# Redefining Procurement Outsourcing: Looking Beyond the Limited Resources of Traditional BPOS

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EXECUTIVE SUMMARY

COMPANIES WHO THINK OF THEIR OUTSOURCING PROVIDERS AS TACTICAL RESOURCES RATHER THAN STRATEGIC PARTNERS - OR OPERATE WITH A “SET IT AND FORGET IT” MENTALITY, CANNOT DRIVE INNOVATION AND SUPPORT SUSTAINABLE COST SAVINGS

To augment staff and alleviate the burdens associated with recurring, time-consuming, and (perceived) low value tasks, many Procurement Departments utilize the services of outsourcing providers to manage specific business functions or subsets of the Procurement lifecycle. However, as companies mature and Procurement functions become more strategically aligned to business goals, traditional outsourcing models become incapable of properly addressing the organization’s needs. Shifting their mindset away from traditional methodologies, Strategic Sourcing & Procurement departments should focus on finding a provider that offers flexible, scalable solutions as well as a full range of resources, expertise, technology, and tools to help them attain and maintain a competitive edge.
INTRODUCTION

Strategic Sourcing and Procurement (SS&P) is becoming increasingly important to organizations. Once simply known as Purchasing, the role of SS&P is no longer limited to one-off purchasing or three-bid-and-buy practices as a way to derive the best price for supplies and services. Responsible for providing greater support and cost savings throughout a corporation, SS&P now serves an important strategic role, with more critical functions including strategic sourcing, category management, negotiations and supplier relationship management.

As new strategic initiatives are added to its charter, SS&P departments are frequently under-resourced, lack certain subject matter knowledge, and often struggle to retain talent, especially due to poaching from other companies. A survey conducted by Source One Management Services found that 30% of professionals in all areas of Procurement in organizations of different sizes feel that their department is understaffed.

With its ever-expanding and changing mission, the SS&P staff must possess a multitude of skills and tools to effectively serve stakeholders in different spend categories, all within the strategic scope of the company. However, in most organizations, it is difficult to maintain Procurement expertise in every area.

To fill in the gaps and optimize processes, more companies are turning to procurement services providers to supplement resources. Serving as an extension of SS&P, these procurement outsources can support internal Procurement operations with a multitude of support from on-demand labor, market intelligence, benchmarking services, training, automation tools, and more.

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THE PROBLEM WITH TRADITIONAL BUSINESS PROCESS OUTSOURCING IN PROCUREMENT

Traditionally, outsourcing was reserved for tactical pieces of a business with functions that could be easily replicated and not disrupt the business strategy (e.g., outsourcing the company’s travel management or telemarketing activities to specialized firms). As outsourcing became a more acceptable option to streamline operations and consulting professionals evolved in their offerings and expertise, companies began to trust more critical functions to third party providers. Businesses with a need for specialized talent or subject matter expertise especially looked for outside support as interim measures during periods of uncertainty, growth, etc.

While requirements have changed to support more strategic areas of business, “Procurement” continues to approach business process outsourcing providers (BPOs) the same way. Believing that all “procurement functions” are tactical and low-value, many companies still turn to the traditional, purchase-order-processing type out-sources. But if Procurement’s scope has expanded well beyond this narrow model to include strategic sourcing, category management, negotiation, and supplier development, who is left to handle the proactive, strategic, high-value activities?

Few traditional procurement outsourcing models go beyond the status quo to offer an end-to-end approach as part of an overall business strategy. Focusing on just the basic procurement processes, they do not drive innovation or help the company to maintain a competitive edge. Many traditional BPOs just offer the same static solutions year after year, even though market and business conditions may have changed. Others only offer limited, specialized support to address specific tasks or are too generalized to understand your industry. As a result, companies experience diminishing returns in their procurement outsourcing engagements.

In this climate, the best procurement services providers are now those offering a strategic sourcing approach that is adaptable to the objectives of businesses. Eliminating the need to work with multiple outsources, this multi-disciplinary, one-stop BPO model offers a complete set of scalable resources that provide on-demand support without being tied into long-term contracts. Working in a transformational capacity as well as transactional, they align their metrics to those of their clients – whether focused on improving operational efficiency, driving cost savings, or better supporting the organization – to offer long-term sustainable solutions and ultimately the highest ROI. (More on the difference of BPOs are discussed in Section III).
DON’T GET CAUGHT IN A BPO TRAP WITH DIMINISHING ROI

In addition to offering little or no competencies for strategic insights, traditional BPOs often trap companies in contracts with diminishing return on investment (ROI). While an initial level of savings may be produced, contract value decreases as the strategy does not meet future needs. For example, should a BPO offer a solution for contingent labor that attains savings of 80%, the value will remain at that level as the outsource model does not consider how to attain the remaining 20%.

