

Global outsourcing trends and VMO

To track the ongoing journey of global outsourcing, Deloitte reached out to industry leaders from organizations of various sizes and operational footprints in the Americas, Europe, and Asia. The executives surveyed in our *2016 Global Outsourcing Survey* represent various legacy functions—including IT, finance, and human resources—from more than 25 different sectors. Our analysis reveals a vibrant pathway for outsourcing to drive innovation into the enterprise.

Technology stands out as an important area of focus for VMOs. The survey found that 85% of companies are looking at innovative technology advancements to further reduce costs and improve quality of IT service. VMOs are looking to the cloud, with 90% of respondents affirming that cloud computing is changing the outsourcing landscape by reducing cost of delivery and speeding up the rate of change. Similarly, 70% of the respondents are currently implementing or are discussing the use of robotic and cognitive process automation to improve outsourcing results.

Successfully harnessing innovation also requires a fundamental shift in traditional VMO capabilities, including an emphasis on training and skills development. A full 64% of the survey respondents have some form of vendor management skills training, indicating companies are recognizing the need to retool and equip their staff with the appropriate skills. Continued development of talent-focused capabilities, and getting closer to the business to understand their impact, can help VMOs better manage innovation.

For detailed survey results, visit www.deloitte.com/us/2016GOS.



Global outsourcing perspectives

Zoom in on value Vendor Management Office (VMO)

From 30,000 feet

Few would argue that global outsourcing innovation is accelerating at an increasingly rapid pace. But what does outsourcing innovation really mean to business leaders, and what is it worth?

For executives, it turns out, there may not be a clear-cut answer. Deloitte's 2016 Global Outsourcing Survey (GOS) reveals a challenge and opportunity for outsourcing innovation, with 65% of respondents indicating they do not currently measure the value delivered by outsourcers through innovation. While companies push service providers to bring innovative solutions to the table, only 28% of those surveyed feel that they have a mature Vendor Management Office (VMO). Further, only one in five respondents consider innovation when developing their contracts, even though they depend upon innovation to improve quality, maintain their competitive edge, improve user experience, and drive profitability.

Clearly, we are at a crossroads, where the pace of innovation threatens to outstrip

an organization's ability to manage global outsourcing initiatives. To effectively realize the value from innovation, organizations must first understand both the opportunity and impact of innovation on the business, and then evolve VMOs to manage these trends.

Challenges and opportunities

While VMOs do not directly implement innovative solutions, they do play a substantial role in managing the growing ecosystem of third parties that do. There are a number of complexities related to managing the operational impact of innovative solutions. This is especially true given the complex web of contracts, budgets, stakeholders, and partnerships. Contractual constructs should be put in place to encourage collaboration and preserve intellectual property (IP) while nurturing collaboration and measuring direct and indirect value. In addition, there are proactive steps that can move vendor management capabilities up the maturity curve and better position the organization to manage innovation long-term:

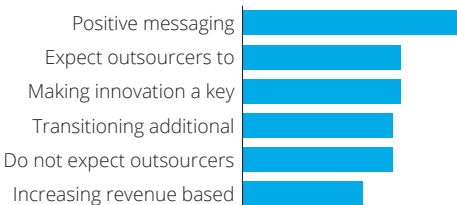
Defining the required benefits

The first step to realizing the desired benefits is a clear definition of end objectives and expectations. Companies are challenged to efficiently operate while balancing priorities to innovate and stay relevant in the market. These challenges can be managed through proactive and transparent service level agreements (SLAs), performance metrics, and continuous operational improvements. Responses to the GOS reflect the importance of SLAs, with 28% of the respondents highlighting “better SLA construction” and 20% highlighting “process transformation” as key learnings for outsourcing contracting.

Motivating the vendor to perform

Motivation is key to forward momentum. There are currently limited commercial models and terms in contracts to measure or incentivize innovation that have proven to be successful. The fact that only 21% of GOS respondents make innovation a key component of the contract highlights the lack of clarity regarding the expectations from innovation.

Approach to incentivize outsourcers to innovate



Post-contract signature issues, along with lack of innovation and leading practices, are two of the top five challenges companies face with their outsourced vendors. This indicates that either the innovation expectations are not clearly defined or there is a lack of strong incentive for the vendor to demonstrate differentiated performance. In either case, VMOs need to continuously scan the market and implement ways to motivate or incentivize vendors using relationship, contract, and commercial levers.

Tracking the realized benefits

With a lack of clear definition on how to track innovation benefits, it is challenging for VMO to differentiate the value derived due to innovation. Though the GOS reveals that existing VMOs continue to be most effective

at traditional vendor management activities, there is substantial room for improvement -- especially in multi-service provider integration, innovation, transformation management, and supplier risk management. How do we know there is work to do? Because key benefits -- measured in terms of service quality, measures of service value, and impact on growth -- are often missing from traditional performance reports and dashboards.

