently available in the company • Focus resources on the core business • Gain access to markets 	<ul style="list-style-type: none"> • Reshape the company and its role in the value chain • Outsource non-core activities to focus on core processes • Align with best-in-class partners along the value chain • Seek opportunities to insource to leverage strengths

FIGURE 5.2: A.T. KEARNEY STAGES OF EXCELLENCESM – OUTSOURCING APPROACHES

PHASE	STAGE			
	I	II	III	IV
STRATEGY AND PLANNING	<ul style="list-style-type: none"> Reactive, opportunistic approach toward identifying and deciding to act on opportunities 	<ul style="list-style-type: none"> Informal process to evaluate whether an individual activity should be considered for outsourcing 	<ul style="list-style-type: none"> Formal process applied periodically to identify and evaluate candidate activities across the company for outsourcing opportunities 	<ul style="list-style-type: none"> Ongoing systematic process to identify and evaluate candidate activities, business units, functions across the company for outsourcing opportunities
CONTRACTING AND RELATIONSHIP DEVELOPMENT	<ul style="list-style-type: none"> For each situation, ad-hoc approach is used for defining requirements, negotiating and selecting suppliers and shaping relationships 	<ul style="list-style-type: none"> Informal and inconsistently applied process exists for defining requirements, negotiating and selecting suppliers and shaping relationships 	<ul style="list-style-type: none"> Formal, consistently applied process used to define requirements, negotiate and select suppliers and shape relationships 	<ul style="list-style-type: none"> Formal process extends to include early identification of relationship growth opportunities and paths/milestones to realize them
IMPLEMENTATION	<ul style="list-style-type: none"> Ad-hoc approach is used for transition planning; "Arms-length" management of the relationship driven by adherence to contract terms 	<ul style="list-style-type: none"> Informal and inconsistently applied process exists for transition planning and relationship management 	<ul style="list-style-type: none"> Formal, repeatable process used to govern the transition and manage the ongoing relationship for mutual benefit 	<ul style="list-style-type: none"> Proactive process used to identify untapped opportunities and develop new relationships with current and potential outsourcing partners

In Stage I, companies approach outsourcing primarily from a cost reduction perspective. Initially, their approaches to identifying opportunities are bottom-up and ad-hoc; they have no processes in place for selecting and negotiating with suppliers or managing the transition or the relationships. A common mistake for a Stage I company is to view outsourcing as a way to get rid of a known "problem" with the expectation that the outsourcing provider can somehow fix it. (Outsourcing failures are very likely to occur in such situations.) As Stage I companies gain experience, they begin to accumulate "lessons learned" (often the hard way), providing a platform for moving to Stage II.

Companies develop into Stage II as the focus shifts away from using outsourcing to get rid of problems or to simply get today's business done for less. Instead, the company uses outsourcing as an extension of the company, to quickly add capacity with little or no investment and to provide backup capabilities. The company begins to put processes in place to plan for and manage outsourcing, but these tend to be informal and inconsistently applied.

As companies evolve into Stage III, they start to look at outsourcing as a way to extend beyond today's business. This includes using outsourcing suppliers to access skills and technologies and to add new capabilities to the value chain instead of developing them in-house. Formal, repeatable processes help the company proactively identify outsourcing opportunities and structure and manage the outsourcing relationships.

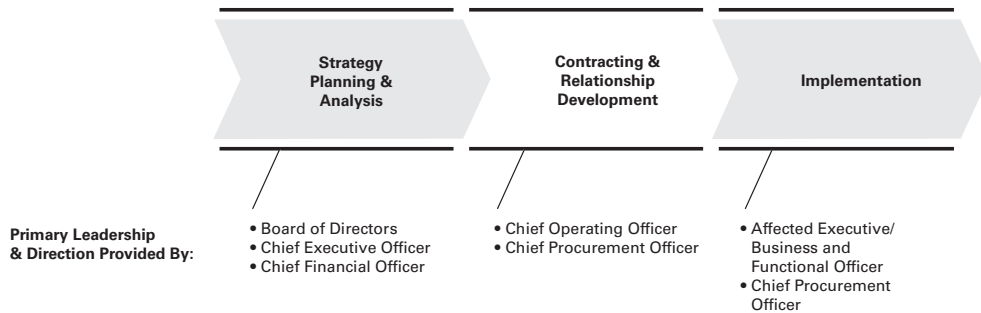
Few if any companies are completely in Stage IV at the current time. A company in this stage would use outsourcing as a way to fundamentally transform its operation. On an ongoing basis, it would identify and evaluate outsourcing candidates across its activities, functions, and value chain steps. At the same time, it would look for opportunities to insource activities from other firms, leveraging its own strengths. Both during the selection of its outsourcing providers and during the operational relationship, a Stage IV company would look for opportunities to grow the relationship and pursue actions to achieve them.

This four-stage model can be used as a self-assessment guide for companies to determine their readiness to take on more sophisticated outsourcing strategies and manage more complex outsourcing relationships. Building a Stage III strategy on a Stage I platform, for example, exponentially increases the risk of failure.

Strategic Intent for Outsourcing

Bearing in mind the company’s readiness, the next part of exploring strategic outsourcing options is to identify the strategic intent of outsourcing. This takes place during the first phase in the three-phase model, and is primarily the responsibility of senior leadership charged with shaping and approving the business strategy, specifically the board of directors and the CEO (see Figure 5.3).

FIGURE 5.3: PRIMARY RESPONSIBILITY FOR LEADERSHIP OF STRATEGIC OUTSOURCING BY PHASE



Strategically, companies like Ford, GM, and Procter & Gamble have outsourced whole lines of business. Others, such as Honeywell, Cisco, and Hewlett-Packard, have outsourced key elements of their supply chains, like order processing and delivery, re-engineering of distribution, and new channel creation. Business processes (call centers, accounting, transaction processing) and design and manufacturing of parts and systems have all been outsourced by a number of companies.

In addition, companies are outsourcing processes that had once been considered to be core competencies, such as design and engineering work in the automotive, aerospace, and electronics industries, and research in the consumer goods industry. The definitions of core competencies and what is truly strategic to the business are shrinking.

Given the above examples, there is a range of strategic outcomes that a company could consider, including:

- **Maintain cost competitiveness.** Ensure that the competitive positioning of the company meets or beats that of the competition, especially regarding cost structure. Companies can take the lead or quickly follow others in non-core competency areas to outsource goods and services to low-cost areas of the world. In addition, through strategic outsourcing, companies may be able to establish business opportunities by outsourcing areas that are considered to be important but lacking in significant investment.
- **Gain revenue via innovation.** Outsourcing and partnering may provide the basis for technology and process innovation that results in revenue enhancement. For example, automotive companies may outsource seat design and manufacturing, or high-tech electronics companies may outsource design and manufacturing work (the latter is already often done under the guise of contract manufacturing).
- **Re-examine legacy core competencies.** Take the lead in an industry space and strategically outsource goods, services, and processes that may have been considered a core competency historically but for which competitors and suppliers have established comparable or leading capabilities due to investment, innovation, and scale. By being a “first mover,” the company may be able to gain significant competitive advantage.
- **Outsource, but maintain control.** Effectively deploy a strategic outsourcing strategy and planning process so as not to outsource goods, services, or processes that provide and/or maintain a competitive advantage. For example, Nokia has retained some aspects of manufacturing for purposes of increased responsiveness, even as its competitors have outsourced. Hewlett-Packard and IBM are among the companies that have outsourced the manufacturing of certain products while maintaining control of second-tier supplier parts to the first-tier outsourced supplier.
- **Restructure the overall value chain.** Establish a strategic outsourcing paradigm that includes key firms in the supply/value chain to truly establish “where” in the chain or web work should be done to create the best overall value add and “lean out” the supply/value chain. For example, GlaxoSmithKline provides its outsourced suppliers with early-stage research results and has them factor in these results and their inherent expertise in order to increase the flow of new products to market. This modification of the pharmaceutical business model can lead to both increased effectiveness and efficiency.³

Strategically, a company may also capture additional business by becoming a preferred outsourcing supplier based on core competencies, for example, by providing the best product engineering capability in the software industry or design engineering in aerospace.

³Foley, S. “GSK Plans Dramatic Extension of Drugs Research Outsourcing.” www.independent.co.uk, November 1, 2004

Maturity of the Outsourcing Market

A company's outsourcing strategy should also reflect the maturity of the outsourcing supply market. Early adopters of outsourcing for a particular activity face hurdles including a limited choice of suppliers, the potential need to create a supply market through co-investment, suppliers whose capabilities are unproven, user backlash at poor service, and unfamiliarity on both the customer's and supplier's parts about how to specify, set up, and manage outsourcing relationships for the specific area addressed.

On the other hand, early adopters can help shape the supply market to their advantage (e.g., drive suppliers to set up offerings or locations advantageous to the company) and can potentially benefit from lower costs as suppliers, hungry to establish an anchor customer (for both credibility and scale), "buy" their way into the market.

Companies that take a "wait and see" attitude to immature markets reduce their operating risks, but may lose strategic advantage both by trailing more aggressive competitors in achieving outsourcing benefits and by letting those competitors define the market.

Company Commitment to Current Business Model

The fourth element in exploring strategic options is to examine constraints to outsourcing imposed by the degree of real and implied commitment to its current business model. For example, companies with an existing value chain, geographic footprint, and asset base face several potential hurdles, including transition costs and related business disruption risks, labor constraints on or backlash from loss of jobs, asset write-downs or write-offs, and possible liabilities for previously granted tax incentives. This makes it all the more critical for these companies to understand the true strategic costs and benefits of their decisions upfront.