And while savings remain static, the cost of BPO services typically increases over the term of the contract, reducing the ROI from year to year (see Figure 1). As many contract terms extend to five years, the cost of BPO services could eventually rival in-house resources as fees increase each year. And due to contractual obligations, the company must continue to utilize resources at the same levels each year, even if not needed. The long-term, fixed cost structures associated with traditional BPOs does not allow for any flexibility as business needs change.

A more scalable sourcing solution offered by strategic BPOs that offers an on-demand solution coupled with strategic goals aligned with the organization will drive greater year-over-year ROI.

The success of this strategic sourcing model is demonstrated with a large consulting company that wanted to gain better clarity with its procurement outsource provider. Initially, the company contracted with a traditional BPO for additional resources possessing expertise in strategic sourcing and category management. Although the BPO provided resources at a lower initial operating cost, the year-over-year FTE-based cost model of the BPO support team eventually matched the cost of in-house resources. And due to contractual terms and lack of strategic alignment, the company could not adjust staffing levels to match evolving business needs.

Unsatisfied with the return on investment provided by the traditional BPO model, the company sought a more customized, scalable solution that offered on-demand resources to match fluctuating needs for greater ROI and sustainability. Rather than focus on just the transactional side of operations, the BPO provided a full-service solution with best practices, market intelligence, and category-based services. Moving away from the larger, fixed costs engagements of a traditional BPO, the company found a cost-effective and sustainable solution with a strategic BPO model that was adaptable, flexible, and comprehensive in its offerings.

**Figure 1:**
The Traditional BPO Model for Procurement and Sourcing has diminishing returns

![Graph showing diminishing returns](image)
THE DIFFERENCES AND VALUE OF VARIOUS BPO MODELS

To support different Procurement operations and needs, companies often feel they must contract the services of several different BPOs to attain the right combination of resources. SS&Ps might supplement staff from one provider, acquire market intelligence from another provider, gain expertise or advice for improving processes from a third, or receive compliance audit services from a fourth. Using multiple service providers for each function effectively results in Procurement having to manage a considerable portfolio beyond all the categories of spend they’re overseeing.

While diversifying a portfolio has shown to be an effective risk mitigation strategy in the world of finance, it is not necessarily the best bet when outsourcing SS&P functions. Consider the level of complexity and effort involved with orchestrating the different outsources to ensure all are working within the realm of the corporate strategy. Does it, then, make sense to contract one BPO to serve all needs of SS&P? And which one(s) best serve the company? First, it is important to understand the differences and limitations of different traditional BPO models:

**CONTINGENT LABOR**

Qualified contractors can be hard to find, screen, interview, and hire. And when you do find them, they’re likely to be focused on one or two categories. With only their individual experiences, work databases and time, they may struggle to handle more than one task at a time or share the processes and results with a team and learn from it. As a result, companies need more contractors, which as we have established are time consuming to acquire.

**TRADITIONAL LARGE FIRMS**

Often brand name resources, these BPOs typically engage in long-term contracts and bypass stakeholders (who better understand the department requirements) to sell directly to executives, often promoting their own services or products sold at an extra fee. In many cases, SS&Ps are pitched an expert but assigned with generalists or less qualified personnel. Deliverables often include standardized reports so general in nature that clients are left with the burden to draw actionable insights from them. On the whole, these firms prove to be very expensive but are not necessarily any more qualified than boutique firms. Plus, they don’t typically stick around for implementation activities.

**GENERIC OR ANALYST-BASED BENCHMARKING AND INTELLIGENCE COMPANIES**

These online subscription services typically provide generic market intelligence or indices that don’t address specific industry and unique requirements. Limited to recent generic insights, they don’t extrapolate data from across industries to draw insights into specific market and don’t provide actionable guidance into how to source/negotiate/etc.

