

Driving High-Performance Outsourcing: Best Practices from the Masters

Executive Survey Results



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"Companies realize that outsourcing is a fairly powerful and effective management tool; it's not just a fad, but part of their business model, which really requires a nuanced approach to setting up and managing those deals and making them work."

Executive Participant Accenture Executive Discussion Forum

When a company approaches outsourcing for the first time, the questions often far outnumber the answers. Several queries from senior executives participating in Accenture Executive Discussion Forums on outsourcing provide a snapshot of the choices and challenges facing newcomers to outsourcing:

- "What timeline can we expect, and what kind of partner do we need?"
- "Which processes should we outsource, and which should we keep?"
- "How do you structure the deal to allow for changes in the business environment over the course of the arrangement?"
- "Can you outsource a business function whose processes are broken, or do you need to fix it first and then outsource?"
- "How does an outsourcing arrangement impact our relationship with unions?"
- "We have projects going all the time; how do you juggle all those projects and introduce outsourcing without the disruption?"

How does a company answer all these questions and get the most from an outsourcing arrangement without going through a painful process of trial and error? One good way is to borrow best practices from the masters — companies that have been outsourcing for several years and have already developed and refined techniques for high-performance outsourcing. A new global cross-industry survey of companies with deep experience constitutes a veritable "how-to" guide for high performance.

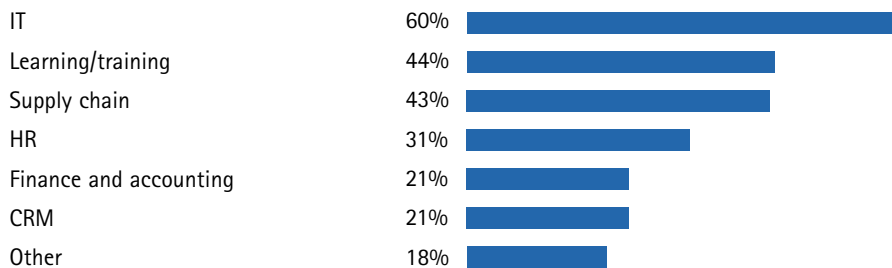
These experienced outsourcers are sophisticated in their approach to managing outsourcing arrangements for maximum business results. Their best practices at times go against conventional wisdom. For example, traditional outsourcing arrangements focus heavily on service level agreements, but

veteran outsourcers build broad business outcomes into their performance measurements from the very beginning, even though cost reductions and service level agreements always remain a high priority.

As a consequence, the vast majority of these experienced outsourcers get better, broader business benefits from outsourcing and are highly satisfied with the results. While some may contend that outsourcing starts with a bang and ends with a whimper, these experienced practitioners demonstrate that when outsourcing is done well, benefits and satisfaction actually increase rather than fade over time.

The survey includes responses from 565 executives working in companies around the world in the automotive, transportation and travel services, retail, consumer goods and services, industrial equipment, and health and life sciences industries. The survey was commissioned by Accenture, which has a broad business expertise in outsourcing and has been a regular sponsor of outsourcing studies over the past decade, and was conducted by the Economist Intelligence Unit. Accenture has worked with many of the world's leading companies in these industry sectors to deliver innovation and drive high performance through outsourcing, and shares with them a deep interest in identifying best practices in high-performance outsourcing. To supplement these statistical findings, Accenture hosted two day-long Executive Discussion Forums in Frankfurt, Germany, in April 2004 and in Chicago, Illinois, US, in May 2004, in which senior executives from a diverse range of companies shared their thoughts and insights on a broad range of issues related to outsourcing.

Figure 1. Functions Outsourced
 Respondents cited IT, learning/training and supply chain as areas most commonly contracted out.



Participating Companies Accenture Executive Discussion Forums

- Acosta Sales and Marketing Company
- Cargill Cerestar BVBA
- Caterpillar, Inc.
- Caterpillar S.A.R.L.
- Delphi
- General Mills
- Kaiser Permanente
- Komatsu America Corp.
- Medicines and Healthcare products Regulatory Agency (MHRA) of Great Britain
- Nestec SA
- Nestlé USA
- Otis GmbH & Co. OHG
- Roundy's, Inc.
- Toys "R" Us, Inc.
- VF Services, Inc.
- Virgin Management

Seeking Out the Voices of Outsourcing Experience: Research Hypothesis and Methodology

Outsourcing as a strategic business tool has been around for well over a decade, long enough for a certain folklore to grow up alongside the facts. Every experienced executive has heard an anecdote about outsourcing deals going badly. Virtually everyone, as a result, can agree that building high-performance outsourcing arrangements calls for an unusually sophisticated blend of skills. Which precise tools are required, and how does one acquire them, except by making the difficult climb up the learning curve? It was to address these questions that a global cross-industry survey of experienced outsourcers was conducted in January and February of 2004.

A logical starting point suggested itself: Experienced outsourcers would know better than most how to manage outsourcing in a different way, and these "experts" may in consequence achieve a different kind of result. The "experienced outsourcer" was defined as an executive working in a company that has had a minimum of two years of outsourcing experience with a business-critical function (see Figure 1 for typical processes outsourced). The survey was a blind study conducted without reference to Accenture as sponsor. Respondents were recruited from the Economist Intelligence Unit's global database and guaranteed absolute confidentiality.



