Current Trends and Future Directions in Services Outsourcing and Offshoring

Lisa E. Ellram, PhD
Professor of Supply Chain Management
480-965-2998; Lisa.Ellram@asu.edu

Wendy L. Tate
Doctoral Candidate
480-965-6044; Wendy.Tate@asu.edu

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Abstract. Managing and controlling services spend continues to be a topic of great interest and importance to all sectors of the economy. This research presents a summary of the results of a survey administered during the summer of 2005. 162 companies from a number of different industries responded to questions on services spending, outsourcing and offshoring. With the growth in services spending and the recognition of the opportunities to improve business results through services purchasing, this topic is very timely.

Summary. The information that was gathered from this research shows a number of changes occurring with regard to the importance and prominence of services purchasing. For example, a high number (38.6%) of respondents indicate that the Chief Procurement Officer is now part of the Supply Chain organization (see Table 1). It is interesting to note how many of the respondent organizations have a formal Supply Chain Department. In addition, many of the CPO's (or equivalent) report up through the finance area. This may reflect more stringent reporting and auditing requirements resulting from the implementation of Sarbanes-Oxley reporting requirements. Functional areas in the "other" category include Procurement and Materials Management.

Table 1: Respondent Characteristics – CPO Functional Reporting Area

Functional Area	% Reporting	Services	Manufacturing	Government
Administration	7.8%	10%	3%	20%
Business Ops.	7.8%	10%	5%	10%
Finance	9.8%	11%	6%	10%
Logistics	2.0%	1%	3%	0%
Manufacturing	3.3%	3%	3%	5%
Operations	14.4%	14%	17%	0%
Supply Chain	38.6%	33%	43%	60%
Other	16.3%	18%	17%	0%

The reporting levels of the CPO are relatively high; however still only about 50% report in at the "chief" level (see Table 2). Note that the Chief Financial Officer has the highest number of responses, followed closely by the Chief Executive Officer. This may indicate that the purchasing function has reached higher, but not the most senior levels within the organization.

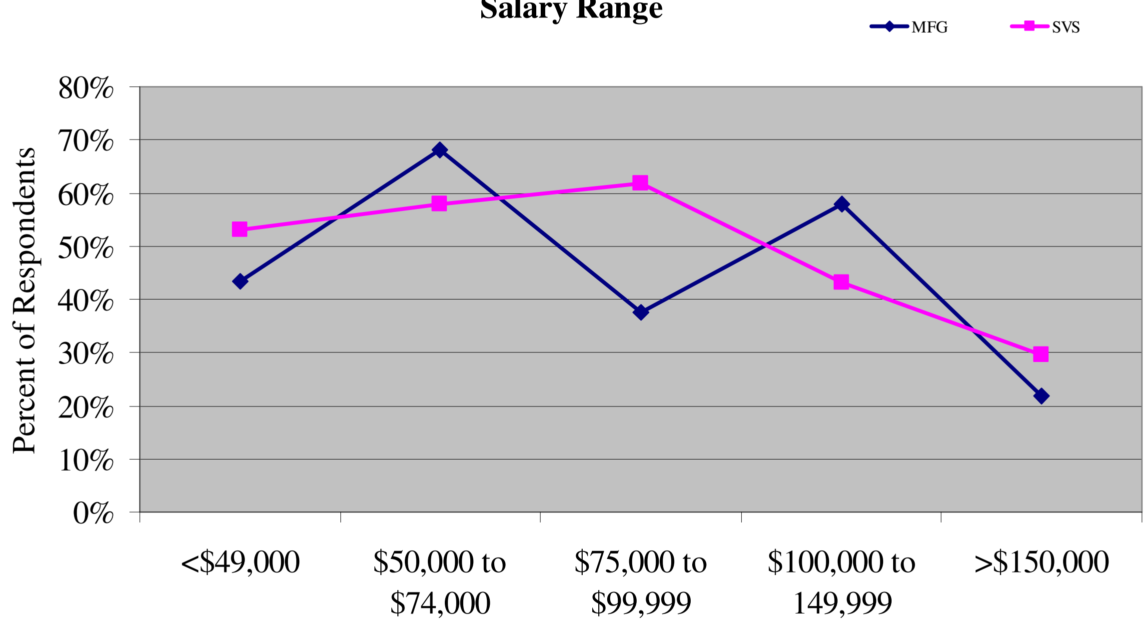
Table 2: Title of CPO of Person to Whom the CPO Reports

Title	% Reporting	Services	Manufacturing	Government
CEO	18.7%	13.8%	20.9%	11%
CFO	23.7%	23.8%	17.9%	22%
COO	5.8%	6.3%	4.5%	---
Executive VP	11.5%	7.5%	14.9%	---
Senior VP	15.8%	17.5%	11.9%	---
VP	4.3%	15%	16.4%	---
Director	3.6%	2.5%	1.5%	22%
General Manager	4.3%	3.8%	4.5%	---
Other	12.2%	10%	7.5%	44%

*Titles listed in the "other" category include: President, Chief Administration Officer and Committee Members.

This benchmarking data indicates that the area of supply management is gaining prominence. Salaries are competitive for those involved in services purchasing in both the services and manufacturing sectors (See Figure 1). Salaries are often a surrogate for perceived worth of a job within an organization.