**ONSITE PROJECT-BASED TEAMS**

While these firms can be contracted on demand, a statement of work is needed and resources must be available each time services are needed. Companies have no guarantee the assigned resources have the right experience relative to their industry or if the same team is available as last time. As a result, you may have to start fresh with a new team that must spend additional time learning your business.
CONSIDER A ONE-STOP-SHOP

Instead of working with different, single-focus procurement outsourcing providers that may not even deliver high quality results, a cross-functional, full-service shop with a strategic operating model can provide all the necessary tools, knowledge, market intelligence, on-demand labor and flexible billing options to address any and all business requirements, while adapting to a business culture.

In addition to coordinating all the resources, the ideal boutique-style procurement provider will offer a dedicated, domestic and local team of experienced sourcing professionals that have worked together on numerous projects. Offering e-sourcing and contract management tools at no additional fees, these full-service outsourcing providers possess solid institutional knowledge and an extended database of market intelligence including industry best practices and prices.

The right single-source provider of procurement services will deliver concrete strategies and more customized solutions instead of standardized reports that adapt to your specific business needs.

ONLY PAY FOR WHAT YOU NEED

When working with any BPO, Chief Purchasing/Procurement Officers (CPOs) must be aware of the total cost of ownership. Long-term contract terms and lack of transparency in the fee model can result in lower ROI. For example, if tied into a three to five year contract with a fixed cost structure, a company might pay for resources that could effectively be reduced or eliminated as work scales back during the contract term. A strategic sourcing BPO model that offers an on-demand workforce gives companies the flexibility to change labor demand as needed and pay for only what it needs.

Contract transparency means there are no hidden costs down the line. Without a well-defined scope of work that anticipates and defines program requirements and costs, companies may find themselves paying more for services down the line that were not in the original contract scope – but perhaps should have been. CPOs need the right partner that can correctly outline a strategic solution the first time and not have to pay to get it right the second or third time around.

One fee model also does not fit all services. Flexible billing options that offer mutually beneficial payment terms can result in better savings. For example, a blended rate that bills different fees for administrative vs. management services would be beneficial on a project where experts outline a program that is administered by lower grade pay workers. Again, contract transparency in knowing the specific services associated with a program is key to understanding costs and activities associated with specific tasks.

An innovative, contingency-based approach, offered by strategic BPO providers, can even defer payment once a solution has proved successful and generated results. For example, should an outsource be contracted to lower vendor rates, only when suppliers actually bill the lower rate and the company generates savings would the procurement services provider receive payment. So, though the program may involve spend analysis, benchmarks, RFPs and contract activities, the BPO does not receive payment until results are proven.
When taking a closer look at the comprehensive services offered by the more strategic procurement providers, companies might be inclined to outsource complete functionality, especially until the Procurement department matures. While outsourcing transactional procurement functions (purchasing/buying) remains relatively low-risk when managed/governed properly, a full outsource solution will not work in the long term as SS&P must be aligned to the corporate strategy.

Even before outsourcing anything, companies should step back and determine the scalability of the solution to meet the organization’s specific needs. The success of an outsourcing engagement is highly dependent on the:

a) **Ability to find the right partner to support business needs**
b) **Amount of governance established for the relationship**

Having met both of these criteria still does not mean any task can be outsourced. Moving everything that falls under the “Procurement” umbrella to an outsourced solution cannot be sustainable in the long-term. Over time, organizations change organically and Procurement will need to change with it – organically. By maintaining an appropriate balance between internal and outsourced SS&P capabilities, Procurement can successfully support the on-going evolution and growth of the company.

Outsourcing the entire Procurement function would mean forfeiting strategic sourcing and supplier relationship management STRATEGIC to the business, especially as it grows. And as many BPOs operate without strategic focus, returns soon diminish.

Typically, it makes sense for SS&P departments to maintain staff for the 20% of vendors/suppliers/products that comprise 80% of spending. However, every company must determine the right combination of outsources and in-house capabilities.

According to the Aberdeen Group, Chief Purchasing Officers are almost five more times likely to select an Incremental Outsourcing Strategy versus outsourcing the entire Procurement Function.*

Prior to contracting the services of any type of BPO, companies should determine how provider services would benefit the long-term business strategy and what processes would be best served accordingly. What specific services or tools should be maintained in house or acquired externally to fill in the gaps or lack of knowledge? Without a strong plan that involves governance and metrics, companies shouldn’t outsource anything. And the more strategic/critical the function to be outsourced, such as contract management and business development, the higher the level of complexity of moving that function outside the company and back into the company.

