

NOA Research - value beyond cost



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How can buyers and suppliers bring added value to their outsourcing relationships? The questionnaire that NOA members were provided with was designed to reveal how successful their outsourcing is, where the successes and flaws lie, and what their aspirations for the future are. The aim was to ascertain not just how important added value is, but what those involved in the outsourcing marketplace are doing to make it work.

It is well known that the best outsourcing relationships are founded on aligned goals and expectations. Hence why another key objective of the research was to find sympathies and disconnects among buyer and supplier attitudes: buyers were asked their view, and suppliers were asked what they thought their customers are thinking, both in terms of their current picture and their plans for the future.

This report documents the results. It provides a comprehensive picture of the outsourcing industry's state, where it's likely to go and what changes are necessary. The analysis should serve to provoke further thought and discussion regarding the report's findings.

Enjoy!

Executive Summary

Creation of added value is moving to central importance in terms of delighting outsourcing clients. As contemporary buyers leave behind the old school 'your mess for less' attitude and demand much more from their partners, the National Outsourcing Association and Polaris conducted a poll to delve into the key influencers, indicators and drivers of added value in outsourcing.

The results were highly encouraging. It is clear that the vast majority of those who participate in outsourcing are convinced of its value, with a significant percentage of buyers certain that there is more value to outsourcing than simply cost-cutting. Despite this, many buyers are not confident in their ability to assess how well their partners are performing, which is highly surprising in this age of data analytics and performance tracking. Buyers are also suspicious when their suppliers offer 'innovation'; the ability to innovate is always desirable, but there appears to be ongoing confusion between buyers and suppliers

over what innovation actually is.

Buyers and suppliers unsurprisingly agreed that a strong relationship founded on trust is a vital component in good outsourcing. However, a strong outsourcing relationship requires aligned beliefs and objectives. While buyers and suppliers were aligned on value-adding activities, commercial constructs and reasons for outsourcing, there's discord between the two parties regarding performance assessment, delivering value, sharing risk, cost-reduction and more. Suppliers are often guilty of adopting a more 'rose-tinted' perspective than their buyers.

Nevertheless, the future looks positive for both sides, with the majority of buyers expecting to expand their outsourcing over the next five years. This may be connected to the rise of outcome-based contracts, which should allow both buyers and suppliers to attain more certainty regarding the success of their outsourcing activities.

Key Findings

- 92% of buy-side professionals agree that outsourcing delivers business value, with 61% strongly agreeing. 81% believe that engaging outsourcing suppliers has made their company more competitive (56% strongly)
- Over a third of buyers (36%) turn to outsourcing providers primarily to improve services
- There is a misconception on priorities in performance assessment, with significant dissonance on the importance of indicators of success:
 - For buyers, the most pertinent factor is increasing productivity/outputs
 - 47% of buyers listed this as their #1 indicator, and 32% as their second
 - Just 23% of suppliers are aware that buyers use increased outputs as the key barometer of outsourcing success (suppliers only rank increased productivity as the fifth most important indicator)
- Confidence in assessing performance is not optimised:
 - 83% of buy-side outsourcing functions claim to be confident in assessing how well their partners are performing
 - However, just 4% of buyers profess absolute unequivocal confidence in doing so
- There is a general trend for suppliers believing things to be going better than their buyers do: on average, suppliers perceive clients to be benefiting 9% more than clients themselves believe they are
- A significant disconnect exists over the use of performance targets for business outcomes as a risk sharing measure:
 - 63% (roughly 2 in 3) of suppliers state that business outcomes feature as part of the deal
 - But just 1 in 4 buyers claim that such measures are in use
- The most popular way for buyers to design a contract is around outputs: 47% of deals are currently structured this way.
- Over the next three years, buying outputs could be usurped by outcome-based contracts:
 - 34% of buyers are using them frequently
 - 36% are planning to use them more
 - By 2017 the majority of new contracts could be constructed around business outcomes
- The topic of “innovation” does not currently appear to be delighting buyers - “innovation” is running at a “success perception” deficit of 31%
- Just 14% of buyers rate innovation labs as a useful investment into an outsourcing relationship
- Financial rewards for success are built into less than half of contracts: 39% of buyers and 45% of suppliers reporting that such incentives are locked in to their deals
- The future looks positive for outsourcing as the majority of buyers plan to increase the scope of their outsourcing (59%),

