Intelligent automation: Fueling next-generation outsourcing

2Q 2018 KPMG Global Insights Pulse Survey Report

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KPMG Global Insights Pulse surveys are a quarterly review of global business services (GBS), intelligent automation (IA), and related service delivery market trends. Input and individual observations are gathered from KPMG’s global network of professionals in our Sourcing Advisory, Financial Management, Technology, Human Resources, Customer & Operations, and other practice areas, backed by KPMG market research.

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Demand for “traditional” outsourcing services has wavered in the face of the advent of competing delivery models.

Demand for traditional outsourcing arrangements focused on cost savings via economies of scale, labor arbitrage, and offshoring faces a strong headwind in the form of increased availability of a host of other options. Cloud, “as-a-service” models, and internal automation initiatives have provided compelling alternatives for organizations to reduce costs for labor-intensive, repeatable processes, historically the bread and butter of outsourcing providers.

While outsourcing has at times failed as a source of innovation in the past, targeted opportunities exist for innovation in the future.

Particularly for complex processes that are not central to business strategy, outsourcing can provide access to technologies that an organization does not have the skills or resources to develop on its own.

Outsourcing will continue to be an important component of corporate strategies, but service offerings must adapt to the new environment.

Successful future outsourcing models will make greater use of advanced technologies, rely on a menu of standardized service offerings, and differentiate themselves more on how services are delivered rather than what is delivered.
Is outsourcing dead? While some consider this an open question, its growth levels are certainly in decline. While the outsourcing market is still growing, organizations increasingly view internal investments, in shared services or otherwise, as the preferred approach to improve service delivery performance and reduce costs.

In the eight years that KPMG has conducted its Pulse surveys, net demand growth for both business process outsourcing (BPO) and information technology outsourcing (ITO) has dropped precipitously. In fact, for the first time since the inception of the survey, net demand growth for BPO has decreased. In contrast, net demand growth for internal process improvement efforts remains steady, as it continues to be the leading method for process enhancement.
Net change in demand by delivery model

* Net change in demand represents the percentage of survey respondents reporting an increase in demand minus those reporting a decrease for a given delivery model.
Organizations seeking to reduce costs and/or improve quality currently enjoy access to a range of approaches to which they did not have in the past. Cloud computing, “as-a-service” models, and advanced automation technologies are all providing organizations access to the benefits that outsourcing has provided in the past.

But, while the demand curve for traditional outsourcing is likely to continue to decline, the business drivers behind why organizations choose to outsource have not changed. Cost reduction is still top of mind in many industries, and with the advent of artificial intelligence (AI) and related technologies, organizations are increasingly looking for opportunities to harness technology to improve the speed, accuracy, and quality of the analysis they use to support critical business decisions. Outsourcing will continue to have a role to play in this new environment.

Internal automation efforts, most significantly in the form of robotic process automation (RPA), lead the way as the preferred approach to improve service delivery quality and reduce costs, with investments in cloud, enterprise software, and data & analytics close behind. All these approaches are more popular than the alternative delivery methods of BPO, ITO, and shared services. However, while these approaches are popular, their ability to deliver on a significant scale have yet to be realized.

Just as the onset of outsourcing as a broadly utilized delivery model caused disruption to clients’ employee bases, so too will the ongoing adoption of automation technologies. This will be true for both clients and service providers. This reality requires organizations to be honest about who can be reskilled, developing training programs when appropriate for those who can, and to take a long-term, holistic approach to where they will source required new skill sets.

Marcus Murph, Principal, CIO Advisory, KPMG in the U.S.

It’s far too early to say outsourcing is dead. However, many organizations see traditional sourcing providers as a source of low-cost labor rather than strategic insight. This opens the door for innovation-based entrants, and presents a complex challenge for many sourcing providers.
Preferred approaches to improve delivery/reduce costs

- Investments into IA in the form of RPA: 54%
- Internal process improvement/reengineering efforts: 51%
- Improve current SSC/outourcing governance: 43%
- Investments into cloud computing services: 32%
- Investments into/improvements to enterprise software: 32%
- Investments in advanced data and analytics: 30%
- Use/expansion of BPO: 25%
- Investments into IA in the form of ML and AI: 20%
- Use/expansion of SSCs: 20%
- Use/expansion of offshore captive SSCs: 19%
- Use/expansion of ITO: 17%
Outsourcing and innovation

The growth of digital technologies, automation, and AI has led organizations to increasingly focus on technological innovation in business process delivery. Does outsourcing have a role to play? Our survey reveals a high degree of skepticism in this regard, with 71 percent of respondents reporting that outsourcing providers have not met the transformation goals outlined in their contracts. Outsourcing providers and their clients bear equal responsibility for this failure, according to more than 60 percent of KPMG practitioners surveyed.

The reasons for this lack of innovation in outsourcing arrangements include:

– Outsourcing providers and their clients have tended to prioritize stability in service delivery over innovation. While innovation can pay long-term dividends, it can also be disruptive in the short term.

– Clients have tended to view outsourcing providers simply as a source of low-cost labor rather than a source of strategic insight. Outsourcing providers, in turn, have tended to focus their service offerings on cost reduction rather than quality improvement.

– Outsourcing providers have often customized solutions for different clients, which makes it harder to make innovation investments that they can roll out broadly across their customer bases.