At the other extreme, consider a "greenfield" startup company, or a new entrant into an existing geographic market. It would face no burden of job loss or underutilized assets by outsourcing activities to others. And, like an early-adopter company, it can shape the market to its needs, as Dell did. Or, if it enters markets where a network of existing outsourcing suppliers exists, it can use this to gain (virtual) scale rapidly, while preserving capital and keeping the focus of management's attention on the business at hand.

Readiness and Capacity for Change

As with any fundamental change in a business, the pursuit of strategic outsourcing opportunities will require the full commitment of executive management and an organizational commitment to make radical changes happen. This is even more critical when a company is attempting a move from one stage of outsourcing maturity to the next.

The commitment to the timing and intensity of major change is tied to the perceived opportunity or need for change, often resulting from a so-called "trigger point" event that creates the conditions (a window of opportunity) when major change can happen and succeed. Experience has shown that a company's ability to recognize and capitalize on trigger points is a key to successfully moving to the next stage.

Trigger points that can drive a company to make strategic outsourcing decisions include:

- Strategic redirection for the company and the resulting need to downsize or shed non-core businesses, capabilities, or activities
- The need for new capabilities to support new products or meet new requirements that are beyond the company's ability to respond with internal resources
- Cost pressures and the need to find radically lower-cost alternatives, either due to an earnings shock or the emergence of a new, significantly lower-cost competitor
- The arrival of a new CEO with experience in using outsourcing strategically in the former company

The company's executive team should include in its plans for strategic outsourcing how it will recognize — and possibly create — trigger points for change, and how it will optimize accordingly. Although establishing trigger points are no guarantee of success, they are often a prerequisite to achieving the radical changes to the company and its role in the value chain that underlie strategic outsourcing.

ADDRESSING THE EXECUTION ISSUES

Regardless of the strategic intent of outsourcing, companies must fully understand the execution issues that must be addressed for success.

Referring back to Figure 5.3, the focus shifts to execution. Phase 2 (contracting and relationship management) and Phase 3 (implementation) are where other executives take on leadership roles, and their specific functional perspectives must also be considered.

From the perspective of the chief financial officer (CFO), one goal is to structure the relationship to ensure that financial opportunities are realized — for example, using another company's plant and equipment reduces capital on the books. Applying research and development resources from suppliers that may have better capabilities and scale can both reduce costs and enhance revenue by bringing improved products and services to market first.

In addition, the CFO should be concerned about ensuring appropriate risk mitigation strategies for outsourcing, especially as suppliers become more dispersed worldwide and are increasingly located in most cost competitive and emerging countries.

The chief purchasing officer (CPO) is also concerned with risk mitigation strategies as the firm establishes the best worldwide supply base and as new and distant suppliers are found and given outsourced business. The CPO must ensure that suppliers transplanted to low-cost countries and local suppliers in those countries meet the design, engineering, manufacturing, and distribution requirements of the buying company. Intellectual property must be maintained, and sufficient availability and quality provided.

Any number of other "C-level" executives, such as those in research and development, engineering, manufacturing, and logistics will be affected by the company's outsourcing strategies and need to participate in their creation. The results and resource reductions or increases can be significant. For example, outsourcing new product development processes, combined with internal work, can shorten product development time (24 hours a day, seven days a week worldwide) while increasing the risk of losing technological capabilities. Losing control over the cost and quality of second-tier supplier parts' volume to an outsourced supplier, while still doing business with the second-tier suppliers (which are first-tier in other areas), gives up leveraging opportunities.

In addition, headcount reduction may be required in various functions due to outsourcing. The autonomy of business units may be impacted by company-wide outsourcing strategies. Given the various and numerous functions and areas of a firm that can be impacted in many ways, it is incumbent on firms to develop the best processes and involve the most appropriate people for strategy and planning, establishing and managing the outsourced supply base, and implementing the outsourcing decisions.

Without the best processes, great thinking, company-wide alignment, and supported implementation, the many barriers to success can limit outsourcing effectiveness and results.

These barriers include, but are not limited to:

- Negative reaction to job loss at a company in the local, regional, and country areas
- Political responses limiting a company's competitiveness
- Internal sabotage of outsourcing because of loss of status, prestige, headcount, and position
- Lack of measurable results
- Perceived loss of core competency and increased risk

Recognizing that these and other barriers exist requires that firms establish the best processes and people at a strategic level to develop and implement outsourcing plans. Company leaders must be fully engaged and aligned, as inadequate understanding of the outsourcing challenge and inadequate strategies and processes will lead to less-than-desirable results.

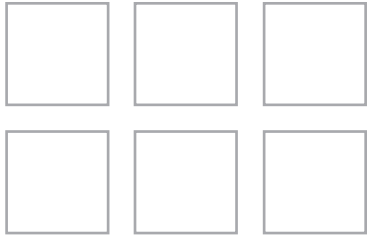
SUMMARY

The research covered in this report demonstrates clear opportunities for outsourcing a range of activities in the company, but the biggest opportunities yet ahead are from thinking and acting strategically about outsourcing. To evaluate your company's position, we suggest considering your company's approach to outsourcing against the following practices.

Does your company take the following actions:

- Ensure that the board of directors regularly reviews strategic outsourcing options and decisions?
- Force itself to challenge and potentially significantly reduce its "core competency" space?
- Create business model scenarios that differ radically from the current model?
- Scan for new technologies that could be a disruptive force to the current business model?
- Look for outsourcing alternatives to create competitive tension with internal functions, operations, processes, and activities (and possibly lead to outsourcing)?
- Require regular competitive benchmarking of key operational, engineering, and business process activities?
- Investigate current and future value contributions from supply markets?
- Focus on the overall external capabilities of potential outsourcing partners (as opposed to just cost reduction capabilities)?
- Address globalization from an outsourcing perspective?
- Link outsourcing strategy to the rate of change for business, technology, and industry?

Leading companies must challenge current business models to be successful in fast changing environments. Correct and timely strategic outsourcing decisions are critical to success.



APPENDIX A: MANAGEMENT CONSIDERATIONS FOR OUTSOURCING PROCUREMENT

Expectations for purchasing and supply organizations continue to rise while budgets for human and technological resources to meet these demands shrink. If they are not already examining the outsourcing option, many purchasing executives will soon face the need to address procurement outsourcing for at least a portion of the activities within their organizations.

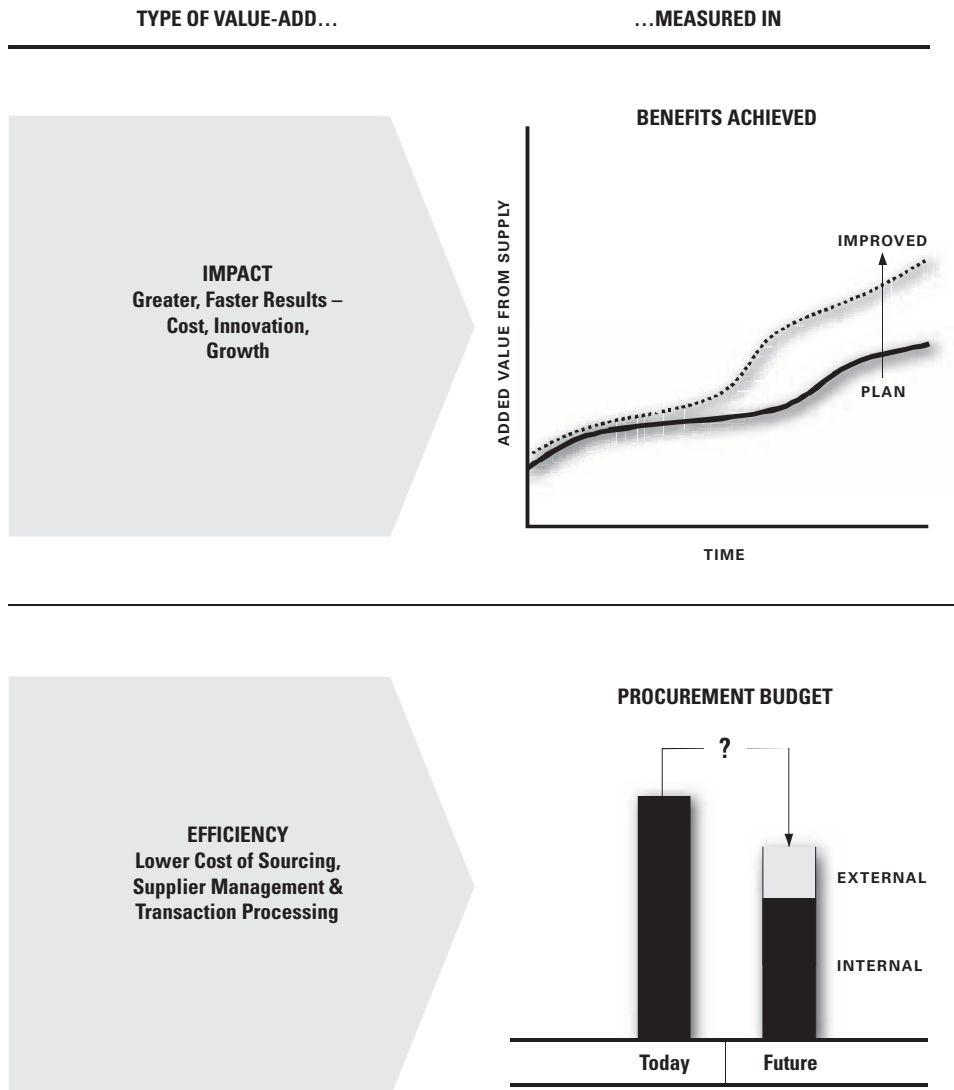
As an aid to executives facing these decisions, this appendix:

- Discusses the rationale for procurement outsourcing
- Provides an overview of the types of procurement outsourcing options available
- Explains an analytical framework and approach to support decision-making

RATIONALE FOR PROCUREMENT OUTSOURCING

In simple terms, the main performance metrics with which to evaluate a procurement or supply management organization are “impact” and “efficiency,” as shown in Figure A.1. *Impact* has traditionally referred to cost reduction on external purchases, but it is increasingly growing to include value created by leveraging supply market capabilities in other areas, such as innovation and revenue generation. *Efficiency* includes the labor cost within the formal procurement organization as well as the extended cross-functional teams and user communities, in addition to the capital and operating costs associated with acquiring, developing, and maintaining databases and tools.