with just 7.8% considering scaling back activity

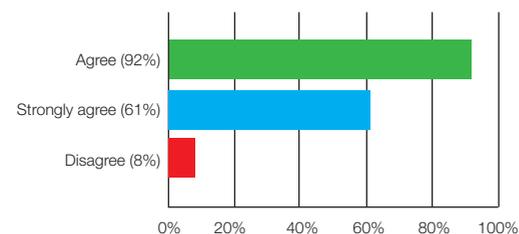
Objectives and Methodology

Partnering with Polaris, the NOA surveyed 158 of its members with a detailed questionnaire designed to illicit expert opinion on matters such as commercial constructs, performance measurement, and governance and risk sharing techniques. Each participant was asked to clarify whether they are a buyer or supplier of outsourcing, which sector they operate in and how many years of outsourcing experience they have. From there, buyers and suppliers answered two separate lists of 14 questions: buyer questions focused on what their partners are providing them with, while suppliers were quizzed on what they thought their buyers are receiving and what they are expecting. The survey sample consisted of many highly experienced professionals, with 71% of buyers and 74% of suppliers having more than 5 years’ experience in outsourcing. Roughly one third (35%) of buyers surveyed have more than 10 years’ service, compared to 56% of suppliers.

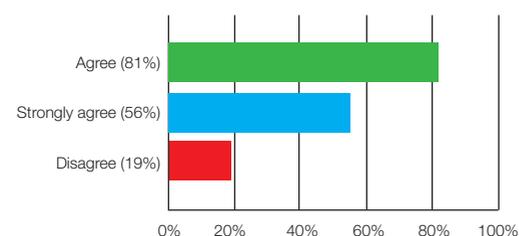
Part One: How Effective Is Your Outsourcing?

Outsourcing Delivers Value and Boosts Competitive Edge

Outsourcing delivers business value (Buyers)



Using outsourcing suppliers makes our company more competitive (Buyers)

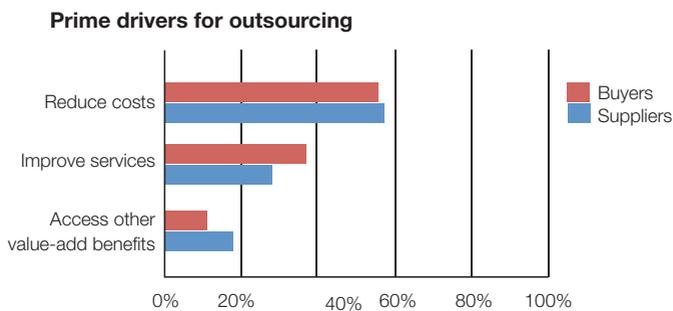


A landslide majority of buy-side professionals, 92%, agree that outsourcing delivers business value. 61% of these members strongly agree.

81% believe that working with outsourcing suppliers has made their company more competitive, with 56% agreeing strongly.

Although most buyers are happy, there remains a 31% gap in perceptions of “value” and “great value,” and a 25% gap in terms of how much of a competitive boost outsourcing brings.

Concurrent Cost Cutting and Service Improvement is Becoming the New Normal



Only 54% of buyers state that reducing costs is their number one driver. 36% of buyers now choose outsourcing primarily to improve their services.

The supplier view is similar: 56% of suppliers reason that their buyers are mainly looking to cut costs on their bottom line, but 27% consider their clients to be mainly choosing outsourcing for the purpose of improving services.

So it would seem that, while buyers certainly want it better, they still want it cheaper too...and who can blame them?

17% of suppliers believe they are being selected for benefits such as cutting edge technology, better talent and processes etc., compared to 11% of buyers citing this reason.

It could be argued that clients are more interested in end results than the alchemy that goes into achieving them, which is a sign of a progressive industry where trust in suppliers is growing.

How is Performance and Value Assessed?

Buyers and suppliers were asked to rank their top 3 measures for evaluating outsourcing performance, where 1 indicated their most used measure.