The Respondents

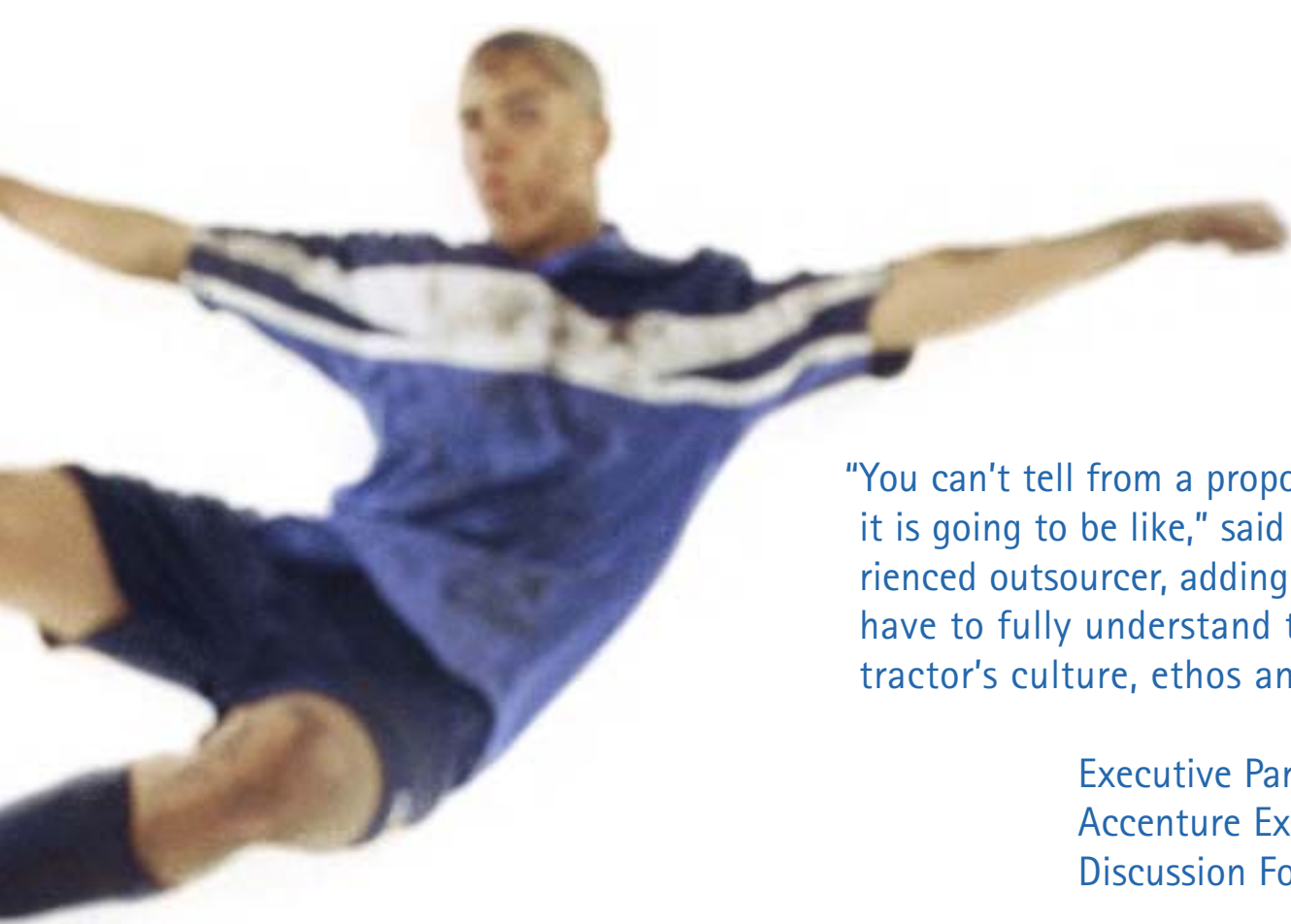
A total of 565 responses were obtained from respondents working in companies that had significant outsourcing experience. Of these, 220 respondents, or 39 percent, worked at companies that were deeply experienced in outsourcing, with seven years or more of outsourcing experience; 61 percent had between two and seven years of outsourcing experience.

Fifty-eight percent of the respondents were C-suite level or functional level executives. Seventy-eight percent of the respondents work in companies with revenues greater than US \$500 million.

Industries surveyed include: automotive, transportation and travel services, retail, consumer goods and services, industrial equipment, and health and life sciences (pharmaceuticals and health plans). Regions surveyed focused primarily on North America, Europe, and Asia Pacific, but did include comparatively small percentages of respondents from various countries outside these regions.

Where Do We Start?

For many companies considering outsourcing, the most challenging questions at times are the most basic ones: Where do we begin? Does a company start with its accounting function, its training programs, human resources, or the call centers in its customer relationship management area? Participants in the Accenture Executive Discussion Forums favored starting with generic, transaction-based and commodity-like business processes such as finance and accounting and information technology, which offer quick wins and attractive returns on relatively low levels of risk.