FIGURE A.1: POTENTIAL VALUE-ADD FROM PROCUREMENT ACTIVITIES



Procurement outsourcing becomes attractive when a company can get greater impact from its external purchases through a third party, or when outsourcing can deliver procurement services at a lower cost. Procurement outsourcing providers may achieve greater impact by consolidating volumes across customers and securing more attractive pricing on the aggregated spend. However, these providers may also have access to scarce or proprietary skills, knowledge, and tools that allow them to tap into additional value in the supply market (e.g., first-hand knowledge, of suppliers in nontraditional markets or the ability to develop innovative workarounds to change the balance of power in captive-to-supplier relationships). On the efficiency front, procurement outsourcing providers may have the scale and scope of operations in their particular area of expertise that makes possible investments in tools and technologies that most individual companies could not afford.

The chief procurement officer should not wait for others to ask questions about procurement outsourcing. Instead, the CPO should develop the value proposition for the procurement function and the investments required to deliver it. The CPO should then proactively steer the company toward the correct, fact-based decision about procurement outsourcing. If the CPO cannot put together the value proposition for keeping a particular procurement activity in-house, that activity is a candidate for outsourcing. For the CPO, the future could be one of “Outsource well ... or be outsourced poorly by someone else.”

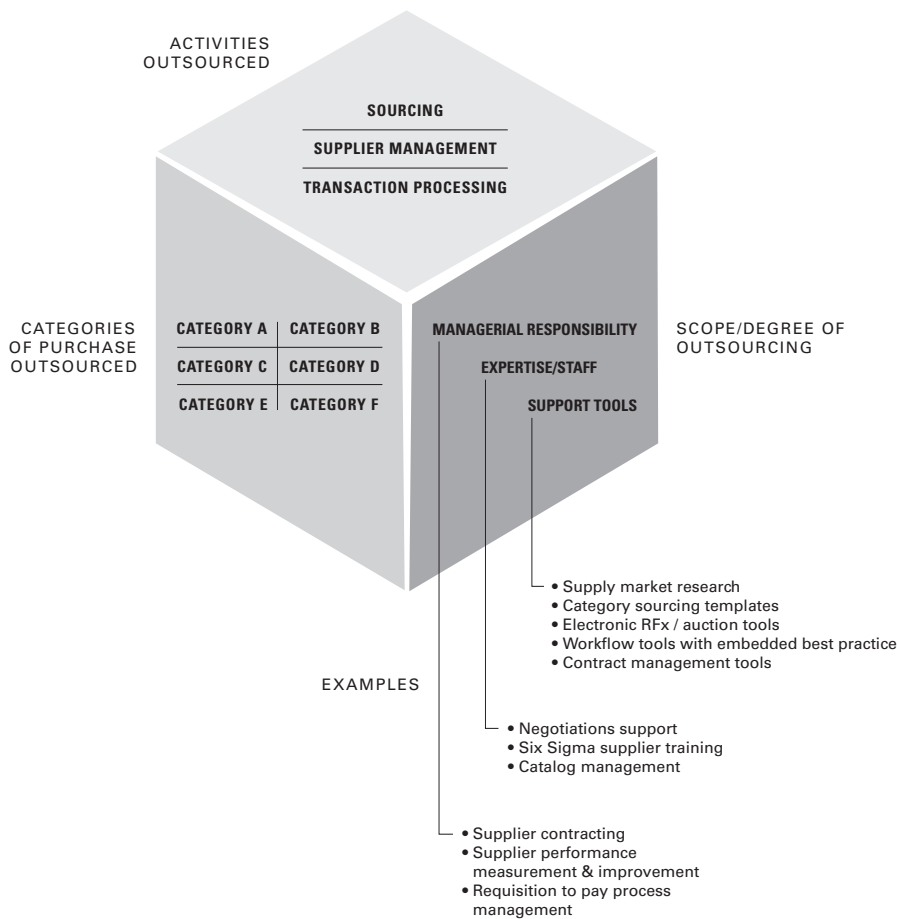
The general approaches for strategic outsourcing described in the body of this report are highly applicable to procurement outsourcing situations — but they will not be repeated in this appendix. Instead the focus is on considerations specific to procurement outsourcing.

PROCUREMENT OUTSOURCING OPTIONS

When evaluating procurement outsourcing, companies should consider options along three main dimensions, as shown in Figure A.2.

- Procurement outsourcing could be focused on a specific category or a group of categories.
- Specific procurement activities (or tasks within them) could be outsourced (e.g., sourcing, supplier management, and transaction processing).
- The scope or degree of outsourcing could be narrow (e.g., acquiring support tools such as industry research, category RFI/RFP templates, and contract management software and auction tools from external providers, rather than developing them in-house), could broaden to include obtaining expert advice or supplemental staff for project work, or could even expand to giving full decision-making, management and operating responsibility to an external party.

FIGURE A.2: DIMENSIONS OF PROCUREMENT OUTSOURCING



DECISION GUIDELINES

Deciding to outsource procurement and selecting which options or combinations of options will best serve the company requires that the CPO know — at a minimum — the following by expenditure category:

- Current and predicted impact of the procurement organization (e.g., by applying best practices)
- Current and predicted efficiency levels (from improved productivity and proper alignment of resources against biggest opportunities)
- Future availability of internal procurement resources (reflecting any likely reduction in resources due to budget squeeze)
- Size of the potential incremental gains in impact or efficiency from using external providers
- Availability and suitability of specific external providers in the marketplace
- Near-term and longer-term risks of outsourcing

There are a number of management considerations and analytical techniques that can help guide the decisions. The following paragraphs illustrate an approach that one company used to evaluate outsourcing options for procurement.

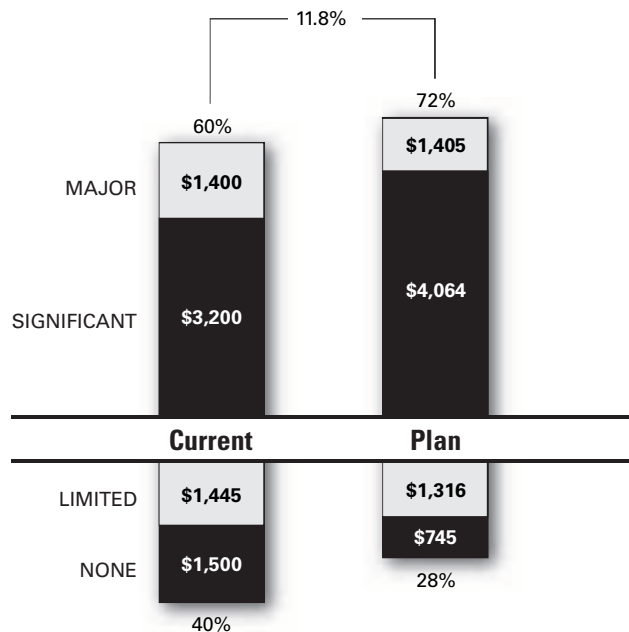
First, the CPO needs to understand what value the procurement organization is currently providing for each category. At the company, the CPO began by looking at the degree to which the procurement organization was involved in the category sourcing decisions, using the scale shown in Figure A.3. Where procurement had demonstrated supply market knowledge combined with the knowledge of the business’ needs for a particular spend category, procurement typically played a significant or major role in sourcing the category. Where this was not the case, the procurement organization played a support role at best.

FIGURE A.3: COMPANY EXAMPLE OF IMPACT SCALE: LEVEL OF PROCUREMENT INVOLVEMENT IN CATEGORY SOURCING DECISIONS

LEVEL OF PROCUREMENT INVOLVEMENT IN CATEGORY SOURCING DECISIONS	DEFINITION
MAJOR	<ul style="list-style-type: none"> • Procurement drives the sourcing process working jointly with business stakeholders. Procurement actively drives specification improvement, standardization, design changes, and other strategies to reduce total cost of ownership. Procurement owns supplier relationship.
SIGNIFICANT	<ul style="list-style-type: none"> • Procurement is actively managing the sourcing process early on. Works jointly with business stakeholders in identifying potential suppliers. Specifications are driven solely by business stakeholders.
LIMITED	<ul style="list-style-type: none"> • Procurement is involved late in the sourcing process (supports bidding and negotiations) and manages the contract administration.
NONE	<ul style="list-style-type: none"> • Procurement not involved in sourcing or contract administration, only provides transaction/purchase order support.

