# Chapter 1.11
# Strategies for Business Process Outsourcing:
## An Analysis of Alternatives, Opportunities, and Risks

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## ABSTRACT

This chapter provides a comprehensive overview of business process outsourcing (BPO) strategies and analyzes related issues. The discussions in this chapter can serve as an aid to decision makers who face the great dilemma of whether to insource or outsource a process, and additionally how to handle outsourcing to offshore locations. While business processes themselves are activities that need to be performed efficiently, outsourcing them is essentially a strategic decision that can ultimately impact the competitiveness of the client firm. This chapter explores the risks and opportunities associated with the numerous strategies related to outsourcing and offshoring alternatives, business process migration, contracting and alliance building, the role of the vendor, the nature of the relationship, multiclient or multivendor relationships, infusing maturity and ushering transformations in business processes, locating required expertise and quantity of workers, and also utilizing on-demand software services from application service providers.

## INTRODUCTION

In *business process outsourcing* (BPO), a client's business process is performed by a vendor. Certain business processes of the client are transferred over to the vendor, and the vendor's office then becomes the "back office" for the client's outsourced business processes. The vendors are given the responsibility to manage the client's business processes, such as call centers, emergency hotlines, claims management, helpdesks, data management, document processing and storage, financial services (banks and insurance), payroll, auditing, accounting, travel management systems, various logistics and information systems services (Millar, 1994, as cited in Lacity & Hirschheim, 1995, pp. 4-5; Sparrow, 2003, p. 11). Hence, a BPO vendor needs to have the capability to provide consistent levels of customer service spanning across a range of services and businesses.

Though BPO has inherent risks, it also provides many benefits to the client. Apart from focusing on short-term cost savings and operational efficiencies, it is important that BPO be performed with a strategic mindset, whereby decisions are based on wider business context and help in gaining competitive advantages in the tough external environment (Sparrow, 2003, p. 8). For effective BPO, an organization should segregate its business processes into two broad categories: (1) the ones where its own core competencies are strong and which have strategic significance, and (2) those that can be performed better by a vendor (Adler, 2003, p.53). In most cases, business processes that represent the client's core competencies and have high strategic stakes are best performed in-house. In order to identify its *"core competencies,"* an organization needs to be very clear about where its own strengths lie and identify the processes that truly give the organization its business value. In order to identify processes that are "strategic," the organizations need to be able to identify processes that differentiate it from its competitors in the marketplace, or processes that gives it the competitive advantage (Porter, 1996).

Importantly, the market is dynamic where the demands and competition changes over time and, therefore, the core competencies or the strategic nature of associated business processes may accordingly change. Hence, organizations also need to have a clear vision of their goals and future strategy in the dynamic marketplace and, accordingly, identify its business processes for outsourcing. Failure to do so can make an organization overly dependent on the BPO vendors for its core or strategic business processes, and it would effectively be at the mercy of vendors. The key here is to have complete power and control over one's core and strategic business processes, while gaining maximum advantages out of the various vendors' strengths in noncore business processes. This chapter discusses the various alternative strategies that clients should consider while pursuing BPO.

## STRATEGIES: BASICS OF OUTSOURCING AND OFFSHORING

### Business Process Insourcing and Outsourcing

The two basic strategies in sourcing business processes are *insourcing* and *outsourcing*. While in *business process insourcing* a firm executes business processes on its own, in *business process outsourcing* (BPO) the client firm establishes a contractual relationship and hands over the responsibility of executing the business processes to a vendor. In other words, a company "insources" from within and "outsources" to an external company, that is, *outsourcing* is the sourcing of work across organizational boundaries.

- **Insourcing:** The business processes are performed by the client itself or a client entity (such as a subsidiary or an internal department).
- **Outsourcing:** The business processes are performed by a nonclient entity (such as a vendor/supplier).

When a firm decides to insource its business processes, there are two basic strategies: (1) the "OK as is" strategy where the client feels that it is running its business processes efficiently and satisfactorily, and hence the strategy is to simply continue with the status quo, and (2) the "fix and keep in-house" strategy where the client might be a bit unsatisfied with the efficiency of its in-house business processes, but believes that insourcing is still the best option, and decides to invest in

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