



How Are BPO Providers *Bringing Innovation* to Customer Relationships?

»»»»»» Interview with **John M. Lutz**, General Manager, Managed Business Process Services, IBM Global Technology Services (GTS).

Each month, SSON is putting a BPO provider under the spotlight, asking them to explain how they are bringing innovation to their clients—a frequent criticism from the buy-side.

SSON: John, we tend to hear a lot of criticism of BPO providers in that they are not bringing enough innovation to clients, at a time when many see innovation as offering more value, or lower cost. What are you doing at IBM to support your customers in this respect?

John Lutz: You're right in that innovation is a keyword, at the moment. I think the reason we've seen so much interest in this is because of the shift in current economics. It's challenging everyone, right now. People tend to characterize it as a drive to cost cutting, and honestly, while cost cutting is very often on the agenda with clients these days, I don't know

that it always hasn't been so. But I've seen the urgency increase in a way that has brought an interesting inflection to the conversations we are having with clients.

Historically, BPO has felt like clients were trying to decide which of two doors to open. One of the doors was marked "cost cutting," and the other "transformation." Each of these doors, each decision, was seen as a very distinct choice. "Cost cutting" has historically been driven largely by labor-arbitrage but also by economy of scale, tooling, expertise, etc. It's often perceived as the less complicated choice, sometimes negatively characterized as somewhat of a knee jerk reaction. And it has been seen as quite distinct from the loftier notion of "transformation," which tends to be associated with more end-to-end kind of work, is perceived as being more elegant, if you like; more sophisticated, more complete, more enduring, and so forth.

What happened was that both clients and providers tended to see the market as falling into one of these two groups. And it's been like this for a while. I see a middle way, however. Our emphasis has been on retooling our customer engagement and delivery approach in a way that, I hope, will provide what is best for both, with minimal risks for either. The idea, for the client, is to get immediate payback and immediate cost savings without locking them in and thereby preventing them from gaining significant improvement to the process from the supplier. The problem in the past was that the cost cutting door was often associated with a process being taken far away and money saved ... but then concrete was poured around it. In other words, it was seen as somewhat of a one-chance opportunity and you didn't get to tinker with it to make it better later.



Now, because so many folks are driven by the urgency of cost cutting and the need to get a “save” right away, we’ve had to respond. And we’ve worked hard to come up with a solution that allows for a cost cutting decision now, but also continuous improvement over the terms of a contract. In other words, you can lift it, you can shift it, and then you can continuously improve it. You’re going to get immediate pay back and then we’re going to improve the process. This is where innovation comes in.

We’ve found that by applying some of our assets, and these would be tools we’ve developed in our centers, our research assets and our software assets from other parts of IBM — we’ve been on a software company buying spree for the last few years, we can leverage our unique capabilities to benefit customers. These kinds of innovations function as the engine to allow improvement and retooling over time, as opposed to having to commit to a heavy upfront transformation; and by the way, those long, heavy transformations don’t always have a great track record, either.

SSON: Can you give some specific examples?

John Lutz: There have been a number of instances where we’ve taken researchers with either horizontal or vertical industry expertise and developed bits that can be applied to a solution to significantly affect the way the process works. More often than not this impacts the quality of a process rather than the cost of it.

As an example, IBM is heavily involved with technology for road user charges. We are running some services for intelligent traffic systems around the world, including in Stockholm and we’ll be extending that to

London, later this year. One of the things that happened was that we needed to develop a way to sense the movements of the drivers. We developed a set of technologies for optical recognition of the vehicles. The requirement was that it be highly reliable—over 99%—and read while the vehicles were in motion. So we brought our colleagues in from research, who did their magic and used technologies they’ve been working on in the lab—many of which, incidentally, they develop before we know what applications they’ll be applied to. In any case, they were able to use optical recognition to work on the problem of recognizing the vehicles. Why would this be relevant to corporate shared services? It turns out, we’re now using some of the same basic technologies around character recognition to work on claims processing. We’re doing a variety of health care processing work in our centers around the world. Just last night the team was taking me through a new proposal for a provider. It’s a fast growing provider in one of the growth markets, not a West European or North American-based firm. It’s a firm that wants to grow very quickly in one of those growth markets. As part of our solution, we are developing a set of capabilities that involve recognition of forms. We think we have a unique angle here. It’s going to significantly improve workflow and reliability of that workflow with technology and it’s coming straight from research.

I mentioned using our software assets, earlier. For example, a lot of our processing work over the last 12 months has included technologies based on Cognos, a software company we bought a year or two ago out of Canada. Cognos has a long track record for doing analytical work. One of the things we’ve done in our process services group, here, is take some of these Cognos technologies and apply them to the business problems of the various shared services domains that we service. For instance, we have a little module available within our HR services called WFA—Workforce Analytics. It’s a high function dashboard that allows management within the lines of business to understand the dynamics of their workforce. It’s not that the problem hasn’t been addressed before, but this is part of our new strategy: taking high function software assets that we have in our catalogue and applying them directly to processing work and getting what we think is the best of both worlds. We’ve put this into some of our newer

deals, and we won a couple of notable global enterprise contracts as a result—Bristol-Myers and Kraft, for example—but we’ve also been able to move this into the production of some of the long established contracts we have. This is another instance where innovation allows us to take work after it’s been moved and improve it significantly.