As a first-cut gauge of the impact that procurement was having on the sourcing process, and to provide a basis for looking at resource allocation, the company rated each category and added up external expenditures for each level of involvement. The left-hand bar in Figure A.4 described its current situation. The company found that for 40 percent of its expenditures, procurement’s impact on sourcing was either limited or non-existent. In examining each of these categories, the company determined that the procurement organization could bring additional value to many more of these expenditures in the form of process expertise and best-practice knowledge. It was ultimately determined that procurement could and should have a significant or major involvement in sourcing a full 72 percent of the company’s spend, as shown in the right-hand bar of Figure A.4.

FIGURE A.4: COMPANY EXAMPLE: CURRENT AND FUTURE DEGREE OF PROCUREMENT ORGANIZATION’S INFLUENCE ON SOURCING DECISIONS



Note: Figures in Millions of Dollars

This type of analysis also provided the company with a basis for evaluating procurement efficiency. Using benchmarks, it built category-specific staffing models and compared these with current and budgeted staffing levels. The company found that it needed to re-balance staff, and even then it faced a shortage due to budget reductions in the department. This prompted the company to look at outsourcing alternatives to gain additional impact and boost staff productivity.

The company learned that the procurement outsourcing supplier marketplace has generally developed on either a category outsourcing basis or primary service provider basis. Some outsourcing suppliers have developed to provide services for specific spend categories, such as travel agencies for the travel spend category and temporary employment agencies for a range of temporary labor categories (e.g., administrative, contract programming, medical, security,

and light manufacturing). The chief advantage these category-outsourcing providers possess is their knowledge of the specific process requirements for each spend category. Their disadvantage is that their customers must manage a number of outsourcing relationships if they outsource procurement for multiple categories.

More recently, primary service providers that have established reputations in information technology have begun to expand into an array of business process outsourcing (BPO) functions. Their chief advantage is “one-stop outsourcing,” which offers fewer supplier contact points for procurement outsourcing as well as the scale to provide broad-based technological advantages that have been introduced into procurement, including e-procurement, approved supplier catalogs, e-sourcing, spend management, and contract management. Their disadvantage is that they are somewhat untested; they do not have many examples of long-term BPO customers at this early stage.

Consequently, the company decided to evaluate the available supplier resources on a category-by-category basis, examining the category’s fit with a category-specific outsourcing model or multi-category BPO outsourcing model (respectively known as “vertical” and “horizontal” models).

For BPO, the scoring mechanism took the form depicted in Figure A.5, while for category-specific sourcing the mechanism in Figure A.6 was used.

FIGURE A.5: COMPANY EXAMPLE: CATEGORY RATING PROCESS FOR OUTSOURCING THE SOURCING/SUPPLIER SELECTION PROCESS TO A BPO PROVIDER

	CATEGORY EVALUATION CRITERIA	CATEGORY RATING SCALE	
		LIMITS OUTSOURCING OPPORTUNITY	SUPPORTS OUTSOURCING OPPORTUNITY
INTERNAL CONSIDERATIONS – IN COMPANY’S CONTROL	<ul style="list-style-type: none"> Category criticality to company’s competitive advantage and business strategy 	<ul style="list-style-type: none"> Extremely important to maintain competitive advantage and support business strategy 	<ul style="list-style-type: none"> Non-critical to maintain competitive advantage (e.g., purely transactional activity)
	<ul style="list-style-type: none"> Current contract constraints 	<ul style="list-style-type: none"> High level of contract constraints, precluding termination of contract or switching suppliers without significant penalties to Company (locked in for more than three years to come) 	<ul style="list-style-type: none"> Minimal or no contract constraints (e.g., early termination “out clause”) or current contract ending within three-year time frame
	<ul style="list-style-type: none"> Degree of customer interface required 	<ul style="list-style-type: none"> High level of customer interaction required due to category complexity (e.g., complex supplier qualification process; difficulty in implementation, balance of trade) 	<ul style="list-style-type: none"> Low level of customer interaction required due to category’s commoditization and transactional nature (e.g., relatively easy qualification process, minimal implementation barriers)
OTHER	<ul style="list-style-type: none"> Regulatory constraints 	<ul style="list-style-type: none"> Complex and numerous regulations that create barriers to supplier competition 	<ul style="list-style-type: none"> Minimal or no regulations

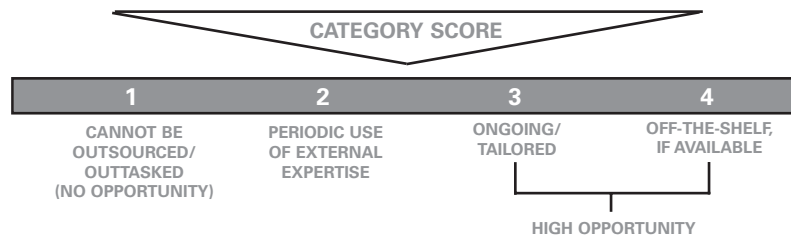
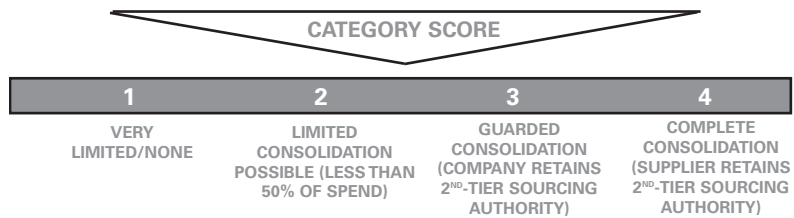


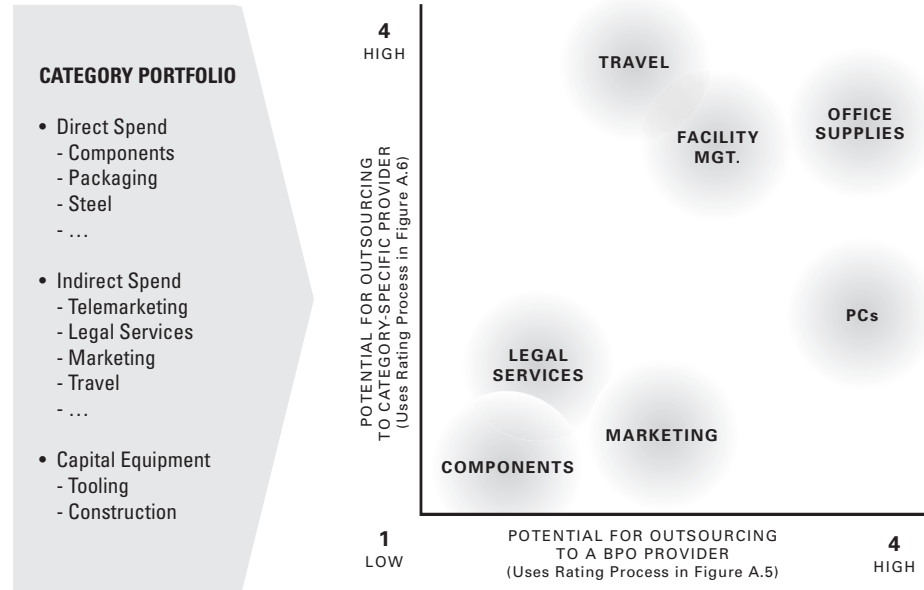
FIGURE A.6: COMPANY EXAMPLE: CATEGORY RATING PROCESS FOR OUTSOURCING THE SOURCING/SUPPLIER SELECTION PROCESS TO A CATEGORY-SPECIFIC PROVIDER

	CATEGORY EVALUATION CRITERIA	CATEGORY RATING SCALE	
		LIMITS OUTSOURCING OPPORTUNITY	SUPPORTS OUTSOURCING OPPORTUNITY
INTERNAL CONSIDERATIONS – IN COMPANY’S CONTROL	<ul style="list-style-type: none"> Importance of ongoing supplier competition 	<ul style="list-style-type: none"> Extremely important to maintain competitiveness in supply market 	<ul style="list-style-type: none"> Minimal impact on supply market competitiveness if categories are consolidated for vertical sourcing
	<ul style="list-style-type: none"> Competence fragmented, unique 	<ul style="list-style-type: none"> Unique, specialized category knowledge/sourcing competence required 	<ul style="list-style-type: none"> Non-unique, specialized category knowledge/sourcing competence required
	<ul style="list-style-type: none"> (Perceived or real) availability of umbrella suppliers who can manage vertically sourced categories (i.e., as Tier 1 or primary supplier) 	<ul style="list-style-type: none"> Lack of umbrella supplier with sufficient technical capabilities (i.e., immature supplier market) 	<ul style="list-style-type: none"> Existing umbrella supplier market with sufficient technical capabilities
OTHER	<ul style="list-style-type: none"> Degree of current vertical sourcing activity 	<ul style="list-style-type: none"> Currently vertically sourced with complementary categories consolidated or sourced together 	<ul style="list-style-type: none"> Not currently vertically sourced



After completing the analysis by category, the company plotted the categories on a grid like that shown in Figure A.7, building an array to better understand its options for outsourcing the sourcing and supplier selection process for these categories

FIGURE A.7: ARRAYING CATEGORIES BASED ON POTENTIAL FOR USING CATEGORY-SPECIFIC OR BPO OUTSOURCING PROVIDERS



The approach that this company used to identify potential activities to outsource is just one of several that could have been taken. It is offered here as an illustration, rather than an all-encompassing “off-the-shelf” methodology.