Most Used

	Buyers	Suppliers	
Increased outputs	1.74	1.66	Cost reduction
Customer surveys	1.88	1.97	Customer surveys
Cost reduction	1.90	2.09	Improved outcomes
Staff/user surveys	2.08	2.09	Decreased inputs
Improved outcomes	2.22	2.21	Increased outputs
Decreased inputs	2.30	2.28	Staff/user surveys

The first significant dissonance in the survey comes in the form of incorrect assumptions of how buyers like to evaluate an outsourcing deal's performance.

For buyers, the most pertinent factor is an increase in

productivity/outputs - 47% of buyers listed this as their #1 indicator, and 32% as their second.

Suppliers only ranked "increased outputs" as the fifth most important indicator, with just 23% of suppliers aware that buyers use it as the key barometer of outsourcing success.

Cost reduction remains an important metric. 56% of suppliers suppose it is the #1 KPI, compared to just 24% of buyers.

Buyer and supplier returns were almost identical on the topic of customer surveys, highlighting a 360° awareness of the role outsourcing plays in delighting consumers/ultimate end users.

These statistics all point towards a buy-side culture of quality over cost, but the difference of opinion in the vitality of increased outputs needs to be addressed.

Reductions in inputs, improved outputs and positive staff user surveys are all important to buyers, but none more so than the boost to productivity once the outsourcing deal beds in.

A smaller survey, conducted during a plenary session at the NOA Symposium 2014, posed this question to the audience:

Service improvement is a top priority for both buyers and suppliers. What do you think is the main inhibitor to this?

43% of attendees answered that contracts are structured around headcount rather than service

30% blamed the lack of simple methodology to measure service improvement

15% called for higher levels of expertise

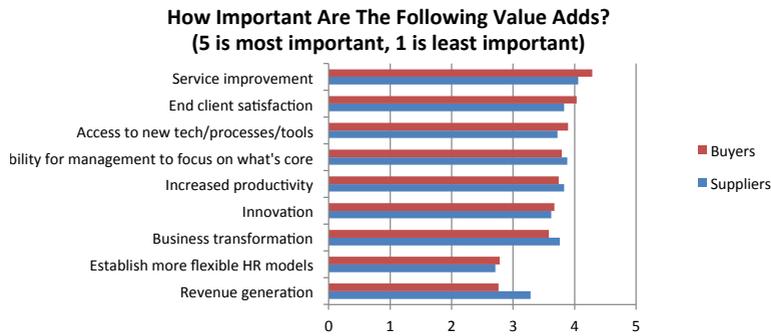
12% said that it is not in suppliers' interest as it may reduce business volumes

Confidence Levels in Assessing Performance

83% of buy-side outsourcing functions claim to be confident in assessing how well their partners are performing, but a mere 4% profess absolute unequivocal confidence in doing so. 1% of buyers are really unconfident, with a further 16% admitting that their confidence levels in performance assessment are less than desired.

From a supplier perspective, 88.5% are confident their efforts are being accurately appraised, with just 3.8% suggesting that their clients are not confident in their own ability to measure suppliers' performance.

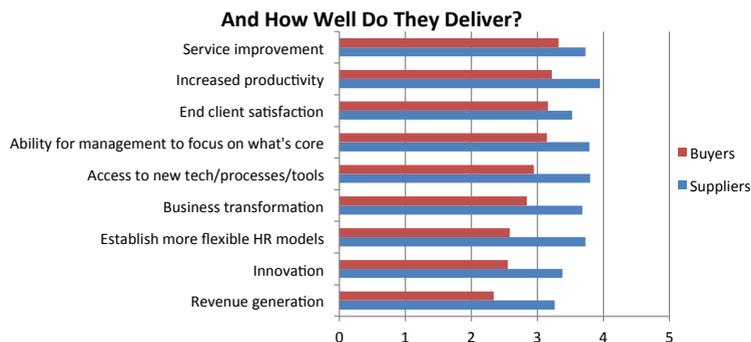
Ranking the Value Adders



There is much agreement on the most important value-adding activities: service improvements, increased ability for management to focus on core activities, better productivity and heightened end-client satisfaction are considered absolutely vital on both sides of the deal and make up the lion's share of both top five rankings.