"You can't tell from a proposal what it is going to be like," said one experienced outsourcer, adding that "you have to fully understand the contractor's culture, ethos and aims."

Executive Participant
Accenture Executive
Discussion Forum

Key Findings: The Longer a Company Outsources, the Better It Becomes and the More Satisfied It Is

The first salient finding from the survey is that the longer a company engages in outsourcing, the better it becomes at the actual managing of outsourcing. This may stand to reason; companies get better at things when they have time to refine their techniques. The second finding is more surprising: The rewards from outsourcing are not front-loaded in "Year One" cost savings, only to decline over time. Experienced outsourcers agree that outsourcing helps their companies perform better, and in overwhelming numbers they report record levels of satisfaction with their outsourcing experience. In fact, performance and satisfaction tend to increase over the long term.

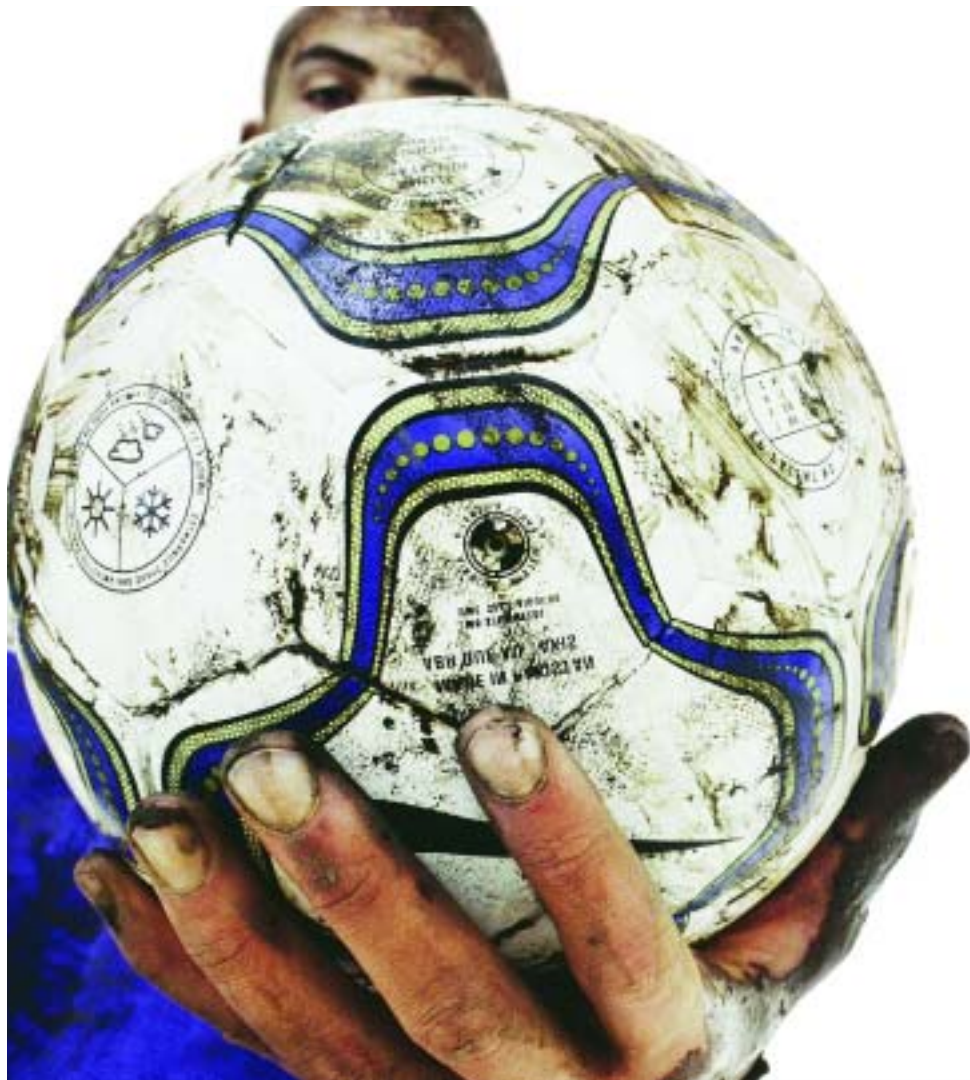
Master Outsourcers Know Better

Experienced outsourcers use a sophisticated approach to manage their complex outsourcing arrangements, enabling them to maximize business performance.

- Almost three quarters (74 percent) of experienced outsourcers use broad "business outcomes" to measure and manage performance. These outcomes invariably include reduced costs and improved profitability, but go beyond to embrace

factors that influence profitability, such as speed to market or market share growth. Veteran outsourcers define what they really want from the outsourcing arrangement at the outset; the vast majority of companies that rely on business outcomes do so from Day One; virtually all introduce them by the third year of an arrangement.

- Companies have a variety of requirements for their outsourcing partners, including process expertise, industry knowledge and many other factors, in addition to attractive pricing. Discussions at Accenture Executive Discussion Forums in Frankfurt and Chicago revealed that many look for continuous cost reduction, which implies continuous process improvement. As one experienced outsourcer at a global consumer goods manufacturer expressed it, "When I tell my superiors that our benchmarks showed that we are in the top 20 percent in our industry, they just tell me, 'Good job, now take your benchmarks and go back to your desk and do better next year.'" While most are looking for upfront cost savings, what companies really expect are continuously declining costs. This simply cannot be achieved by doing today's process the way it is done today. Inevitably, companies are driven to look beyond cost toward deeper process improvements and business transformation.