ADDITIONAL CONSIDERATIONS

Even though a company identifies procurement outsourcing as an attractive option, it should also consider other factors in its decision process:

- Supplier marketplace maturity
- Enabling technologies
- Tipping point

Supplier Marketplace Maturity

The procurement outsourcing marketplace is fragmented: many segments are relatively immature, and the market as a whole is in flux as BPO providers jockey for position while building experience and scale. With this in mind, companies should evaluate the competence, capability, and stability of potential procurement outsourcing providers even more

carefully than for other business activities with more mature outsourcing markets. What experience and references can the provider point to? What have its customers to date experienced? How likely is a service failure? If one occurs, what is the level of confidence that the provider can correct it quickly? If the supplier suddenly exits the market, what is the fall-back position? How difficult will it be to recover?

Enabling Technologies

The challenge of keeping up with developments in enabling technologies is very often a key reason to consider outsourcing. This phenomenon occurred previously in information technology. In the 1970s and 1980s, companies still considered building applications systems “in-house” to retain a competitive technology position. However, by the early 1990s it was clear that companies paid a high price for the investment and focus on this management and technological capability. Packaged applications became popular and companies shifted in-house investment to more core activities, transferring information technology architecture, operations, and significant amounts of applications development to third-party providers.

Enabling technologies for procurement are likely to follow a similar pattern. For example:

- When e-sourcing consists of a few “pilot” reverse auctions, companies can afford the required resources. But when best practices develop into specialized and integrated approaches for individual spend categories or supplier geographies, scale and leverage are also required from outsourced suppliers
- Similarly, pioneering companies may have invested in “homegrown” supplier portals, collaboration software, and supplier certification techniques, but now these activities can benefit from scaled, single-access, multiple-use approaches from a third-party outsourced service
- Spend management requires integration with existing processes and systems and resources to cleanse and classify supplier data. Spend management extends into features to reduce maverick spending and support consumption or demand management programs. This technology is just beginning to enter the complexity stage in which it will rapidly outrun an individual company’s appetite for capital and management focus

Tipping Point

Another factor to consider is whether procurement outsourcing has reached a “tipping point.” Has a respected company engaged in this activity to the extent that it has gained credibility in the CEO’s mind or created a real or perceived disadvantage for those companies that do not do it? Again, a comparison with IT outsourcing is useful. It is generally felt that Eastman Kodak made information technology outsourcing “respectable” when it transferred data center operations to IBM in 1989. This activity legitimized the transfer of what was then felt to be a difficult, expensive, and almost unmanageable function to a highly regarded technology specialist.

The market may soon come to recognize this tipping point for procurement outsourcing and thus signal the impetus for acceptance within an industry, or for an innovative approach that gains wider acceptance.



APPENDIX B : SURVEY QUESTIONNAIRE

STRATEGIC OUTSOURCING RESEARCH
2004 PULSE SURVEY

A JOINT RESEARCH EFFORT BY
CAPS RESEARCH
A.T. KEARNEY, INC.

INTRODUCTION

INTRODUCTION AND BACKGROUND TO THE RESEARCH

Thank you for participating in this research and benchmarking study of strategic outsourcing, being conducted jointly by CAPS Research, Arizona State University, and A. T. Kearney, Inc.

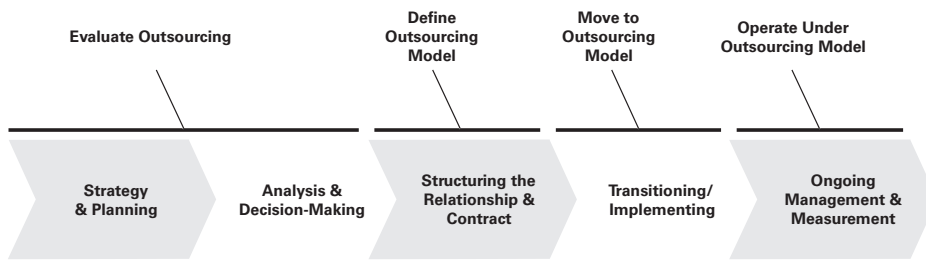
Interest in outsourcing has increased substantially in the past few years, as companies seek greater focus, lower costs, greater flexibility and access to new capabilities and markets. In some areas such as information technology, manufacturing, and logistics/distribution, outsourcing is an established practice that produces major benefits for companies that manage outsourcing well. In other areas such as human resources, product development and procurement, outsourcing is in the early stages. Service provider markets and proven practices for outsourcing management are still developing.

As companies look at entering into outsourcing, or expanding their use of outsourcing across a range of activities, what can executives learn from the experiences of others to improve the probability of a successful outsourcing decision? This study's purpose is to find out by accomplishing three primary objectives:

1. Understand how companies plan for and manage strategic outsourcing relationships
2. Determine which strategic outsourcing management approaches are the most effective for achieving superior results
3. Help clarify the current state of procurement outsourcing

To structure the research, we have developed the following research framework. Several questions in this survey incorporate this five-step strategic outsourcing process.

FIGURE B.1: RESEARCH FRAMEWORK: THE STRATEGIC OUTSOURCING PROCESS



MAJOR RESEARCH HYPOTHESIS: Successful companies excel at all parts of the strategic outsourcing process

GUIDELINES

SURVEY GUIDELINES

THE SURVEY IS STRUCTURED AS FOLLOWS

Participant description: Contact and background information

Part 1 – Outsourcing profile: Questions 1 and 2 ask about the present and future scope of outsourcing within your unit and the role of procurement in the outsourcing process

Part 2 – Reasons for outsourcing: Questions 3 and 4 ask about the reasons behind your outsourcing decisions.

Part 3 – Goal achievement: Questions 5 - 9 ask about results achieved against your outsourcing goals, and the factors that contributed to your level of achievement.

Part 4 – Best and worst case examples: Questions 10 - 12 ask about the factors contributing to your outsourcing performance compared to your goals for your best and worst case examples.

Part 5 – Procurement outsourcing: Questions 13 - 19 ask about the present and future scope of outsourcing within your unit specifically for procurement activities.

INSTRUCTIONS FOR COMPLETING THE SURVEY

Please pre-select a particular unit of your company (e.g., corporate, SBU, division, region) and answer all questions from the perspective of that unit.

CONFIDENTIALITY NOTICE

Individual responses will not be released without approval of the participating company.

PARTICIPANT DESCRIPTION

PLEASE PROVIDE YOUR CONTACT INFORMATION

Name of person completing survey: _____

Title: _____

Company name: _____

Address: _____

City/State: _____

Country/Postal Code: _____

Telephone: _____

Fax: _____

Email: _____

Please indicate the unit of your company for which you are responding (e.g., corporate, division, SBU, region).

Unit name: _____

Unit headquarters location (country): _____

Please indicate your unit's primary industry (check one only).

- | | |
|---|---|
| <input type="checkbox"/> Aerospace | <input type="checkbox"/> Metals/glass processing |
| <input type="checkbox"/> Automotive | <input type="checkbox"/> Mining |
| <input type="checkbox"/> Chemical, oil and gas | <input type="checkbox"/> Pharmaceuticals |
| <input type="checkbox"/> Components and systems | <input type="checkbox"/> Professional/information services |
| <input type="checkbox"/> Construction | <input type="checkbox"/> Pulp and paper |
| <input type="checkbox"/> Engineering | <input type="checkbox"/> Retail |
| <input type="checkbox"/> Financial institutions | <input type="checkbox"/> Technical appliances and equipment |
| <input type="checkbox"/> Food and nutrition | <input type="checkbox"/> Telecommunications services |
| <input type="checkbox"/> Heavy machinery | <input type="checkbox"/> Transportation services |
| <input type="checkbox"/> High-tech network infrastructure | <input type="checkbox"/> Utilities |
| <input type="checkbox"/> Household and cosmetics | <input type="checkbox"/> White goods |
| <input type="checkbox"/> Media/entertainment | <input type="checkbox"/> Other (_____) |

PARTICIPANT DESCRIPTION

*Please indicate the approximate 2003 annual revenue for your unit
(please convert to US dollars).*

- Under \$100 million
- \$101 million - 500 million
- \$501 million - \$1 billion
- \$1.1 billion - \$5 billion
- \$5.1 billion - \$10 billion
- \$10.1 billion - \$20 billion
- Over \$20 billion

SAMPLE

PARTICIPANT DESCRIPTION

Please indicate the countries/regions where your unit has significant operating or marketing presence (check all that apply).