Figure 1
Salary Range



When respondents were asked how they would view a move from managing direct materials to managing services, perception was mixed. As indicated in Table 3, the perception was more positive within the services sector

Table 3: View of a Move From Managing Materials To Services

	Manufacturing	Services
Promotion	4%	17%
Demotion	21%	2%
Lateral	73%	74%

However, there still seems to be a workload discrepancy, with services buyers having many more active suppliers, despite a comparable spend level (see Table 4). Interestingly, this discrepancy is even more pronounced in the services sector than in the manufacturing sector. In fact, the average spend per PSM employee for onshore service providers was comparable to that of the average spend on direct materials per PSM employee. However, the number of active suppliers being managed was almost three times as great for service buyers. Additionally, PSM employees that manage offshore suppliers oversee almost twice as many active suppliers as those that purchase direct materials.

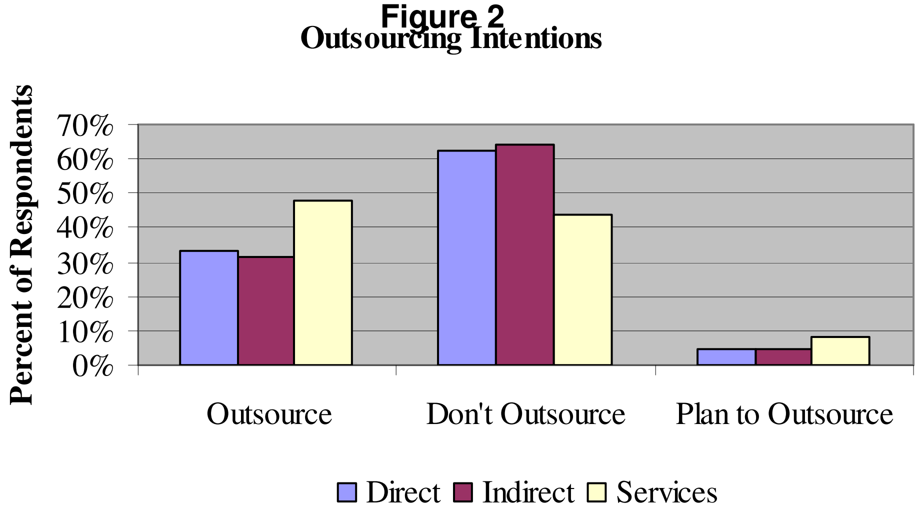
Table 4: Supplier and Spend Responsibility by Purchase Category

	Direct Materials	Indirect Materials	Onshore Services*	Offshore Services
Average number of active Suppliers per PSM Employee	36	101	105	71
Average Spend per PSM Employee (in Millions)	$24.5	$13.0	$24.9	$15.0

*Onshore and offshore service spend is estimated based on percentages of total services spend reported by the respondents.

Most of the respondents see their firms spending more in the future, but don't see a huge growth in outsourcing. The respondents to this survey indicate that more organizations outsource services than either direct or indirect materials (see Figure 2). A greater percentage of respondents also plan to outsource services.

Figure 2



Yet, services purchasing management still lags and needs improvement in a number of areas. For example, IT implementation to manage and monitor services suppliers is the lowest of any of the spend categories (see Table 5). There is a surprising difference between the information technology and controls used when comparing direct materials to both onshore and offshore services. For example, 71.3% of the participants indicated that an ERP system was used to control direct materials whereas 58.5% of onshore spend and 48.0% of offshore spends is controlled through an ERP system. However, the use of PSM software such as Ariba, Perfect Commerce, Rearden, SABRE, and Chimes is similar across the participating firms for all categories except offshore services. The use of information technology tools to control offshore PSM spend was the lowest in all categories.

Table 5: Usage of Information Technology

	Direct Materials	Indirect Materials	Onshore Services	Offshore Services
ERP (such as SAP, Microsoft, Peoplesoft, Epicor)	71.3%	66.4%	58.5%	48.0%
B2B or Supply Chain Software (such as Oracle, SAP APO, I2, Manugistics)	36.8%	30.8%	27.7%	16.5%
PSM (such as Ariba, Perfect Commerce, Rearden, SABRE, Chimes)	34.6%	39.3%	36.8%	25.9%
Custom/Legacy	48.0%	39.0%	34.4%	21.7%

Also, supplier performance on service purchases is often not measured, especially for offshore services (see Table 6). The manufacturing sector respondents use a greater variety of methods for measuring services suppliers than do services sector firms. The table below shows the percentage of respondents that measure onshore and offshore supplier performance.

Table 6: Measurement of Onshore and Offshore Services Suppliers

	Onshore Services	Offshore Services
Percent of respondents that measure supplier performance.	65.3%	38.1%
For those who measure, percent of active supply base covered	46.5%	56.9%

In addition, participants were asked to estimate the percent of active suppliers that meet or exceed contractual performance expectations. On average, 79.9% of participants indicated that onshore suppliers meet or exceed expectations, vs. 74.3% for offshore suppliers. In comparison, 81.5% of the participants indicated that the active direct and indirect suppliers meet contractual performance expectations.

Based on all of the information compiled for the survey participants, there are indications that PSM plays a bigger role and is more confident of its abilities and more satisfied with performance for offshore versus onshore services providers.

Conclusion. The bottom line is that good progress has been made in the management of services purchasing. There is still much opportunity for more involvement and higher level involvement. Other findings show that there can be improvements in the management and measurement of services suppliers. There is a belief among participants that the total cost of ownership (TCO) of offshore suppliers is higher than that of onshore. However, if we don't measure our suppliers, than how do we know the true cost picture? And, if we don't manage, how can we understand the improvement opportunities? So, as supply managers, you should feel good about the progress that has been made, but continue to be proactive in improving services purchasing.

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