- Performance measures and the quality of the outsourcing relationship are more important than the contract as primary management tools after three years of outsourcing. Most outsourcing arrangements run for several years, requiring continuing adaptation to changing business conditions on the part of both the company outsourcing and the service provider. As one participant in an Accenture Executive Discussion Forum noted, the element of change means that the majority of outsourcing contracts need to be renegotiated before the end of the contract. This reality suggests that it is wise to accept and plan for the change in advance. Performance measurements and the working relationship between the outsourcing company and its service provider, more so than the contract itself, are the practical tools veterans use to keep their outsourcing arrangements aligned with their changing business conditions.
- A majority (59 percent) use risk/reward incentives to spur high performance from their outsourcing partners. Incentives may be used to reward extraordinary performance or to encourage higher levels of risk. Respondents reported using incentives to spur a range of actions on the part of the service provider, from the making of greater capital investments to the assumption of potentially riskier operational challenges.
- Governance is more sophisticated; 74 percent exercise moderate-to-extensive reliance on governance. Almost three quarters of the companies surveyed (69 percent) have an executive dedicated to the management of the outsourcing relationship.
- Veteran outsourcers focus on three top objectives: reduced costs, improved processes, and the ability to focus on their core business. A large portion of companies meets these objectives.
- The more experienced outsourcers (those with seven or more years of experience) consistently gain more benefits than those with two to seven years of experience.

What Is a Business Outcome?

What does "good" look like to your company? Establishing business outcomes is all about the outsourcing company answering a few critical questions, beginning with "What do I want the provider to optimize?" Is it price or speed or quality or a combination of these? With all the attention in the media devoted to outsourcing in general and offshore outsourcing in particular, participants in Accenture Executive Discussion Forums acknowledged that the two terms were not synonymous, and that geography should never be the fundamental issue. As one participant said, "We should not be asking, 'Should I go to India, or Manila?' The real question is 'Where do I want my asset capability model to be in a few years?'" If companies want a range of services today, and also want an annually reduced cost of service, the only way to do that is to take advantage of increasing scale, wherever this can be found. Outsourcing arrangements should involve partners that give companies the flexibility to follow the evolution of the outsourcing marketplace.

Masters of Outsourcing Get Higher Performance and Greater Satisfaction

Executives unfamiliar with outsourcing may be tempted to believe that the most work and the biggest benefits come in Year One. They are only half right. The first year is always a challenge, but responses from experienced outsourcers tell us that satisfaction starts high and actually increases as the outsourcing arrangement proceeds.

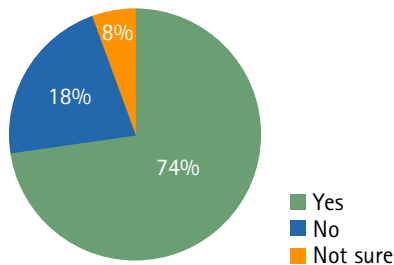
- Sixty-one percent agree that outsourcing helps their companies perform better. For one experienced executive at a global consumer goods company which has already established a shared services center, outsourcing is the only way he can imagine taking his operational performance to the next level: "We have wrung all we can out of productivity on our own; now we need to take the next step."
- Seventy-four percent of all respondents with deep experience in outsourcing are satisfied with the results they achieve in the first year of their arrangement.
- Satisfaction increases as the outsourcing relationship matures; 76 percent are satisfied with results after the first year.

- The longer a company outsources, the more satisfied it becomes. Companies that have been outsourcing more than seven years experience higher satisfaction than those outsourcing two to seven years. This satisfaction increases after the first year.

These satisfaction levels are the highest ever seen in Accenture outsourcing studies. In an earlier survey of outsourcing conducted in August 2003 with a broader sample that included companies with any level of experience in outsourcing, only 46 percent of respondents reported that they were satisfied. The satisfaction difference is presumably due to the experience and better practices employed by the more experienced outsourcers, thereby leading to higher performance and satisfaction.

Figure 2. Respondents using business outcomes to measure the benefits of outsourcing

74% of experienced outsourcers measure outsourcing benefits by looking at broad "business outcomes."



"Business Outcomes" Defined

"Business outcomes" was defined for purposes of the survey as an observable result or change in business performance possibly supported by transaction-based metrics, resulting from an event or action, such as outsourcing. Many outsourcing arrangements feature service level agreements and operating level agreements that codify acceptable levels of performance in the outsourcing arrangement. Most companies presume these minimum requirements will almost always be met. Business outcomes go beyond, defining more valuable business benefits to be gained from the outsourcing initiative. Examples of higher-value business outcomes might be increased speed to market, reduced defects or rework, and lower working capital requirements made possible by higher efficiencies.