REGION/COUNTRY	OPERATING - MANUFACTURING LOCATIONS OF OUR UNIT (PRODUCTS AND SERVICES)	MARKETS SERVED BY OUR UNIT
<i>NORTH AMERICA</i>		
Canada	<input type="checkbox"/>	<input type="checkbox"/>
Mexico	<input type="checkbox"/>	<input type="checkbox"/>
United States	<input type="checkbox"/>	<input type="checkbox"/>
<i>CENTRAL/SOUTH AMERICA</i>		
Argentina	<input type="checkbox"/>	<input type="checkbox"/>
Brazil	<input type="checkbox"/>	<input type="checkbox"/>
Venezuela	<input type="checkbox"/>	<input type="checkbox"/>
Central America/Carribbean	<input type="checkbox"/>	<input type="checkbox"/>
Other South American countries (please specify: _____)	<input type="checkbox"/>	<input type="checkbox"/>
<i>EUROPE, MIDDLE EAST, AFRICA (EMEA)</i>		
Eastern Europe	<input type="checkbox"/>	<input type="checkbox"/>
Central Europe	<input type="checkbox"/>	<input type="checkbox"/>
Western Europe	<input type="checkbox"/>	<input type="checkbox"/>
Middle East	<input type="checkbox"/>	<input type="checkbox"/>
South Africa	<input type="checkbox"/>	<input type="checkbox"/>
Other EMEA countries (please specify: _____)	<input type="checkbox"/>	<input type="checkbox"/>
<i>ASIA/PACIFIC</i>		
Australia	<input type="checkbox"/>	<input type="checkbox"/>
China	<input type="checkbox"/>	<input type="checkbox"/>
India	<input type="checkbox"/>	<input type="checkbox"/>
Indonesia	<input type="checkbox"/>	<input type="checkbox"/>
Japan	<input type="checkbox"/>	<input type="checkbox"/>
Malaysia	<input type="checkbox"/>	<input type="checkbox"/>
Philippines	<input type="checkbox"/>	<input type="checkbox"/>
Singapore	<input type="checkbox"/>	<input type="checkbox"/>
South Korea	<input type="checkbox"/>	<input type="checkbox"/>
Taiwan	<input type="checkbox"/>	<input type="checkbox"/>
Thailand	<input type="checkbox"/>	<input type="checkbox"/>
Other Asia/Pacific countries (please specify: _____)	<input type="checkbox"/>	<input type="checkbox"/>

OUTSOURCING PROFILE

1. Please indicate your current and expected future level of outsourcing for the following activities.

Currently outsourced (check one column per row)

ACTIVITY	None 0%	Very Little 1-25%	Some 26-50%	Majority 51-75%	Significant Majority 76-99%	All 100%
Research	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Product and service development	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Marketing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Sales	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Procurement/Supply management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Engineering/detailed design	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Manufacturing/operations	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Distribution/Fulfillment	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Customer call center	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Field service	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Finance and accounting	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Legal/regulatory	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Human resources	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Information technology	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Plan to outsource in the next 18 months (check one column per row)

ACTIVITY	None 0%	Very Little 1-25%	Some 26-50%	Majority 51-75%	Significant Majority 76-99%	All 100%
Research	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Product and service development	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Marketing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Sales	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Procurement/Supply management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Engineering/detailed design	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Manufacturing/operations	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Distribution/Fulfillment	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Customer call center	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Field service	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Finance and accounting	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Legal/regulatory	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Human resources	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Information technology	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

OUTSOURCING PROFILE

2. Please indicate your procurement organization's involvement in the outsourcing management process.

Degree of involvement of your company's procurement organization in the outsourcing management process (check one column per row).

ACTIVITY	Degree of involvement				
	None 1	2	Somewhat involved 3	4	Significant 5
Research	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Product and service development	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Marketing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Sales	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Procurement/Supply management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Engineering/detailed design	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Manufacturing/operations	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Distribution/Fulfillment	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Customer call center	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Field service	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Finance and accounting	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Legal/regulatory	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Human resources	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Information technology	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

REASONS FOR OUTSOURCING

3. For those activities that you are currently outsourcing or will outsource, what are the primary reasons that you chose to outsource?

Reasons to outsource (check all that apply)

- Gain access to technology not resident in our company
- Increase speed to market
- Reduce capital investment
- Grow revenue
- Turn fixed costs into variable costs
- Improve quality
- Reduce operating cost
- Meet downsizing requirements
- Gain access to needed skills
- Focus on core business
- Reduce development costs
- Gain access to markets
- Increase flexibility and responsiveness
- Reduce customer response cycle time
- Create additional capacity
- Align with company policy/philosophy/culture
- Provide back-up capabilities
- Provide an alternative to building the capability inside our company
- Obtain intelligence on/benchmarks of competitiveness for in-house activities
- Other (_____)

REASONS FOR OUTSOURCING

4. For those activities that you are not outsourcing, and do not plan to outsource, what are the primary reasons you have chosen not to outsource?

Reasons not to outsource (check all that apply)

- Lack of adequate supply base (cost, environmental, technical, social)
- Loss of control
- Protection of intellectual property
- Company policy/philosophy/culture
- Possibility supplier will become a competitor
- Difficulty reversing decision in the future
- Fear of becoming too dependent on the supplier
- Activities not outsourced are highly profitable
- Activities not outsourced are considered core competencies
- Concerns for labor/union/community reaction
- Previous lack of success with outsourcing
- Physical distance
- Loss of critical capability
- Maintain internal morale
- Labor union restrictions
- Legal restrictions on workforce changes
- Other legal restrictions
- Inadequate business case
- Other _____

GOAL ACHIEVEMENT

5. Where you have chosen to outsource activities, to what extent have you met your goals on these performance dimensions? If the performance dimension was not a goal, please indicate.

Performance dimension (check one per row)	Fell far short -3	-2	-1	Achieved Goal 0	1	2	Far exceeded 3	Not a goal
Gain access to technology not resident in our company	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Increase speed to market	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Reduce capital investment	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Grow revenue	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Turn fixed costs into variable costs	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Improve quality	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Reduce operating cost	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Meet downsizing requirements	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Gain access to needed skills	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Focus on core business	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Reduce development costs	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Gain access to markets	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Increase flexibility and responsiveness	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Reduce customer response cycle time	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Create additional capacity	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Support company policy/philosophy/culture	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Provide back-up capabilities	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Provide an alternative to building the capability inside our company	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Obtain intelligence on/benchmarks of competitiveness for in-house activities	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

GOAL ACHIEVEMENT

6. What range of cost savings have you realized from your outsourcing efforts?

Range (check one only)

- Too early to tell
- None
- 1 - 5 %
- 6 - 10%
- 11 - 15%
- 16 - 20%
- 21 - 25%
- 26 - 30%
- Over 30%

7. How quickly did you begin to realize these cost savings?

Timing (check one only)

- Not applicable
- 1 - 6 months
- 7 - 12 months
- 1 - 2 years
- Beyond 2 years

GOAL ACHIEVEMENT

8. To what degree did the following factors contribute to your level of performance against your goals?

Degree that this factor contributed to your level of performance (Check one per row)

Factor	Degree that this factor contributed to your level of performance (Check one per row)						
	No impact 1	2	3	4	5	6	Major impact 7
OUTSOURCING STRATEGY AND PLANNING							
Systematic processes to identify candidate activities for outsourcing based on competitive analysis	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Executive consensus about the appropriateness of this activity for outsourcing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Clear directional business case and rationale to justify outsourcing this activity	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
ANALYSIS AND DECISION-MAKING							
Formalized financial and situational analysis processes to decide whether to outsource this activity	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Cross-functional decision-making and agreement to outsource this activity (cross-unit where appropriate), including approaches to overcoming barriers to success	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
STRUCTURING THE RELATIONSHIP AND CONTRACT							
Formal process to establish requirements and select the outsourcing supplier for this activity	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Cross-functional decision-making to select the outsourcing supplier for this activity (cross-unit where appropriate)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Formalized and clear intellectual property rights and ownership agreement with the supplier	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Pre-established and agreed-upon business and technical goals for the relationship, including performance metrics	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
High degree of trust	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Formal contract and service level agreement	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Systematic process to determine what information to share with each other	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Clear roles and responsibilities for managing the execution of the contract	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Formal contingency/exit strategy	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

GOAL ACHIEVEMENT

8. (continued) To what degree did the following factors contribute to your level of performance against your goals?

Degree that this factor contributed to your level of performance (Check one per row)

Factor	No impact						Major impact
	1	2	3	4	5	6	7
TRANSITIONING/IMPLEMENTING							
Formal governance process and project plan (schedule) to guide and manage the transition to the outsourced model	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Joint education and training for affected activities and processes (both outsourced elements and interfaces with remaining internal elements)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Formal plan to maintain motivation of outsourced or displaced staff during the transition process	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Clear accountability for transition management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
ONGOING MANAGEMENT AND MEASUREMENT							
Clear assignment of responsibilities to the correct people, from both parties, to manage the relationship	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Accurate and effective bilateral information flow to execute the requirements of the contract and SLA	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Formal joint problem resolution process	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Accurate and valid performance metrics	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Mechanisms to track and report performance versus goals	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Formal process to take corrective action	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

GOAL ACHIEVEMENT

9. What involvement did your procurement organization have at each point in the outsourcing management process?

Degree of involvement of your company's procurement organization in the outsourcing management process
(check one per column per row)

<i>Outsourcing management process steps</i>	None 1	2	Somewhat Involved 3	4	Significant 5
Outsourcing management and planning	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Analysis and decision-making	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Structuring the relationship and contract	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Transitioning/Implementing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Ongoing management and measurement	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

BEST AND WORST EXAMPLES

10. For those activities that you have outsourced, please indicate the activity where you have had the overall best results and the overall worst results (maximum one check per column)

ACTIVITY	BEST	WORST
Research	<input type="checkbox"/>	<input type="checkbox"/>
Product and service development	<input type="checkbox"/>	<input type="checkbox"/>
Marketing	<input type="checkbox"/>	<input type="checkbox"/>
Sales	<input type="checkbox"/>	<input type="checkbox"/>
Procurement/Supply management	<input type="checkbox"/>	<input type="checkbox"/>
Engineering/Detailed design	<input type="checkbox"/>	<input type="checkbox"/>
Manufacturing/operations	<input type="checkbox"/>	<input type="checkbox"/>
Distribution/Fulfillment	<input type="checkbox"/>	<input type="checkbox"/>
Customer call center	<input type="checkbox"/>	<input type="checkbox"/>
Field service	<input type="checkbox"/>	<input type="checkbox"/>
Finance and accounting	<input type="checkbox"/>	<input type="checkbox"/>
Legal/regulatory	<input type="checkbox"/>	<input type="checkbox"/>
Human resources	<input type="checkbox"/>	<input type="checkbox"/>
Information technology	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>

11. For both the best and worst result cases which you identified in Question 10 above, please describe the most significant reasons or causes (up to three) for high (best) and low (worst) performance. Please focus on a specific situation in responding.