At the other end of the scale, revenue generation and establishing flexible HR models are not considered among the most important desirables, with only 50% of buyers citing them as important.

One difference of opinion concerns the amount of revenue generation clients expect their partners to create: suppliers suppose revenue generation to be 10% more important than it actually is to clients.



The data highlights perception gaps in terms of how important a value-add benefit is, and how well it had delivered benefits.

For example, service improvement is weighted with an importance of 4.29/5 for buyers. Its average delivery of business benefits rating of 3.32 indicates a 22.6% success perception deficit, i.e. it is delivering, but not in line with how important it is.

For buyers, all listed benefits were in success perception deficit, with an average of 17.8%. The worst offender was "innovation," recording a 31% success perception deficit.

Another perception gap is the general trend for suppliers believing things to be going better than their buyers do. On average, suppliers perceive clients to be benefiting 9% more than clients themselves believe they are.

Midterm Conclusions

Outsourcing is widely perceived to be delivering business value, but three main issues present themselves:

1) There is a misconception on priorities in performance assessment

Buyers value productivity increases above all other KPIs. However, for suppliers, increased productivity is some way down the list, with only 23% of suppliers reporting their awareness that buyers use this as the #1 barometer of outsourcing success.

Buyers and suppliers should work together towards aligned governance procedures that account equally for all stakeholders' needs. This would go some way to addressing the aforementioned success perception gaps, currently running around -19%.

2) Confidence on assessing performance is not optimised

With only 4% of buyers citing absolute confidence in their ability to judge a supplier's efforts, building confidence levels in knowing how well outsourcing partners are performing would be desirable for the industry as a whole: the best governance schedules take out the gut feel aspect of decision-making and actually measure the relationship. This is what it takes to be in the 4%, and spreading this best practice is a key priority for the NOA.

3) There seems to be a general miscommunication as to how well things are going

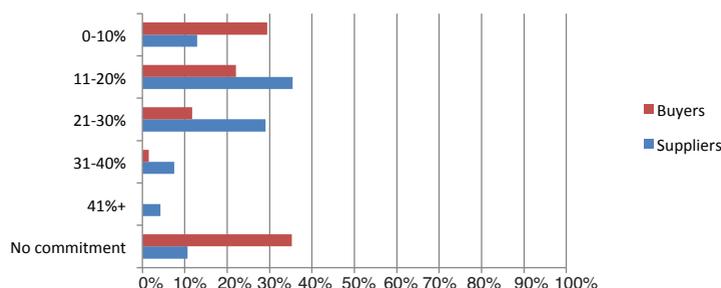
For buyers, all key value-adding benefits were in success perception deficit, i.e. delivering, but not in line with how desirable they are. The same was not the case for suppliers, who thought increased levels of productivity, access to new technologies/processes/tools and establishing more flexible HR models were all delivering above expectation.

These three findings - plus the general trend for suppliers believing things are going 9% better than the situation clients describe - highlight the need for more transparency in performance appraisals, perhaps with a rethink of the metrics being assessed, in order to build widespread confidence in performance tracking.

Part Two: Making Outsourcing Work

Committing to Better Productivity

What Productivity Improvements Are Being Committed To?



Over one in five buyers (22%) have been promised between 11-20% productivity improvements. Around 1 in 3 is expecting a boost of up to 10%; an ambitious 1.5% are expecting a 31-40% hike in productivity.

1 in 3 suppliers believe their clients have been promised between 21-30% better productivity, while only around 1 in 10 buyers think that this is the case.

When considering cases of no expected improvements at all, 1 in 3 buyers have not been promised improvements, while only 10% of suppliers report there being no expected commitment to enhanced productivity.

Customers' views are usually based on what is actually contracted for, whereas suppliers' views represent their capability deliver. When drawing these intentions into a contract, proposed improvements tend to be toned down due to the customers' appetite for internal change, adaptations to new processes and tools, and also their willingness to switch from staff augmentation to outcome-based models.

It should also be mentioned that many contracts focus purely on cost reduction and prioritise reduced staffing levels over productivity. These deals can only ever commit to agreed price rates, because they lack the maturity to measure and improve productivity.