The Experts Bring a Seven-Piece Skill Set to the Management of Outsourcing Arrangements

The survey reveals a body of seven "best practices" shared by experienced outsourcers, who grow increasingly more insightful in their ability to govern outsourcing arrangements for maximum performance. Here is how they do it:

1. Build in Broad Business Outcomes Early and Often:

The conventional view is that outsourcing is all about cost reduction. This survey confirms that while savings are a significant driver of outsourcing, experienced outsourcers take a much broader view of the benefits to be gained. Seventy-four percent report that their companies measure and manage outsourcing performance by looking at a range of broad business outcomes (see Figures 2 and 3). Increased profitability tops the list, reflecting the cost-conscious mindset, but significant numbers of respondents also cited other desirable business outcomes. Equally significant, 60 percent of experienced outsourcers build these business outcomes into the arrangement from the beginning, and by the third year, virtually 100 percent of respondents are relying on outcomes. Real-world experiences help put the price issue in its proper context.

2. Hire a Partner, Not Just a Provider: Veteran outsourcers know that hiring an outsourcing service provider is not just a matter of the lowest price quoted or the highest savings promise proffered. Experienced outsourcers demand a lot from their partners, price being only part of the equation along with expertise, flexibility and a spectrum of other assets (see Figure 4). In discussions with senior executives at Accenture Executive Discussion Forums held in the spring of 2004, participants generally acknowledged that the so-called "soft issues" are often harder than the "hard issues" of pricing and contractual terms. "You can't tell from a proposal what it is going to be like," said one experienced outsourcer. "You are not allowed to put down 'act of faith' as a selection criterion. You have to fully understand the contractor's culture, ethos and aims." Another participant itemized the criteria his company used in its selection process: reputation, proven experience in business process outsourcing, excellence in the technology platform to be used; trust and cultural fit with top management; and, finally, price and quality. But he added, "On both deals I have worked on, we did not select the cheapest offer."

3. It's More Than a Contract, It's a Business Relationship:

Contracts are clearly critical for aligning expectations and interdependent responsibilities at the outset of an outsourcing arrangement. Experienced outsourcers suggest that over time, the contract gives way to performance measurements and the relationship between the outsourcer and the service partner as key success factors (see Figure 5). Discussions among American and European executives at Accenture Executive Discussion Forums suggest that most companies follow a proven process in searching for, evaluating and selecting an outsourcing service provider. Initial research is typically followed by a formal Request for Information and then a Request for Proposal, culminating with negotiations, due diligence and then determination of contractual or commercial arrangements. What was clear from all participants, however, is that selecting an outsourcing partner is not your standard procurement exercise. As one participant put it, "I am buying into a journey and a route. I do not know exactly how I am going to get there, but I am confident that I will reach the destination, because of the cultural fit" between his company and the outsourcing service provider he chose.

Figure 3. Business outcome metrics companies use to measure outsourcing performance
Veterans use a spectrum of "big picture" business outcomes to assess outsourcing performance.



Base: Respondents reporting using business outcomes; 418 individuals or 74% of all respondents

Figure 4. Importance of factors in choosing an outsourcing provider

When it comes to selecting an outsourcing partner, the masters look for expertise, flexibility and price.

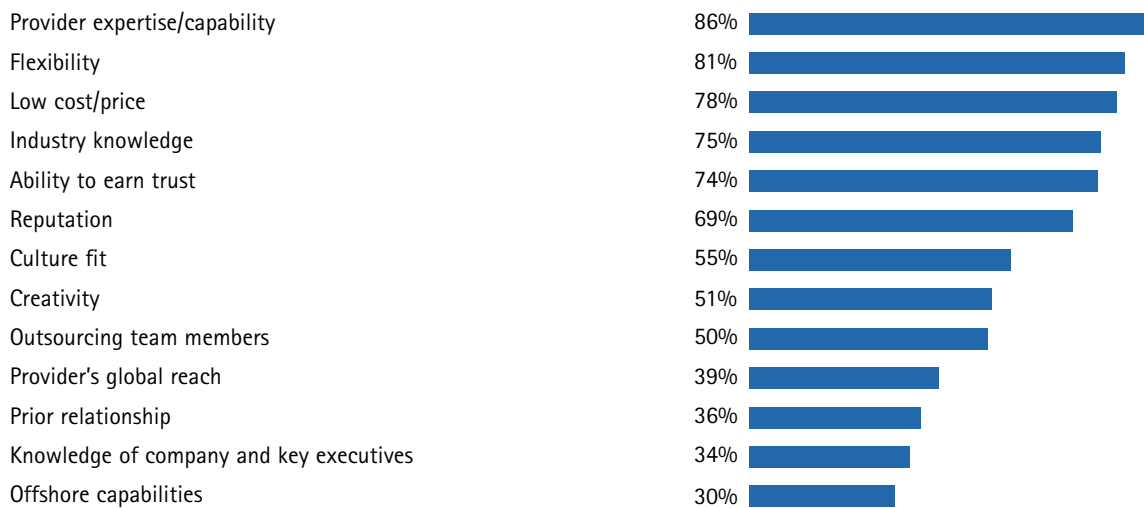
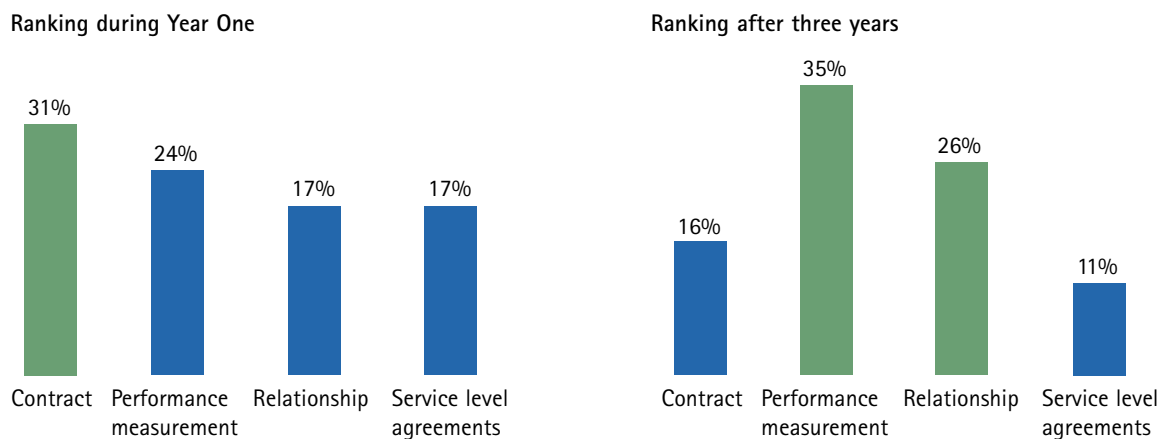


