

In Search of the Holy Grail

Innovation Through Sourcing

By Mark Mayo, TPI

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Sourcing relationships begin with a tremendous amount of excitement, energy, and high expectations. The parties have just completed an intense, protracted, sourcing process through which they defined the mutual expectations of the contractual association and developed the foundation of the ongoing relationship. The client is generally expecting lower costs, improved service delivery, and continuous innovation derived from a long-term commitment to one of the industry's leading service delivery organizations. The service

provider, excited to be finished with the long hunt and flushed with the thrill of success, is anxious to establish a relationship with the client that will last for eons. The common denominator is the focus on a relationship.

Fast forward three to five years, and there are far too many instances where neither party is satisfied. Our experience reveals that clients typically feel they're receiving lower costs than would have been otherwise possible had their outsourced functions remained in-house. On that score, the merits of outsourcing generally hold high marks. However, the story is mixed on improved service delivery. Some clients recognize the inherent thresholds embodied by contractual service levels, while others view those metrics as guideposts around a broader service quality theme. A critical determinant on service quality satisfaction seems to be the effectiveness of the client's governance organization to establish and manage the expectation of its business operations.

While the topic of quality is decidedly mixed, the one consistent theme we hear is that the clients feel they're not receiving the innovation that they viewed as part of the bargain. In our experience, most outsourcing deals are justified internally as providing a channel through which an industry-leading service provider is motivated to deliver differentiating capabilities over the life of the agreement—something that an in-house organization is challenged to do. Yet, in execution, many times the service providers will agree that they're falling short of client expectations in the areas of innovation but will point out that the primary focus of the relationship is on lowering costs and maintaining high-quality service delivery.

Who's right? As usual, there are two sides to every story, and both have value. It would be easy to go down the path of identifying the extensive hurdles preventing innovation in these relationships. Instead, let's determine how to facilitate innovation through sourcing by first defining what we mean by innovation, and then examining the common attributes of sourcing relationships that *have* produced significant innovation.

Innovation for innovation's sake is meaningless. Clients are looking to service providers for their economies of scale, centers of subject matter expertise, broad market knowledge of best in class practices, tools and methodologies, as well as the resulting solutions that improve service delivery, lower costs, and, most important, *deliver significant impact and value to their business*.

And to be clear, we're talking about ongoing innovation delivered throughout the contract—not innovation introduced when a service provider responds to a one-time event such as contract term expiration—and then introduces significant innovation as part of a contract renegotiation or re-compete. >>



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There are six key attributes we typically see in relationships that have delivered innovation with significant client business impact. They are as follows:

Strategic Alignment on Innovation

Both parties have innovation high on their strategic agenda, and it's part of their ongoing daily dialogue and priorities, as opposed to being an issue they revisit once a year. Typically, the direction is established by the client, through communications to the service provider and throughout the client organization. The service

provider leadership rises to the challenge and drives this agenda throughout its organization as well. Partnership is an overused and ill-understood term but probably the most appropriate one for these relationships in this aspect. Both organizations, the client and the service provider, are focused on delivering significant business impact for the client as part of one team.

It's worth noting that the widely accepted multisourced service provider model of today was enabled by the increased sophistication of client governance organizations and the vast proliferation of service provider alternatives driven by companies out of India and other countries across the globe. This multisourced model provides at least two major disruptive changes to the traditional sourcing model of the '90s. First, clients have substantially more alternatives to receive the business value enhancing services they desire. Second, service providers are experiencing much stronger continual competitive pressure, driving the successful ones to excel in all areas, including delivering ongoing innovation. Over time, this will minimize the ability for service providers to become complacent with the status quo.

Stable Service Delivery Environment

The attention devoted to accounts with service delivery problems tends to be focused on fixing those deficiencies—and not on identifying and bringing new innovation to the client. In most cases, this is more true for the service provider

than the client, but the practical result is the same: no innovation.

As an industry, we must move toward more standard solutions rather than unique client-driven approaches. While we've touted this for years, the industry has not generally delivered on it. The one-to-many model versus a one-to-one approach will enable service providers to deliver more stable and reliable service at a lower price point. It requires clients to be willing to accept standard approaches and outputs.

Fair Economic Bargain

It takes energy, resources, and focus to create innovation, and it's not free. Service providers aren't charities, and each account has quarterly and annual commitments to its company. Service provider accounts struggling to meet these on an ongoing basis typically don't have the ability to dedicate the time and resources to better understand the client's future needs and to leverage their corporate strengths for the betterment of their client's business. They tend to fall in the rut of just "answering the mail" by focusing on their day-to-day contractual obligations. On the other hand, clients that feel they're overpaying for services tend to not approach the relationship in a constructive manner. Here, a basic conflict should be noted—clients aren't motivated towards spending more for outsourced services; yet service providers are largely incentivized toward revenue objectives. Adopting new technologies or capabilities that allow a client to spend less but that also yields greater service provider profitability ought to be the focus.

Enabling Contractual Structure

The contracts for successful innovation-producing relationships facilitate win-win situations that encourage the service provider to continually bring innovation to the table. This will affect many contractual provisions, including the contract scope, pricing approach, definition of and structure for pricing new services, gain-sharing, and potentially pricing based upon client business value metrics. The flip side of an enabling contractual structure is minimizing burdensome contractual requirements that may be onerous for the service provider and of minimal value to the client.

The sourcing industry has matured substantially during the past 40 years, and especially in the past 15. During that time, sourcing has become



accepted and commonplace; the process has been institutionalized; and we continually hear that the business has become commoditized, especially in the area of information technology outsourcing. It's time for the industry to step back and review the overall contractual structure we've developed to ensure that we haven't pushed the envelope too far in some of today's commonly used terms and conditions provisions. In particular, we should ensure that a well-performing service provider isn't unmotivated to deliver increased business value, such as may be the case with innovations that yield lesser revenue but higher profit margins.

Facilitating Governance Structure

The key is to drive the focus on innovation through the organization. Annual strategic retreats between key client and service provider leaders (including relevant subject matter experts) have proven effective, as have annual reviews of the client's strategic needs and the service provider's current capability by the service provider corporate subject matter experts. The ongoing focus is usually developed through quarterly scorecard reviews and permeates the ongoing interactions with an appropriate focus on innovation in general, as well as specific in-flight tactical efforts. The service provider's staff, who are tasked with ongoing delivery services, have a difficult time raising their heads from the tactical to focus on the strategic. Consequently, service provider organizations

successfully producing ongoing innovation have a small but effective team dedicated to the identification and realization of such innovation.

Innovative and Inspired Leaders

Last, but perhaps the most important, innovative and inspired leaders at the top of both the client and service provider organizations are the common component we see in successful relationships. Innovation requires change, and change is difficult. It doesn't happen without inspired and energetic leaders championing it. The client leader who really believes in and wants continuous innovation will set the agenda, require the service provider to step up to it, and insist on a service provider client executive with the requisite vision, energy, and skills to meet that agenda. I can't overemphasize the importance of the role of these two key individuals in the creation of ongoing innovation that drives true client business impact.

Have we found the Holy Grail of innovation through sourcing? Not in all cases—but in many. With focused intent by all members of the industry, I'm convinced the future holds many more opportunities for innovation produced through sourcing relationships. The keys are clear. Using them in the ongoing quest is up to us. [s]

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