Another small survey conducted during a plenary session at the NOA Symposium 2014 posed this question to the seated audience:

Buyers believe that suppliers are not committing to productivity improvements. Why?

11% of attendees thought buyers are not really insisting upon them.

34% said buyer expectations are too high, without even knowing current levels.

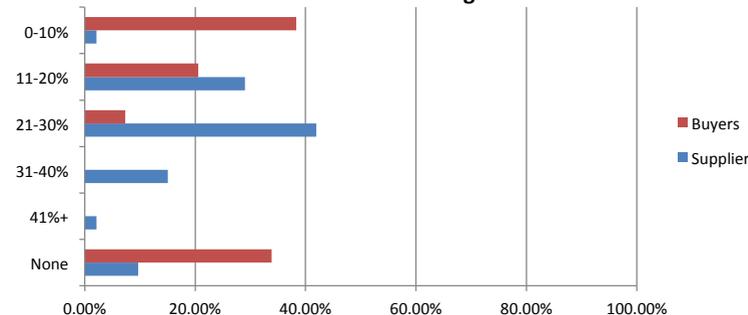
25% claimed suppliers need real expertise to deliver, hence they hesitate to commit.

21% believed suppliers are showing willingness to commit but make it too difficult to implement.

8% thought none of the above.

Committing to Lower Costs

What Cost Reductions Are Being Committed To?



Suppliers appear to be offering more cost reductions than buyers believe are on offer.

38% of buyers are expecting up to 10% cost reduction, which was the most popular answer.

The second most common return was no commitment at all, which around 34% of buyers are expecting. No buyers are expecting cost cutting of 30+%, but 17% of suppliers declare they are offering such reductions.

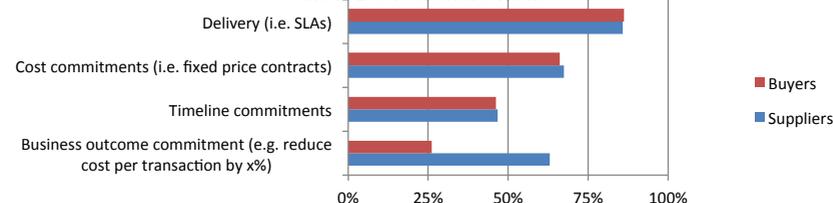
42% of suppliers claim to be offering 21-30% cost reductions. Less than 1 in 10 confess that they have no immediate plans to reduce their clients' costs.

Suppliers are committing to cost reductions and productivity improvements simultaneously. Both elements are linked to an extent, e.g. where process efficiency or automation leads to lower headcounts.

At the same time, as service providers bear much of the investment and risk of internal process improvements that generate productivity benefits, situations where not all of advantages can be passed on to the client are not uncommon.

How Is Risk Shared?

How Do You Share Risk?



Almost exactly an equal number of suppliers and buyers reported heavy usage of risk sharing via delivery metrics such as SLAs and cost commitments.

Timeline commitments are used in less than half of deals (46%).

14% of deals appear not use SLAs - or at least not with particular rewards or penalties attached.

One major disconnect is over the use of targets on certain business outcomes as a risk sharing measure.

63% of suppliers state that business outcomes feature as

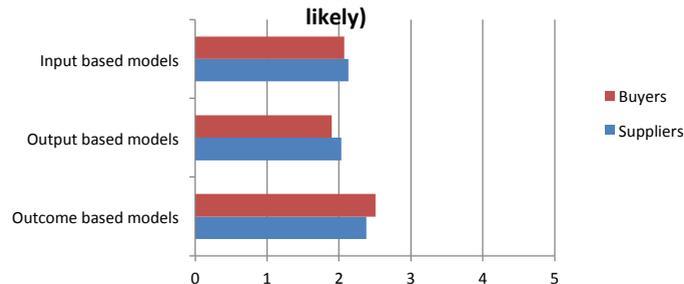
part of the deal (roughly 2 in 3) - but just 1 in 4 buyers claim that such measures are in use.

Buyers seem to perceive higher risk attached to the use of outcome-based contracts. There is the belief that outcome contracts demand much more work on their part, and have a tendency to require restructuring relatively soon.