Managing legislation and regulatory risk

Although 75% of companies surveyed feel confident in their outsourcer’s ability to stay on top of legal and regulatory issues, many companies are expressing growing concern about legislative and regulatory risks. In some industries, especially financial services, the regulatory bodies are placing an increasing focus on companies to track risks of not only third parties but also fourth-party subcontractors. Banks and other financial institutions are increasingly scrutinized for risk management programs by such regulatory bodies as the Office of the Comptroller of the Currency, Consumer Federal Protection Bureau (CFPB), and the Federal Reserve Board. In one of the enforcement cases, the CFPB required an organization to pay hundreds of millions in fines and restitution to settle charges resulting from actions taken by the organization’s suppliers. Over the last five years since its inception, CFPB has provided approximately \$11.7 billion in relief to consumers through its supervisory and enforcement work. (CFPB, 2016)

In addition, regulators are heavily focused on what controls companies have implemented to track and report on the critical risks of third parties. Areas of particular sensitivity include outsourcing relationships where there is risk of an organization’s data being shared or transferred overseas, and instances where the outsourcer has direct contact with the companies. As a result, some organizations are making significant investments in building out vendor risk management and third-party compliance control and governance functions within the VMO. As the mix of products and services becomes more complex, regulators will focus even more closely on the provisions in agreements for commercial, contractual, and legal coverage and liabilities, which the VMO will need to manage and report on.

Lens on innovation: Alignment

VMOs, though traditionally perceived as tactical execution support groups for managing vendor relationships, can play a key role in driving the innovation agenda and cross-collaboration within the service provider ecosystem. This is especially evident as the ecosystem continues to become more complex with the introduction of consortiums of service providers, joint ventures, and a growing number of alliances between service providers. Alignment across several dimensions can help VMOs effectively drive an innovation agenda while managing transformation outcomes and ensuring seamless cross-service provider collaboration. From operating models to contractual constructs, stronger alignment helps solidify a foundation for innovation.

Innovative technology, solutions, and methodologies impacting VMOs include:

- Robotic and cognitive process automation (RCPA)
- Analytics
- XaaS
- Digital models
- Mobile banking
- Social media
- Cloud-based solutions
- Agile methodology

Vendor management operating model

To better harness and manage innovation, companies likely need flexible vendor management operating models that act as strategic enablers of innovation. This means that the processes, while well-defined, should be well-differentiated and able to change quickly to adapt to evolving business needs. It also means having the appropriate governance in place.

In some cases, it makes sense for a third party to perform select functions that are noncore to the organization so that the VMO can adapt a more flexible operating model. Overall, 30%-35% of the companies surveyed are currently outsourcing or considering outsourcing vendor management functions to a third party. This percentage has remained fairly consistent over the last couple of years.

Vendor management tools

Identifying tools that can help automate operations, especially while performing such repetitive tasks as performance reporting and contract analytics, is important. Tool adoption not only helps streamline processes, but can have a direct impact on talent that VMO's should embrace because of the need for technical skills required to operate these tools. Close collaboration with service providers to develop and customize tools is an effective way to meet the innovation needs of the organization.

Vendor management skill sets

VMOs should develop trainings that lend transparency into the leading practices, business operating models, and the role of vendor management functions. These trainings can be performed by a third-party service provider with increased visibility into marketplace innovation. Training and skills should be tailored to drive engagement across the workforce.

According to Deloitte's Human Capital 2016 Trends report, more than half of the workforce today is made up of millennials that value career growth and culture at almost twice the rate at which they value compensation and benefits. With such changing workforce demographics, VMOs should increase focus on improving engagement by providing value-added services, training, and a work culture that fosters cross-pollination of ideas and innovation.

Contractual constructs

It's important to demonstrate a commitment to innovation, transformation, and multi-service integration. This commitment should take the form of a contractual construct that includes a set of clearly defined expectations and RACI models, and also address any IP related concerns with regard to innovation. This can establish a faster contracting process and enable faster innovation. The development of clear risk assessment guidelines and SLA review guidelines can minimize contract renegotiation and associated changes during contract execution. Custom, value-driven, and gain-share pricing models are appropriate for select initiatives and service providers. A move toward these custom models can help facilitate innovation, but they also require an increased focus on financial management.

A look ahead

As companies continuously scan the ecosystem for new outsourcing trends, investments in VMO will likely remain a key component. By taking an elevated and strategic approach to innovation, VMOs can manage innovative forces across multiple service providers. This not only requires changes in how outsourcing deals are constructed, managed, and delivered, but also necessitates new tracking and measurement capabilities to demonstrate value. In the ongoing competition for talent, VMOs should focus on engagement, ensuring a clear career path forward and adequate learning opportunities for their talent to keep pace with the industry.

Let's talk

It takes strategy, vision, and experience to tap into the potential of innovation in outsourcing. If you're looking for ways to better navigate the evolving global outsourcing landscape, manage risks, and realize opportunities in vendor management, we should talk.

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