Figure 5. Importance in effectively managing an outsourcing arrangement

Among experienced outsourcers, performance measures and relationships become more useful than the contract for managing arrangements.



What is "Governance"?

In the Accenture Executive Discussion Forums, American and European participants shared a variety of approaches to governance. "Governance" can be defined as the use of formal and informal processes and rules to manage the relationship between organizations. Governance in outsourcing is a term used to describe a wide range of techniques aimed at managing the arrangement over time. Simple examples of governance procedures may be periodic review sessions between the outsourcing company and its service provider, and formally defined escalation procedures in the event of a disagreement. At high levels, governance can embrace annual performance reviews and the setting of strategic directions for the next fiscal year.

4. Leverage Gain-Sharing: Nearly six out of ten respondents (59 percent) working at experienced outsourcing companies report that they use risk/reward incentives to spur the performance of their service partners (see Figure 6). In some cases, these incentives are intended to elicit performance beyond contractually mandated agreements. In other situations, incentives are used as inducements to take on especially challenging corporate chores, such as operating in a groundbreaking endeavor or in a precarious financial environment.

5. Use Active Governance: Experienced outsourcers understand that it is not enough to sign up and hand off; effective outsourcing arrangements require active involvement. Nearly three out of four (74 percent) of respondents say their companies rely on moderate or extensive governance procedures (see Figure 7). More than 90 percent use some form of governance. In the Accenture Executive Discussion Forums, many American and European participants agreed that governing the outsourcing arrangement and managing the relationship between the outsourcing company and the service provider are among the most important, yet sensitive, issues to be addressed. As one experienced outsourcer expressed it, "Governance must work at the very top level all the way down to the operational level. Is everyone talking to everyone at every level?" Open communication is obviously critical; less apparent are the formal governance structures required for success.

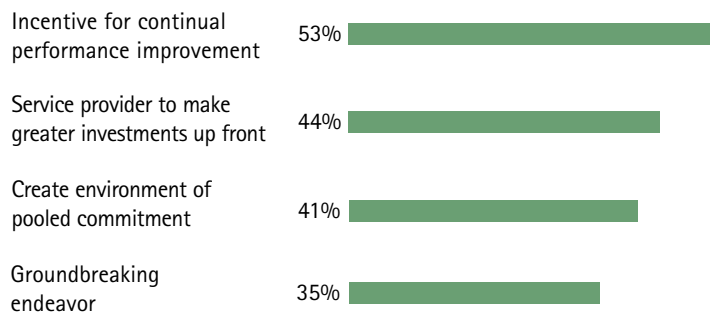
6. Assign a Dedicated Executive: Almost seven out of ten respondents (69 percent) report that their companies have assigned a dedicated executive to the task of supervising their outsourcing arrangement. Outsourcing is a full-time

business proposition requiring focused attention at the management level. For every company, the decision to outsource is only the beginning of the journey. Most arrangements are multi-year deals running to five, seven or even ten years, so the relationship between outsourcing company and service provider depends for its success on the care and nurturing of the arrangement over time. "You need a different skill set for managing an outsourcing relationship," one executive commented at an Accenture Executive Discussion Forum. A proper, coordinated approach to human resources issues is particularly important. Defining new and revised roles in the retained organization, as well as those positions being outsourced, is of paramount importance to all employees. "There is as much worry and uncertainty to the people who remain as for those people who leave the organization," said one participant. Communications strategy becomes a principal task of the executive charged with leading the outsourcing initiative.

7. Focus Relentlessly on Primary Objectives: When asked to rank objectives for the outsourcing arrangement two years into the deal, respondents cite a lengthy "wish list," but three objectives stand out above all others: cost reduction (67 percent), improved processes (48 percent) and focus on the core business (35 percent). Of all those that rank these three at the top of the list, 70 percent report that their companies have been successful in achieving these objectives (see Figure 8). For some companies, failure is not an option. One participant at an Accenture Executive Discussion Forum said, "When my largest competitor's SG&A is at 15 percent and mine is at 24 percent, how am I going to compete? Outsourcing is the only way I am going to make my numbers."