The majority of customers are currently more comfortable buying capacity or staff augmentation models because they easy to measure and control.

What Commercial Models Are Used?

Which Commercial Constructs Do You Plan To Use Over The Next 3 Years? (5 being the most likely, 1 is least likely)



	Use frequently	Use infrequently	Never use	Plan to use more	Average
Input Based Models	26.47%	47.06%	19.12%	7.35%	2.07
Output-based Models	47.06%	30.88%	7.35%	14.71%	1.9
Outcome-based Models	33.82%	17.65%	11.76%	36.76%	2.51

Suppliers

	Use frequently	Use infrequently	Never use	Plan to use more	Average
Input Based Models	29.03%	38.71%	22.58%	9.68%	2.13
Output-based Models	46.24%	25.81%	6.45%	21.51%	2.03
Outcome-based Models	37.63%	22.58%	4.30%	35.48%	2.38

The most popular way for buyers to design a contract is around outputs.

47% of deals are currently structured this way. But over the next three years, buying outputs could be usurped: 34% of buyers are using outcome-based contracts frequently with 36% planning to use them more.

By 2017 the majority of new contracts could be constructed around business outcomes.

Currently, just 4% of suppliers never use outcome-based contracts, compared to 11% of buyers.

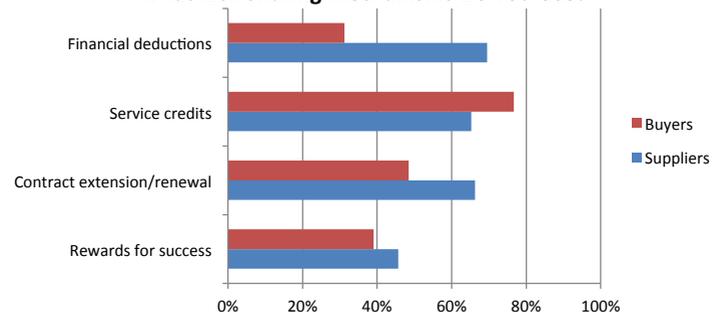
Many contracts are built around outputs: tickets solved, transactions processed, email boxes monitored etc. i.e. a clearly measurable unit of work, rather than a business outcome.

But sometimes with output contracts, a customer can suffer paying heavily for less value, for example, a high number of tickets processed at a lower service quality would cost more, thus rewarding undesirable behaviours.

The NOA has long been an advocate of outcome-based contracts: the most certain thing in business is change, and if your contracts are focused on the ultimate end goal, it'll mean they're much more likely to stay relevant. This way clients avoid having to renegotiate on small details that only matter because of the way deals were set up in the first place.

What Risk Sharing Mechanisms are Used?

What Risk Sharing Mechanisms Do You Use?



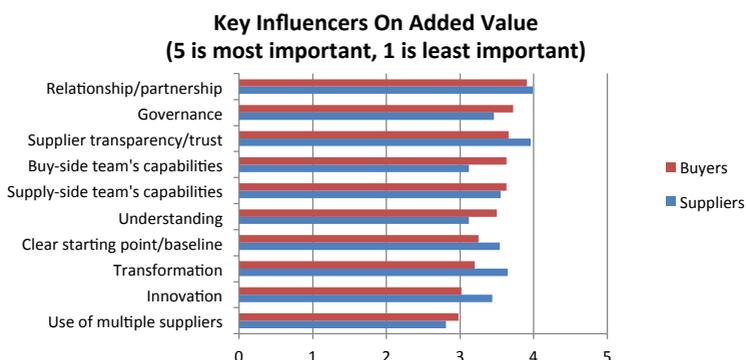
Only 1 in 3 buyers believe that they are sharing risk by applying financial deductions, compared to almost 70% of suppliers. 13% more suppliers believe that the re-awarding of the contract remains at stake (66%) than buy-side professionals suggest (49%).

Financial rewards for success are built into less than half of contracts, with 39% of buyers and 45% of suppliers reporting that such incentives are built into their deals.