The successful use of procurement outsourcing is about balancing both internal and external resources for maximum cost efficiencies and performance.
CASE STUDY:
STRATEGIC BPO DRIVES INNOVATION AND ROI FOR PHARMACEUTICAL COMPANY

Change is hard, especially when results are unproven. The following case study makes the case for SS&P departments to consider – and move – to a more strategic BPO model, especially in support of multiple and complex strategic sourcing requirements.

A pharmaceutical company with a very lean strategic sourcing and procurement staff was faced with the challenge of supporting a surge of projects throughout other departments. Recognizing the need for expanding their support capabilities in a variety of functional areas, they chose a multi-disciplinary procurement services provider (PSP) over a traditional BPO model to gain the flexibility to ramp staffing up and down to match business needs as well as gain knowledgeable resources to embed into its business culture without interruption to stakeholders.

Among the projects managed by the PSP was sourcing the right resources to support a new product launch to niche market areas. Marketing efforts represent a core function in driving revenue within the pharmaceutical industry in addition to being a significant business expense. To address the business strategy of the product launch, the PSP needed to source a variety of agencies with core competencies in creative, digital, medical education, and public relations services that also tapped into the patient and HCP community.

Activities included identifying suitable candidates, developing RFx documents, analyzing proposals, orchestrating pitch presentations to negotiating competitive rates and contractual terms with finalists, and facilitating the onboarding process. Taking an innovative approach to cost, the PSP leveraged specialized skills to develop functional, rather than blended rate cards that reduced the number of quoted hours tied to web and app development fees. The PSP also negotiated with a parent company to develop a comprehensive rate card across the agency network for more competitive rates.

When the pharmaceutical company launched another ground-breaking product, the PSP was again tasked with sourcing marketing support; but, this time, the company wanted a highly strategic, new service provider outside of its standard agencies to develop and manage the entire web platform. In addition to having experience in the design, development and support of user-friendly IT platforms, the supplier needed to have experience with HIPAA compliance.

After performing an in-depth qualitative analyses aligning company metrics with those of the potential suppliers, a quantitative cost comparison benchmarked supplier rates to ensure the vendor would deliver the highest level of quality at the most competitive cost. Going outside the box, the PSP asked potential suppliers to present innovative approaches to the IT platform design in addition to participating in an interactive planning session to present a strategy in a simulated environment. This atypical planning session resulted in the selection of a provider with the ability to rigorously capture and organize the company’s ideas and strength in design strategy and innovative thinking.

A tiered rate structure for all services directly associated with scope of work for current and future endeavors allowed the company to gain innovation and creativity at a cost that would not force them to forego future projects. Innovative thinking and planning such as this separates traditional BPOs from more strategic PSPs who can partner with companies in providing unparalleled value and ROI on a variety of sourcing projects.
IN CONCLUSION

The traditional BPO model for strategic sourcing and procurement is outdated and inefficient - because it is not scalable – it simply trades existing procurement resources for that of a service provider. Fixed cost structures and rigged contracts without strategic focus limit the value and the return on investment you can expect from these services.

A strategic BPO model offers a more scalable set of resources in providing flexible and comprehensive solutions, sustainable to business growth. More aligned to company’s strategic requirements than a one-size-fits-all approach, a strategic sourcing BPO focuses on providing procurement services that properly address company needs while identifying savings opportunities and capitalizing on economies of scale.

If the value or ROI of your sourcing BPO solution is not meeting your objectives or contracts do not align with current sourcing needs, it is time to consider a more strategic BPO that delivers solutions that are category-based, customized and scalable for higher savings and lower costs.
Source One is a strategic advisory and BPO firm that believes strategic sourcing and procurement groups are more than just bid administrators or corporate negotiators. Best-in-class companies use their sourcing groups strategically, gaining a competitive advantage in the industry and using them to gain access to new products and innovation, optimizing supply chains, and exploiting capacity restraints to disrupt competition. Our strategic sourcing solutions provide the tools and technologies, best practices, and market intelligence to ensure our clients stay ahead of the curve without being tied into fixed price, long-term contracts. Our flexible, on-demand procurement outsourcing model aligns with a customer’s needs, providing access to on-demand, real-time market insight and the ability to rapidly deploy third-party sourcing resources where they are needed the most. Find out more at: http://www.sourceoneinc.com/.

RESOURCES

4. Source One Management Services, How One Pharmaceutical Company Utilized An On-Demand Set of Resources and To Reduce Costs and Gain Access to the Best Ideas in the Marketplace, Copies requested at: info@sourceoneinc.com