MOST SIGNIFICANT REASONS FOR HIGH PERFORMANCE (BEST CASE)

- 1.
- 2.
- 3.

MOST SIGNIFICANT REASONS FOR LOW PERFORMANCE (WORST CASE)

- 1.
- 2.
- 3.

BEST AND WORST EXAMPLES

12. For your best and worst case examples, what involvement did your procurement organization have at each point in the outsourcing management process?

BEST CASE

Degree of involvement of your company's procurement organization in the outsourcing management process (check one per column per row)

<i>Outsourcing management process steps</i>	None 1	2	Somewhat Involved 3	4	Significant 5
Outsourcing management and planning	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Analysis and decision-making	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Structuring the relationship and contract	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Transitioning/Implementing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Ongoing management and measurement	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

WORST CASE

Degree of involvement of your company's procurement organization in the outsourcing management process (check one per column per row)

<i>Outsourcing management process steps</i>	None 1	2	Somewhat Involved 3	4	Significant 5
Outsourcing management and planning	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Analysis and decision-making	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Structuring the relationship and contract	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Transitioning/Implementing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Ongoing management and measurement	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

PROCUREMENT OUTSOURCING

Please indicate whether the following procurement activities are not currently outsourced, currently outsourced, or planned for outsourcing. Please provide separate answers for direct materials, maintenance, repair and operating supplies, other indirect purchases, capital expenditures, services, and goods for resale as noted.

13. Outsourcing of procurement activities for direct materials (includes raw materials, components, assemblies, packaging)

Procurement activity (check one entry per row)	Not currently outsourced	Currently outsourced	Definitely plan to outsource
Category/commodity strategy and supplier selection	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier assessment and evaluation	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier development	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier certification	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Ordering and replenishment and payment/settlement transaction processing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Coding and catalog management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Procurement information systems management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

14. Outsourcing of procurement activities for maintenance, repair and operating supplies (includes supplies to maintain buildings and production equipment)

Procurement activity (check one entry per row)	Not currently outsourced	Currently outsourced	Definitely plan to outsource
Category/commodity strategy and supplier selection	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier assessment and evaluation	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier development	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier certification	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Ordering and replenishment and payment/settlement transaction processing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Coding and catalog management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Procurement information systems management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

PROCUREMENT OUTSOURCING

15. Outsourcing of procurement activities for other indirect materials (includes materials and supplies to support non-production activities)

Procurement activity (check one entry per row)	Not currently outsourced	Currently outsourced	Definitely plan to outsource
Category/commodity strategy and supplier selection	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier assessment and evaluation	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier development	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier certification	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Ordering and replenishment and payment/settlement transaction processing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Coding and catalog management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Procurement information systems management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

16. Outsourcing of procurement activities for capital expenditures

Procurement activity (check one entry per row)	Not currently outsourced	Currently outsourced	Definitely plan to outsource
Category/commodity strategy and supplier selection	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier assessment and evaluation	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier development	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier certification	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Ordering and replenishment and payment/settlement transaction processing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Coding and catalog management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Procurement information systems management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

PROCUREMENT OUTSOURCING

17. Outsourcing of procurement activities for services (includes administrative, professional, transportation, travel and utilities services)

Procurement activity (check one entry per row)	Not currently outsourced	Currently outsourced	Definitely plan to outsource
Category/commodity strategy and supplier selection	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier assessment and evaluation	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier development	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier certification	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Ordering and replenishment and payment/settlement transaction processing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Coding and catalog management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Procurement information systems management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

18. Do you purchase goods-for-resale? (Includes goods sold by wholesalers and retailers, and spare equipment and parts purchased and resold by OEMs to their installed customer base)

Yes No

If yes, please continue to question 19, if no, please proceed to end of survey.

19. Outsourcing of procurement activities for goods-for-resale

Procurement activity (check one entry per row)	Not currently outsourced	Currently outsourced	Definitely plan to outsource
Category/commodity strategy and supplier selection	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier assessment and evaluation	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier development	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supplier certification	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Ordering and replenishment and payment/settlement transaction processing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Coding and catalog management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Procurement information systems management	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Other (_____)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

PROCUREMENT OUTSOURCING

Thank you for participating in this survey.

Please send this completed survey to

Debbie Maciejewski

CAPS Research

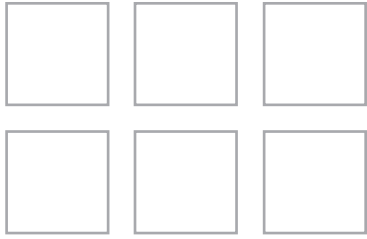
P.O. Box 22160

Tempe, AZ 85285-2160

Phone: 480-752-6276

Fax: 480-491-7885

SAMPLE



APPENDIX C : DESCRIPTION OF STATISTICAL ANALYSIS METHODOLOGY

The analytical approach used in this research had three distinct steps:

1. Summary and analysis of raw data, to provide basic profiles of the respondents and their use of outsourcing
2. An exploratory data analysis with the objective of identifying underlying patterns in the data
3. The development of several prescriptive models based on the outsourcing strategies and approaches used by survey respondents and the results they achieved.

Each of these steps yielded unique insights into the strategic outsourcing process and procurement's role within it. The first step required only basic statistical analysis techniques. The second and third steps required a far more sophisticated and rigorous approach to the analysis. For those readers interested in the technical details, this appendix describes the techniques used, and the results of the step-two and step-three analyses.

ANALYTICAL TECHNIQUES USED

For the analyses of steps two and three, the research team used the following analytical techniques:

- Factor analysis: a technique for analyzing the underlying structure of a set of variables. In this case the variables were the individual responses to the strategic outsourcing survey instrument. The basic idea is that the members of a set of variables, each of which has been measured for a number of observations, have some of their structure determined by certain underlying common constructs or factors
- Exploratory factor analysis (EFA): EFA requires that the investigators hypothesize beforehand the number of common criteria or factors. The hypothesis regarding the number of criteria (factors) must be based upon the nature of the considered variables and an expectation of which factor is likely to load on which variable

A number of step-two and step-three analyses were conducted for all respondents in the survey, and comparative analyses were conducted for industry groups and for other subsets of the population. The analyses providing the greatest insight are summarized below.

ANALYSES OF THE ENTIRE POPULATION

Analysis 1: Is the five-phase strategic outsourcing process model valid and can it be improved?

As mentioned in the body of this report, the research team initially developed a five-phase model for the strategic outsourcing process and identified a number of activities that take place within each phase. This model formed the basis for several questions within the online survey instrument. Question 8 specifically asked respondents to rate the degree to which each of the activities contributed to the level of performance against outsourcing goals.

The first analysis performed in step two was to test the validity of the five-phase model, and revise it as appropriate. The requirement for using EFA was satisfied in the investigation by defining the major criteria and the stated subcomponents of each criterion in Question 8.

In order to determine the underlying structure or latent variables associated with Question 8, an EFA was accomplished using principal components analysis. EFA enables data reduction through identifying latent variables from the larger set of variables that can be used later in multivariate analysis. The use of EFA also allows for testing of the *a priori* outsourcing five-phase process used as the basis of the strategic outsourcing survey. The original process outsourcing model is pictured in Figure C.1. The related activities for each phase in the five-phase model are pictured in Figure C.2.

FIGURE C.1: INITIAL FIVE-PHASE RESEARCH FRAMEWORK

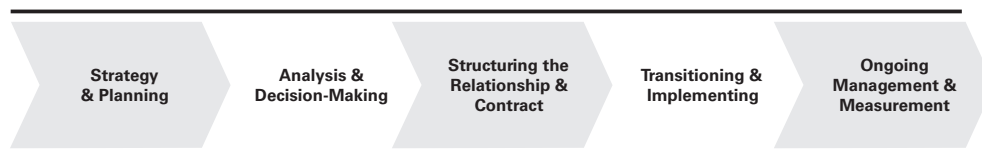


FIGURE C.2: INITIAL FIVE-PHASE STRATEGIC OUTSOURCING PROCESS MODEL ACTIVITIES
STRATEGY AND PLANNING

- a. Systematic process to identify candidate activities for outsourcing based on competitive analysis
- b. Executive consensus about the appropriateness of outsourcing this activity
- c. Clear directional business case and rationale to justify outsourcing this activity

ANALYSIS AND DECISION MAKING

- d. Formalized financial and situational analysis processes to decide whether to outsource this activity
- e. Cross-functional decision-making and agreement to outsource this activity

STRUCTURING THE RELATIONSHIP AND CONTRACT

- f. Formal process to establish requirements and select the outsourcing supplier for this activity
- g. Cross-functional decision-making to select the outsourcing supplier for this activity
- h. Formalized and clear intellectual property rights and ownership agreement with the supplier
- i. Pre-established and agreed-upon business and technical goals for the relationship, including performance metrics
- j. High degree of trust
- k. Formal contract and service level agreement
- l. Systematic process to determine what information to share with each other
- m. Clear roles and responsibilities for managing the execution of the contract
- n. Formal contingency/exit strategy

TRANSITIONING AND IMPLEMENTING

- o. Formal governance process and project plan to guide and manage the transition to the outsourced model
- p. Joint education and training for affected activities and process
- q. Formal plan to maintain motivation of outsourced or displaced staff during the transition process
- r. Clear accountability for transition management

ONGOING MANAGEMENT AND MEASUREMENT

- s. Clear assignment of responsibilities to the correct people, from both parties, to manage the relationship
 - t. Accurate and effective bilateral information flow to execute the requirements of the contract and service level agreement
 - u. Formal joint problem resolution process
 - v. Accurate and valid performance metrics
 - w. Mechanisms to track and report performance versus goals
 - x. Formal process to take corrective action
-

The statistical analysis revealed that the *a priori* five-phase model was a good approximation of the latent variables underlying the data collected in the survey, but that an even better model existed with three major phases as pictured in Figure C.3. The new three-phase model combined the first two phases from the original model (“outsourcing strategy and planning” and “analysis and decision-making”) into a new first phase titled “strategy planning and analysis.” The majority of activities in the original middle phase remained in place, making a new phase that can be viewed as “contracting and relationship development.” The new three-phase model combined the last two phases from the original model (“transitioning and implementing” and “ongoing management and measurement”) into a new third phase titled “implementation.”

