In the late 1990s and early 2000s, service providers actively pushed arrangements such as joint ventures, asset purchases, and deals tied to a share in future earnings from new clients to establish anchor clients upon which they intended to grow their BPO business. Many of the early deals also had relatively unsophisticated full-time equivalent (FTE) only pricing models where buyers paid per FTE deployed (usually offshore). Therefore, guarantees of savings were a differentiator in the marketplace.

For the most part, services buyers fared pretty well with these deals, although they did take on the risks and growing pains of being early adopters. Service providers experienced mixed results. From a marketing perspective, these early deals gave them much-needed qualifications that allowed them to secure new revenue when the market was just getting ready to take off. However, from an operational perspective, these early deals gave them much-needed qualifications that allowed them to secure new revenue when the market was just getting ready to take off. However, from an operational perspective, the promise of creating cross-company “one-to-many” platforms and associated synergistic savings only partially materialized, as they often gave up on this aspiration in search of market share.

As the market matured during the mid-2000s, the appeal for these alternative commercial models waned. Buyers, supported by more third-party advisors, became more sophisticated in their pricing models. They asked for guaranteed productivity improvements, transaction-based pricing, and associated cost reductions as part of their basic deal, rather than as a differentiator offered as part of a “partnership.” Service providers responded in kind with more sophisticated mechanisms to estimate and contract for these productivity improvements. Overall market demand was very robust as many of the “fast follower” buyers jumped on the BPO bandwagon. Tier 2 providers built out their capabilities and became Tier 1 providers, resulting in reduced differentiation among providers. Yet, there was still enough pie for everyone to have a slice. And the providers did not feel as compelled to offer differentiated commercial models as demand often outstripped capacity.

Then the Great Recession hit. Large BPO deals slowed dramatically, replaced by restructurings, smaller add-ons, and multisourcing with multiple providers. Buyers took much longer to make decisions, dampening what had been very robust growth. No longer was the pie big enough for everyone to take a bite. Not surprisingly, some service providers have reverted to the old commercial strategies, hoping to lock in preferred relationships with buyers with reduced competition and then grow the accounts over time.

Does the following sound like a familiar pitch from an outsourcing service provider?

“We are looking to partner with a select set of customers. For the right to enter into an exclusive outsourcing relationship with you (with at least no initial competition), we will provide you guaranteed savings over the life of the contract. We have successfully entered into similar partnerships with other clients, and we would like you to consider a similar arrangement with us.”

We thought this proposition had mostly lost its luster in the marketplace, but have recently seen a resurgence. While it was enticing in the early days of business process outsourcing (BPO), how much value do buyers really stand to gain from such arrangements?
From a buyer perspective, just because the alternative commercial models proved largely beneficial in the early days of BPO does not necessarily mean they will do so today. Consider the following:

- The number of service providers with similar capabilities has dramatically increased. This is particularly true for the horizontal BPO offerings such as Human Resources, finance and accounting, and customer care. For these processes, no longer is there an incentive for buyers to enter into a partnership since there is a large pool of comparable providers that can service their needs. However, the same cannot be said for more analytical and less developed industry-specific processes. In fact, service providers are increasingly focusing on industry niche processes with fewer competitors, hence making these types of partnership relationships potentially attractive to buyers.

- “Price down” guarantees and transaction-based pricing are now achievable with or without partnership models. This is particularly true for horizontal BPO offerings where leading practices are well known, and both providers and buyers have the tools to adopt these practices to yield productivity improvements. However, less mature industry-specific and analytical processes still have more uncertainty in attainment of productivity, cash flow, or other business outcome benefits. In these cases, a savings or business outcome guarantee may be a much larger enticement for buyers.

- Service providers have gained religion on the need to standardize on cross-company process, location, and technology platforms to increase margins among decreasing rates of growth. Increasingly, we are seeing them develop platforms both for industry-specific processes and for horizontal processes geared toward a specific industry. If a buyer is seeking a major systems upgrade, entering into a “partnership” arrangement may be a solid driver for becoming an anchor client for a service provider’s platform solution with associated investment or related concessions from the provider.

- “Penetrate and radiate” can be a good approach for both parties. Service providers, particularly those based in India, historically adopted this strategy to gain a foothold into a client and then spread their tentacles further into the enterprise. While this practice can pose undue risk on buyers lacking robust governance and thus allow unmanaged growth, governance has come a long way from the early days of BPO. Buyers are much more sophisticated today in assessing the market and deciding whether an extension of services on a sole-source basis is warranted. Buyers with robust governance processes, programs, structures, and relationship management tools are now better equipped to gain the innovation and related benefits of a partnership without losing the advantages often inherent in a more competitive process.

- Risk management has become more important in today’s economy in areas including compliance with law, data security, transparency, and business continuity. Buyers may find that service providers are more willing to be flexible on contract terms and conditions in a “partnership” arrangement. With the proper determination of risk transfer—and due diligence to determine whether a service provider is in fact in a position to shoulder risks—a partnership arrangement can be more beneficial for a buyer seeking to more aggressively manage risks. However, buyers should be equally conscious of managing risks flowing the other way (e.g., exit provisions for dissolution of a partnership).

- The physical delivery location for the proposed partnership is an exceptionally important consideration. Is it a region prone to political instability and unrest? How solid is the technological and travel infrastructure? Does the provider have ready and robust access to the required talent to ensure rapid transition and go live?

- Some partnership arrangements, such as joint ventures, historically have provided certain tax advantages for buyers. However, these advantages have often been reduced or eliminated in the last few years. Before entering into such an arrangement, buyers should carefully assess the most recent tax laws.

While the answer as to whether to enter into an exclusive BPO partnership is far from cut and dry, my primary caution is “caveat emptor.” Before simply accepting what at first blush may sound like an enticing proposition, carefully evaluate your particular situation against the current market. Actively seek out the advice and counsel of third-party advisors and others who have made the partnership tradeoff for themselves.

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