If buyers are applying financial deductions, they should be very careful in a multisourced scenario. Creating a collaborative mentality of cross-vendor teamwork that promotes succeeding or failing together is essential. Risk figures and targets should be matched when vendors are working on the same outcome; this means all parties sign up to lose fees for not meeting targets, irrespective of who is responsible.

The same targets should be interlinked with buy-side appraisals: if vendors lose part of the fees, performance bonuses of customers' internal staff should be affected too.

Ranking the Influencers on Added Value



The variegated factors affecting a deal's value-adding performance were ranked, collated and expressed as a % influence factor. The top ranking influencers on added value are similar on both sides.

“Relationships/Partnership” and “Supplier Transparency/Trust” are in both sides’ top three, with a minor dispute over whether good governance (buyer view) or aggressive transformation (supplier view) will add more value.

Interestingly, good governance does not make the suppliers top five. It seems suppliers would rather be trusted than governed.

Buy-side skills are something that buyers and suppliers value equally, with around 70% of both returning that strong buy-side outsourcing skills are a must for making a deal a success.

The stats clearly show that, whilst usually considered hot topics, innovation and multisourcing are seen as low priority compared to the core facets of relationship building.

In fact, the figures seem to show that multisourcing can actually distract from added value - 41% of buyers and 45% of suppliers did not return that they thought multisourcing was important from a value-adding perspective.

Polaris and the NOA agree that influencers can be grouped into three levels of criticality: trust and transparency right from inception are vital to building a relationship that can work through the inevitable day-to-day issues.

To push for ultimate value in the relationship, customers need strong buy-side capability, deep understanding and robust, intelligent governance. Equally crucial are a clear starting point/baseline and suppliers’ people skills: without these, buyers won’t know success when they see it, and if they do glimpse success, won’t actually feel the warm glow of satisfaction.

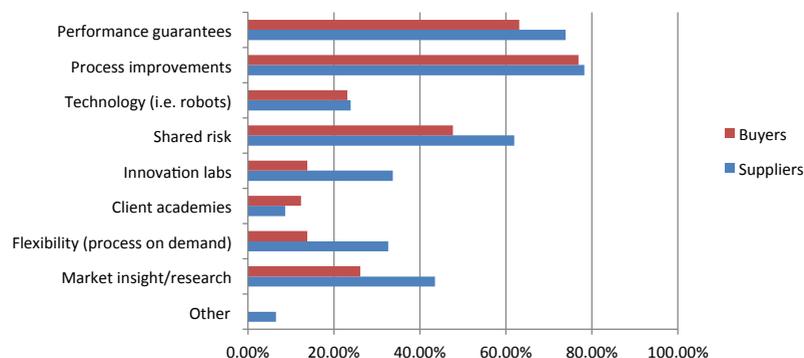
Buyers also need processes in place to track on-going progress. It’s essential to have a high-definition picture of the situation from the very start. Once the contract begins, baselines, scope and management all change, gradually followed by timetables.

To monitor the value of outsourcing throughout all these

inevitable adaptations, maintain a clear dataset that tracks service levels, volumes and costs, alongside other key benefits such as customer satisfaction.

Investments into the Relationship

What Are The Most Valued Investments Into The Relationship?



Buyers and sellers agree that meeting performance guarantees and bringing about process improvements are the cornerstones of a happy relationship.

The stand-out figures in this dataset point towards what is not valued in a relationship. When asked to rate the importance of innovation labs, just 14% of buyers valued them (compared with 33% of suppliers).

Process-on-demand generated an equally underwhelming response - just 14% of buyers state that they make use of flexible services.

Robots only feature in the plans of around 23% of all respondents.

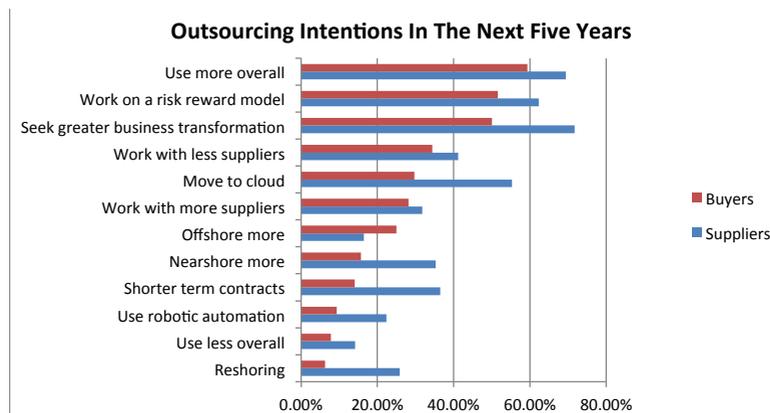
The one relationship investment that suppliers perceive to be even less useful than clients do is ‘client academies’: just 1 in 10 suppliers’ believed their clients value them, compared to 12% of buy-side professionals.