FIGURE C.3: REVISED THREE-PHASE STRATEGIC OUTSOURCING PROCESS MODEL



This is an interesting finding in that the implementation activities of the new strategic outsourcing process model are highly correlated and explain the 55 percent variation in how factors contribute to a firm’s level of performance against goals. “Contracting and relationship development” and “strategy planning and analysis” explain 5.8 percent and 4.7 percent of the variance, respectively. The revised process-outsourcing model with the related activities for each category in the three-phase model is pictured in Figure C.4. Note that the number following each activity is important and reflects the relative degree of influence of the activity on firm performance against goals within each phase of the new process model.

FIGURE C.4: REVISED STRATEGIC OUTSOURCING PROCESS MODEL ACTIVITIES

	RELATIVE DEGREE OF INFLUENCE ON FIRM GOALS
STRATEGY AND PLANNING ANALYSIS	
b. Executive consensus about the appropriateness of outsourcing this activity	0.84797
c. Clear directional business case and rational to justify outsourcing this activity	0.81901
a. Systematic processes to identify candidate activities for outsourcing based on competitive analysis	0.67089
f. Formal process to establish requirements and select the outsourcing supplier for this activity	0.63230
d. Formalized financial and situational analysis processes to decide whether to outsource this activity	0.55417
o. Formal governance process and project plan to guide and manage the transition to the outsourced model	0.50626
g. Cross-functional decision-making and agreement to outsource this activity	0.38981
CONTRACTING AND RELATIONSHIP DEVELOPMENT	
k. Formal contract and service level agreement	0.72851
n. Formal contingency/exit strategy	0.71375
l. Systematic process to determine what information to share with each other	0.70518
j. High degree of trust	0.63523
m. Clear roles and responsibilities for managing the execution of the contract	0.61610
h. Formalized and clear intellectual property rights and ownership agreement with the supplier	0.54003
i. Pre-established and agreed-upon business and technical goals for the relationship, including performance metrics	0.44179
IMPLEMENTATION	
w. Mechanisms to track and report performance versus goals	0.91026
x. Formal process to take corrective action	0.88701
u. Formal joint problem resolution process	0.87416
v. Accurate and valid performance metrics	0.83850
s. Clear assignment of responsibilities to the correct people, from both parties, to manage the relationship	0.65360
t. Accurate and effective bilateral information flow to execute the requirements of the contract and service level agreement	0.61634
r. Clear accountability for transition management	0.60455
p. Joint education and training for affected activities and processes	0.56706
o. Managing the formal governance process and project plan to guide and manage the transition to the outsourced model	0.55758
q. Formal plan to maintain motivation of outsourced or displaced staff during the transition process	0.45772

Analysis 2: Can the new three-phase outsourcing process model predict “level of savings” and “time to savings”?

The dependent variables of range of savings (Question 6) and time to savings (Question 7) can be regressed on these new process model phases individually to determine if a significant relationship exists between the latent and dependent variables. The predictive model was highly significant at a p-value of <0.0001. The model explains approximately one-quarter of the variance within the data. The beta parameters for implementation (0.402) and contracting and relationship development (0.397) were both positive and significant at 0.05 level. This indicates that implementation activities and contracting and relationship development activities are significantly associated with a higher level of savings as a result of outsourcing. Outsourcing strategy and planning and analysis activities were not significantly related to the level of savings. These results confirm an *a priori* hypothesis of the researchers that emphasis placed on post-contracting activities is positively related to savings achieved through outsourcing.

A similar regression analysis was attempted for regressing “time to savings” (Question 7) on the new process model phases individually to determine if a significant relationship exists between the latent and dependent variables. The model was not significant, and remedial measures did not improve the model. There was no discernible predictive value between the components of the outsourcing process model and the time to savings. In other words, the “time to savings” for outsourcing projects is not related to emphasis placed on any one component of the strategic outsourcing process model.

Analysis 3: How is “goal achievement on performance dimensions” related to the types of goals set? (Question 5)

An EFA was performed on the data from Question 5, the extent to which goals were met for each performance dimension listed. The responses to this question were dependent on the goals that each company had set in the outsourcing process. The first company macro goal (see Figure C.5) shows a balance between cost and capacity. The second company goal was a pure growth- and velocity-focused one. The third company goal was focused on acquiring needed technology and skills externally while reducing capital investments.

FIGURE C.5: CLUSTERING OF GOALS

COMPANY GOAL 1 (COST AND CAPACITY)	RELATIVE DEGREE OF INFLUENCE ON FIRM GOALS
• Reduce operating cost	0.79320
• Turn fixed costs into variable costs	0.69070
• Create additional capacity	0.66702
• Increase flexibility and responsiveness	0.46824
• Focus on core business	0.45783
COMPANY GOAL 2 (GROWTH AND SPEED)	
• Increase speed to market	0.84058
• Grow revenue	0.80124
• Improve quality	0.67551
• Increase flexibility and responsiveness	0.41109
COMPANY GOAL 3 (ACCESS TO SKILLS AND TECHNOLOGY)	
• Gain access to technology not resident in our company	0.83457
• Gain access to needed skills	0.80218
• Reduce capital investment	0.46354

The “cost and capacity” goal explained the 32 percent of the variation in how companies were able to meet goals or goal achievement. Goal 2, growth and speed, and Goal 3, access to skills and technology, explain 11.8 percent and 11.4 percent of the variance, respectively. As before, note that the numbers following each individual item are important and reflect the relative degree of influence on firm goals of the items within each firm goal category listed below.

Analysis 4: Can a company's outsourcing goals predict "level of savings" and "time to savings"?

The dependent variable "time to savings" (Question 7) was regressed on the goals listed in Figure C.5. The model explains approximately 7 percent of the variance within the data. The beta parameter for Goal 1 (-0.274) was negative and significant at 0.01 level. This indicates that a cost-and-capacity-oriented strategy is significantly associated with a faster time to savings as a result of outsourcing. Goal 2, growth and speed, and Goal 3, access to skills and technology, were both insignificant in the model.

The dependent variable "level of savings" (Question 6) was regressed on the goals listed above. The model explains approximately 6 percent of the variance within the data. The beta parameter for Goal 3, access to skills and technology, (0.473) was positive and significant at 0.01 level. This indicates that a strategy of acquiring skills and technology external to the firm and the resultant reduction in capital investments increases the relative level of savings attained through outsourcing. Goal 1 and Goal 2 were both insignificant.

It is interesting to note that the factors that contribute to the "level of savings" and "time to savings" are distinct, indicating that the goals influencing time to savings and level of savings are unique. Additionally, the sign of Goal 2, growth and speed, was negatively related to faster time to savings and to the level of savings. Although the factor was insignificant, it may indicate that a growth and speed strategy may be incompatible with achieving outsourcing goals in the shorter term.

Figure C.6 places these analyses in perspective. Strategic outsourcing to acquire new or better skills and technology from a partner seems to generate greater savings for participating firms. Similarly, strategic outsourcing for the purpose of reducing costs and adding capacity through supplier networks seems to generate faster savings for participating firms. Strategic outsourcing to foster revenue growth and increase speed to market was not correlated significantly with either speed to savings or level of savings. However, this does not mean that outsourcing for revenue growth and increase speed to market would not generate significant competitive advantage in the longer term. The research team believes that the impact of these goals was not captured in our study due to the longer-term nature of the benefits associated with revenue growth and increased speed to market.

FIGURE C.6: CORRELATION OF GOALS WITH SPEED OR LEVEL OF SAVINGS

STRATEGIC OUTSOURCING GOAL	CORRELATION WITH SPEED OF LEVEL OF SAVINGS
SKILLS AND TECHNOLOGY	• Correlation with greater level of savings
COST AND CAPACITY	• Correlation with faster time to savings
GROWTH AND SPEED	• No significant correlation with either speed of level of savings

Analysis 5: Are “level of savings” and “speed to savings” correlated?

The correlation between the two dependent variables time to savings (Question 7) and level of savings (Question 6) was calculated at -0.05766. The test for the correlation being significantly different from zero was not rejected (p-value = 0.55), supporting the idea that the two variables are statistically uncorrelated. This evidence supports the need to treat these variables as independent measures of outsourcing success. They are not sufficiently correlated to form a single latent construct of outsourcing performance. This supports separate regression analysis for these two dependent variables.



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