Reasons for failure of outsourcing innovation goals

<table>
<thead>
<tr>
<th>Reason</th>
<th>Percentage</th>
</tr>
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<tbody>
<tr>
<td>Equal lack of effort/failure on behalf of both client and service provider</td>
<td>61%</td>
</tr>
<tr>
<td>Innovation goals unrealistic/unachievable/unmeasurable</td>
<td>19%</td>
</tr>
<tr>
<td>Lack of effort/failure on behalf of service provider</td>
<td>13%</td>
</tr>
<tr>
<td>Lack of effort/failure on behalf of the client</td>
<td>6%</td>
</tr>
</tbody>
</table>

Note: due to rounding, data may not add up to 100%
But just because outsourcing has fallen short as a source of innovation in the past doesn’t mean that it can’t be one in the future. Given the wealth of current alternatives to outsourcing, forward-thinking outsourcers will supplement their traditional, cost-focused offerings with innovative new ones, more tailored to serve the needs of specific functions and industries.

While many organizations are understandably reluctant to outsource innovation, particularly when it is central to their business strategies, outsourcing providers often possess the scale and expertise to provide solutions based on advanced technologies in a more effective manner. And, particularly for more complex processes, many organizations simply lack the required technical or functional skills to develop automation-based solutions on their own.

In the end, the answer to the question of whether to look to outsourcers as a source of innovation lies in four fundamentals: time, cost, focus and capability. Simply stated, does an organization seeking innovation want to incur the time investment, cost and potential distraction from more important initiatives by doing it on its own? And, most importantly, does it have the capability to do it in the first place?

Oftentimes innovation is the backbone to a company’s growth strategy. This is where outsourcing providers have an opportunity to evolve into an “as-a-service” solution and/or vertical-based providers to become a value-added partner to their clients instead of simply being the recipient of a traditional sourcing deal.

Randy Wiele, Managing Director, Shared Services & Outsourcing Advisory, KPMG in the U.S.
Learning from the success and failures of past approaches to outsourcing and recognizing past mistakes can help inform new approaches that will deliver greater value. Though it still has, and will continue to have, an important role to play in many organizations, cost-focused outsourcing based on exploiting economies of scale and other labor cost advantages will become increasingly commoditized, and will likely continue to be integrated with other delivery models.

In the future, successful outsourcing arrangements will make greater use of advanced technologies, incorporate flexibility in service delivery models based on a menu of standardized services, and encompass collaborative relationships between clients and providers that focus on value rather than cost. Greater use of advanced technologies stands as the single most important success factor for future outsourcing arrangements, according to KPMG specialists, followed closely by improved governance of outsourcing efforts.

Future outsourcing will include far less customization and far more off-the-shelf services, driving lower costs, faster transitions and higher quality. With a suite of standard services to focus on, outsourcing providers can more effectively target innovation to impact large portions of their customer bases.
Outsourcing agreements must adapt to reflect this new reality. The key characteristics of successful future outsourcing agreements include:

**A focus on standard rather than custom services.**

Customization of core services results in higher cost, lower quality, increased time lines and higher degrees of provider “lock in.” While there may be some short-term financial gains associated with customization, standard services offer the highest return in the long run. Clients need to be less interested in being different, and service providers need to better enforce standard approaches.

**Differentiation at the service provision layer rather than the definition layer.**

How a service will be performed will become more critical than simply what will be provided. However, this focus on the “how” does not involve customization of core services, but rather definition of how the core services will be provided and what add-ons to core services can offer additional value. While the content will differ for each service provider, successful agreements will utilize a common format to review and normalize proposed solutions.

**A well-defined process to accommodate unavoidable customizations.**

In some cases, differences between standard service provider capabilities and client requirements cannot be avoided. A well-defined exception process is the most efficient path to supply such customizations.

**Incorporation of third-party tools and services.**

Used properly, third-party tools and services are an excellent means to reduce the cost of governance, improve integration of services, facilitate interaction between service providers, and reduce operational redundancy.
Key success factors for future outsourcing arrangements

- Greater use of advanced technologies to enable cutting-edge technology-enabled outsourcing efforts: 47%
- Improved governance, risk and compliance capabilities coordinated across all outsourcing efforts: 46%
- Greater focus on value delivered over time rather than just costs to deliver services: 40%
- Integration with IA efforts overall and integration of IA technologies and services into outsourcing efforts: 37%
- More flexible contracts and pricing models to enable more flexible and creative service delivery models: 37%
- More of a business alliance/collaborative client/SP relationship rather than a client/vendor relationship: 36%
Actions to consider

You can’t always do it on your own

Understand when to undertake automation efforts internally and when to look to external providers for support, access to technologies, and ongoing service management.

Eliminate technology and provider silos

Evaluate the use of advanced technologies and data & analytics systematically, integrate dispersed efforts across functions, business units and internal and external providers, and recognize that some activities are better eliminated than automated.

Focus on governance

Ensure effective governance of automation efforts, whether internally or externally delivered, take a long-term view of the ROI of these initiatives, and ensure realistic and measurable metrics are in place to track them.

Responsibly reskill

Recognize the impact of the implementation of next-generation technologies on employees, and maintain realistic expectations about the extent to which existing employees can be reskilled. Phase out job roles that cannot be repurposed.
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