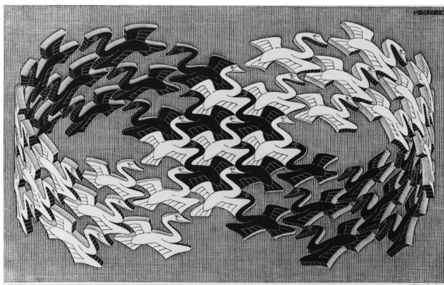
Perspectives

Transformation from the Outside In



The Boston Consulting Group

Transformation from the Outside In

What does it feel like to be “outsourced”? The question is increasingly relevant as outsourcing becomes, almost by default, the tactical choice for companies seeking to improve efficiency and focus. But outsourcing comes at a cost: loss of control. You’re dependent on outsiders. Outsourcing also torpedoes morale, because the message to your employees is “You’re not important enough or good enough to improve.” It is an unpalatable compromise, sometimes justified. But can it be broken?

What if the goal of working with an outsider were truly to *transform* a process or function, rather than simply to achieve the same performance at lower cost? Instead of farming *out* the function, as in traditional outsourcing, the company would bring *in* a team of qualified personnel from the third party for a prescribed period. The objective would be to help the company develop expertise and capabilities that resulted in a *self-sufficient,* better-performing work force in the long term.

When the agreed-upon period expired, the company and the vendor would part ways—with the company far better equipped to manage and profit from the transformed function. In a world where deconstruction—the break-

ing down of value chains in search of new efficiencies—is the norm, this kind of approach could be thought of as "rehab and return," or "*re*construction."

How Might Transformation Work?

Initially, a company would target for improvement a function that was underperforming and resistant to change—say, its IT division. The company would establish a baseline against which any change would be measured. It would also begin the search for a vendor (preferably thinking of the vendor as a *partner* rather than just another supplier, given the necessary closeness of the working relationship). Choosing the right partner would be paramount: not only would this partner need proven capabilities and expertise, it would also need individuals who could work effectively in close collaboration with internal employees toward a common aim.

The partner would then lead the development of a transformation plan, outlining an exact timetable (probably two to four years in duration) as well as the specific deliverables—in terms of both cost reduction and capability development. There would have to be absolute clarity on the quantifiable goals of the initiative, with milestones, performance metrics, incentive structures, and accountability for all elements of the transformation spelled out. Hammering out such an agreement would be time consuming because it would be more com-

plex and ambiguous than the arrangements that most vendors are used to.

Once the transformation was launched, the partner would inject senior staff into the company. These people would be responsible for introducing higher-quality working practices and driving efficiency improvements and cultural change. Depending on the extent of the transformation required and the company's internal management capabilities, up to two-thirds of the function's most senior management roles might be staffed by the partner at the outset. The size of the infusion below the senior level would vary, although it would probably equate to between 5 and 10 percent of all staff. That might seem high, but making change stick in an underperforming function requires building a meaningful backbone of higher-caliber resources to lead by example.

As the transformation progressed, the company would need to continually assess the partner's performance using both quantitative and qualitative criteria. Joint incentives (for example, shared bonuses for milestones achieved) could ensure that both the partner's and the company's personnel remained focused on the same goals. An important part of this effort would be the direct linkage of a substantial portion of the partner's compensation to the company's ability to perform at an agreed-upon level *after* the partner's exit. This stipulation would help keep the partner's sights trained on

sustainability—and on the internal organization's long-term self-sufficiency—rather than merely on short-term results.

Implementation would be more complex than for a standard outsourcing arrangement. Change-management and personnel issues, for example, could arise among the company's staff: accepting a better-qualified partner employee as a colleague, superior, or role model could be a fairly bitter pill for some to swallow, despite the transformation's generally positive impact on morale. At the same time, partner personnel might not perform up to expectations, and the company might need to take remedial measures.

Finally, the company would need to formally review progress on a regular basis—ideally every 6 to 12 months—to make sure that the effort stayed on track. And the company would need to be flexible because changes in the business environment or insights from the transformation program might necessitate adjustments to the original plan.

A Viable Alternative

This approach is not just a concept. There are cases of companies using it to achieve 50 percent gains in productivity and 20 percent reductions in cost. Maybe more important, these companies have remained in control and appear to have made lasting improvements in talent and capability: their employees now have

superior, value-creating skills that perhaps will even continue to grow after the transformation effort ends. So far, most of the examples are in IT, but we see no reason why other functions could not be similarly transformed.

In many situations, outsourcing may still be the right approach to achieving cost-based competitive advantage. In some instances, however, it may make more sense to transform in-house talent and capability in a critical area, thereby giving yourself a more durable or renewable advantage—and ultimately a more powerful one.

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