Customers do not currently believe that innovation labs offer added value. This is a problem for suppliers as it may show buyers have a low appetite for innovation, or perhaps they do not trust their suppliers’ capability to innovate.

As many contracts are structured around staff capacity rather than outcomes, it is not hard to see why process-on-demand isn’t widespread, but as more and more contracts move over to outcome models, expect to see process-on-demand accelerate in popularity.

Part Three: Outsourcing Aspirations for the Future

The Future Intentions of Outsourcers



The majority of buyers plan to increase the scope of their outsourcing (59%), while just 7.8% are considering scaling back activity.

Half of buyers are seeking greater business transformation but suppliers are expecting even more transformation, with 72% of them suggesting clients will ramp up efforts to transform. Attitudes to offshoring may come as a slight surprise: 1 in 4 buyers are planning to offshore more, and only 6% are seriously considering re-shoring.

Suppliers, however, think that three-quarters of their clients are keen to re-shore.

Only 29% buyers are currently planning to move to cloud, but suppliers think that over half (55%) are considering such a move.

The feeling that multi-sourcing isn't an essential driver of added value could be represented by the number of buyers, just 28%, who are planning to work with more suppliers.

But as just 34% are planning to work with less suppliers, the figures could indicate that most buy-side outsourcing functions feel that their current blend of suppliers is working well.

There are many more suppliers under the impression that clients will push for shorter term contracts (36%) than there are buyers with a mind to do so. Just 14% of clients are planning to initiate shorter term contracts over the next three years.

Conclusions

The Future Appears Bright

60% of outsourcing buyers plan to use outsourcing more in the next five years: the outsourcing industry will continue to grow, as existing buyers increase the scope of the work they send out. It is expected that suppliers would appear more enthusiastic about the results being delivered than clients; despite this, the survey clearly elucidates how the vast majority

of outsourcing arrangements deliver solid business value, with most outsourcing buyers satisfied that outsourcing improved the competitiveness of their business. But expectation is running high, as the majority of suppliers are committing to concurrent productivity improvements and lower bills for clients.

Outcome-based Contracts Will Catch On, Eventually

Outcome-based contracts will increase in popularity, although traditional output-based contracts with SLAs and cost commitments are still commonplace. There does appear to be some confusion around outcome-based contracts and risk sharing: nearly triple the amount of suppliers purport that risk is shared via outcome-based contracts than the amount of buyers who state that they operate with such models.

Performance Tracking Needs Improving

There are also some issues around performance tracking, with major dissonance around the importance of key indicators such as productivity. As improvements are being widely promised, there needs to be redoubled effort at every turn when it comes to tracking these productivity improvements and their residual benefits.

Relationships and Skills before Innovation

While there is slight buyer/supplier dissonance around how to make relationships work optimally, it appears that a greater emphasis on people and relationship skills would go some way to aligning perceptions of collaborative success.

Relationships are the most valued contributor to positive performance: their importance is lauded by buyers and suppliers equally. Investing in the relationship is vital, but so is making the right investments. Popular initiatives like client academies and innovation labs are not as well received as their organisers would hope; maybe there is a need to reinvent these activities, as well as to track them and celebrating any value they create.

Innovation does not currently appear to be delighting buyers - the success perception deficit of 31% and the disdain for innovation labs point towards this. Buyers and suppliers need to work together to foster innovation at appropriate levels, to avoid a slowdown in terms of generating competitive advantage in the client's business.

Above all else, getting the basics right, such as building relationships and developing quality intelligent governance are lauded as the cornerstones of creating added value in an outsourcing relationship.