Figure 6. Cases where companies use a shared risk/reward arrangement

Shared risk/reward arrangements help align outsourcing outcomes with corporate objectives and challenges.



Base: Companies using shared risk/reward arrangement; 334 respondents

Figure 7. Reliance on governance to manage an outsourcing relationship

74% of experienced outsourcers rely on the use of moderate-to-extensive governance.

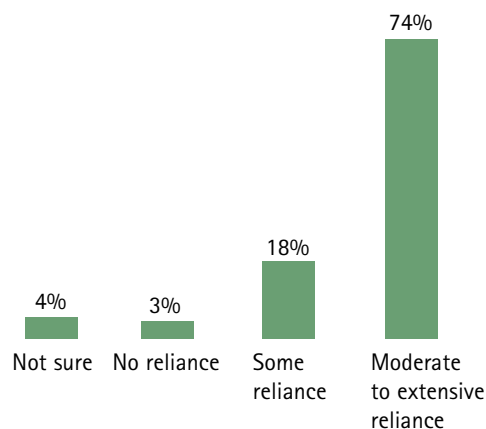
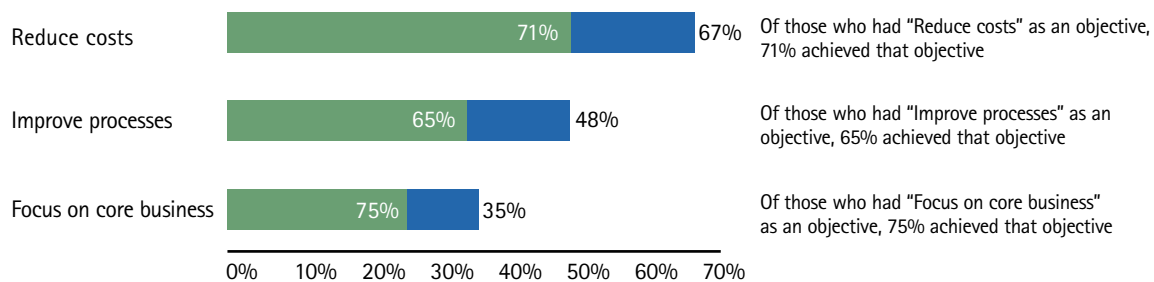


Figure 8. Percentage of respondents reporting objectives for outsourcing/achievement of objective

Of those who share these goals, 70% on average achieve their objectives.



Masters of Outsourcing Leverage Their Skills to Achieve High Performance and Are Highly Satisfied with Their Outsourcing Experience

What do experienced outsourcers get when they apply their skills to the task of maximizing their outsourcing arrangements?

Performance.

Nearly two-thirds of experienced outsourcers report that outsourcing helps their company perform better (see Figure 9). In simple terms, high performance outsourcing contributes to higher performance overall. Whether the improved performance is a function of increased profitability, improved business processes, other factors or a combination of several factors, the majority of experienced outsourcers have clearly seen a performance gain from the decision to outsource.

Consistent with the overall findings from this survey, improved performance is a benefit that increases rather than decreases

over time (see Figure 10). Slightly less than 60 percent of outsourcers with two to seven years of experience report performance gains, a number that jumps to two out of three when outsourcers with seven or more years of experience are queried.

And satisfaction.

Satisfaction with the outsourcing experience would logically go hand-in-hand with performance, and it does. Nearly three-quarters (74 percent) of the respondents report that their companies are satisfied with the outsourcing results they achieve in the first year. Still more (76 percent) are satisfied with the long-term results of outsourcing. Both satisfaction readings are among the highest, if not the absolute highest, levels ever recorded in a survey of this type (see Figure 11).

In fact, the longer a company outsources, the more satisfied it becomes with the results. Companies that have been outsourcing longer than seven years tend to be even more satisfied than those that have been outsourcing between two and seven years (see Figure 12).

Figure 9. Agreement with statement, "Outsourcing has helped my company perform better."
Six out of ten survey respondents (61%) agree: Outsourcing helped my company perform better.

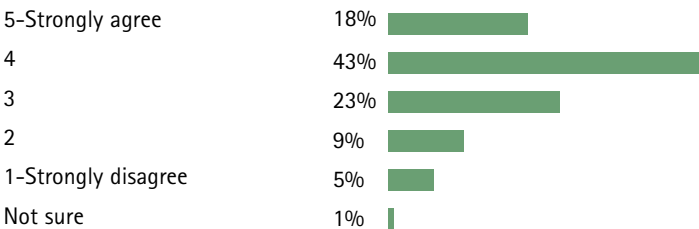


Figure 10. Agreement with statement, "Outsourcing has helped my company perform better."
The longer you do it, the better you get at it: Highly experienced outsourcers tend to get high-performance outsourcing.

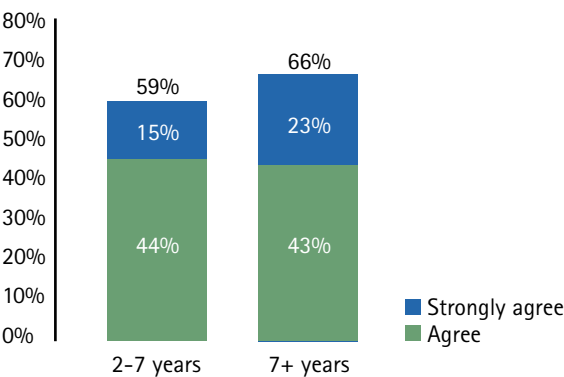
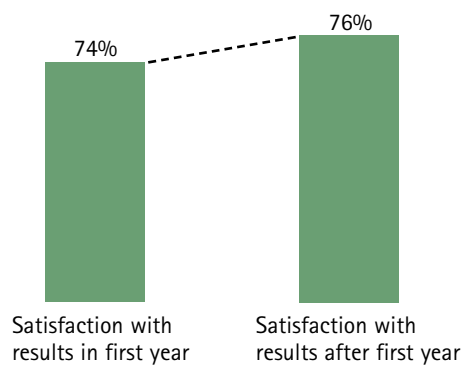


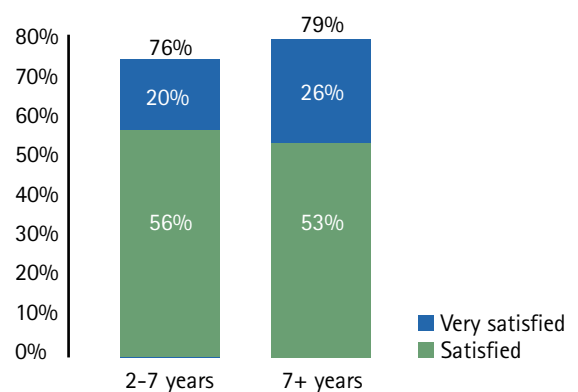


Figure 11. Satisfaction with outsourcing results received
Experienced outsourcers overwhelmingly agree: Satisfaction starts high and, rather than fading, actually grows over time.



Among those who agree with the statement, "Outsourcing has helped my company perform better," 86% are satisfied with the results they receive from outsourcing after the first year.

Figure 12. Satisfaction levels by experience
Experienced outsourcers are the most satisfied and become even more satisfied over time – reporting the highest levels ever seen in surveys of this kind.





"The next time we do it, we will probably sole source. If you are looking for a partnership, you are not going to nickel and dime someone."

Chief Information Officer
Global Consumer Goods
Company

Borrow Best Practices from the Masters — Become a High-Performance Outsourcer

Every outsourcing arrangement is a complex and long-term business relationship. But companies just getting started with outsourcing do not need to wait years to achieve high performance and high satisfaction. And companies already outsourcing should compare their current practices against current best practice. In both instances, there are proven techniques for getting the most out of your outsourcing initiative.

By adopting these sophisticated outsourcing practices, companies can achieve high-performance outsourcing and high levels of satisfaction with the returns they achieve on their outsourcing arrangement.

"We clearly are not best in class, so I ask how do we not just catch up, but leapfrog?"

President
Global Consumer
Products Company

Experienced Outsourcers' Seven Best Practices

- 1. Build in Broad Business Outcomes Early and Often:**
Incorporate business outcomes as a performance measure from the outset of the arrangement.
- 2. Hire a Partner, Not Just a Provider:** Look for an outsourcing provider that brings a wide set of skills and strengths, and a long-term track record of delivering results, in addition to competitive pricing.
- 3. It's More Than a Contract, It's a Business Relationship:**
Give as much attention to performance measurement and the quality of your relationship with your provider as you do to the contract.
- 4. Leverage Gain-Sharing:** Use risk/reward provisions as incentives for higher-performance outsourcing.
- 5. Use Active Governance:** Use active governance to manage the outsourcing relationship for maximum performance.
- 6. Assign a Dedicated Executive:** Task your talented executives with the mission of optimizing your outsourcing arrangements.

- 7. Focus Relentlessly on Primary Objectives:** Be clear about objectives — cost, process improvement and the ability to focus on the core business are the most common among outsourcing veterans.

Outsourcing at Accenture

For more than a decade, Accenture has worked with many of the world's leading companies in travel and transportation services, consumer goods manufacturers and retailers, automotive manufacturers, industrial equipment manufacturers, and life sciences enterprises to deliver innovation and high performance through outsourcing. We provide a comprehensive set of outsourcing offerings, from technology infrastructure to business applications and processes to complete business transformation. Accenture's outsourcing business, with approximately 20,000 people serving more than 450 clients worldwide, helps clients leverage outsourcing to lower costs, improve processes and lift business results.



About Accenture

Accenture is a global management consulting, technology services and outsourcing company. Committed to delivering innovation, Accenture collaborates with its clients to help them become high-performance businesses and governments. With deep industry and business process expertise, broad global resources and a proven track record, Accenture can mobilize the right people, skills, and technologies to help clients improve their performance. With approximately 90,000 people in 48 countries, the company generated net revenues of US\$11.8 billion for the fiscal year ended August 31, 2003. Its home page is www.accenture.com.

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