This kind of innovation, whether it be from researchers or through software assets, is absolutely essential, because you can’t just ask the folks manning the work-station in the cubicles to make the system go much better. If it were that straightforward it would’ve happened already.

When it comes to analytics, there are a couple cases where not only have we used the software asset but we’ve directly applied researchers. In one case, and unfortunately I can’t name the company, a financial services firm was trying to understand how they could improve performance in terms of their assessment of risk, predict default and foreclosure. On the surface what we’re doing is running the service, the processing. But it’s not just taking what that firm was doing already and trying to do it a little cheaper, or faster, or better. We’re trying to do it in a way that’s smarter. And by applying some of this unique research insight into risk—because we have scientists in that major in this—we’ve been able to improve performance. Not the efficiency of the production line, where people always start, but in terms of the effectiveness of that process within the firm. There is often more benefit to be gained there, than there is in the efficiency of the function. We see that all the time. We have customer care call center work where what we’re really working on is not improving the average call time, or the efficiency of the engine, but getting that engine to be smarter. In the case of a media company we do work for, we’re working to reduce the number of times that an outbound physical service call happens. Truck rolls, as they call it. They are trying not to roll the truck with the service tech in it out to the house. If we can make a little bit of a dent in that metric, we will have a more profound economic impact on the overall situation. We’re trying to innovate around the value proposition we propose to clients. We’re saying that we’re going to look at both the productivity of the group and the other benefits to the firm. We call it Total Service Value.

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SSON: It's sort of taking it a step further, then, to operating end-to-end within the client facility?

John Lutz: Absolutely. When I was first thinking about this it seemed like we had one or two scattered instances where it might be a useful concept. We discovered it really applies to everything. For example, F & A, where we might take on accounts payables. This doesn't seem like an area where you'll have some sort of interesting innovation. We've done some work with an eye toward this higher intelligence, this smarter payables, where we've scanned historical patterns of payees and understood from this whole corpus of transaction, where we might have duplicates. I was skeptical at first, because I thought duplicates had to be pretty easy to spot. But they said no, because sometimes you have part-payments, sometimes you have miscoded invoices, and so forth. So even though we're really just paying the flow of transactions on behalf of our client, we are now able to do a better job of recognizing where they might be overpaying. A few of these a month create a bigger economic impact for the client than making the productivity of the payables engine go a little faster.

So those are some of the things going on here.

SSON: I can see if you are negotiating with a new client, bringing this to the table is a great draw—but what about for established clients? What is the incentive for an outsourcing provider to bring innovations to ongoing contracts? And how do contracts allow for some share of the savings?

John Lutz: That's something we're all wrestling with. You're on a key topic. Historically, a lot of contracts were done in a sort of "linear to labor approach." The cost

equation was very clear, tied, as it was to specific metrics: bums on seats or minutes on the phone. But it didn't allow much opportunity for any of the things we've been talking about. One of the things we've had to do, to your point, is develop some different contracting mechanisms so that we can share some of this benefit with our client because what we really want is to align our client's motivation and our motivation, such that when we improve the quality in a way that is beyond expectation, by using some of the tools I've mentioned, then we benefit and the client benefits. We've been able to do some of that, but I would say it's a work in progress from both sides. It requires that we be flexible and innovative in our terms and that the client be able to accept them.

We've been able to learn a lot from our IT outsourcing business, which has been in operation for a long time—15 to 20 years—and has therefore gone through a number of renegotiating periods, even for its 10 year contracts. We've learned a lot from these. One thing that happens in the maturation process is that as a supplier we know that you do need to deliver continuous improvement, even mid-contract. In some cases that means renegotiating. If we think we have a way to make a piece of the work go a lot better, be a lot faster, or offer better quality, then we'll go back in and say we have an idea here, and we'll pursue this idea if you'd like us to, and we think it might be something that would cause us to look at this part of our arrangement with each other and make a change. In some cases that gets us more volume and an even bigger deal. In other, it makes something more efficient and makes the deal smaller for us. This question requires us to be very nimble and requires clients to be very flexible in how they think.

SSON: Does this push for better solutions come from external market competition or from the clients themselves, who are simply expecting more today?

John Lutz: I think the external environment has hastened some factors that probably would've played out anyway. It's hard to say whether it's just one or just the other. You always have a cross section of clients who are pushing the edge and some who are following along. I'll tell you that the change for us is driven very much by the idea that it's not interesting for anybody

to have only a highly commoditized, completely price-driven, completely labor-arbitraged kind of program. The client may get an initial hit of cost savings but not much after that. So it's not terribly interesting to us over time. It's not how IBM participates in the other markets we participate in either. If you think about it, we tend, in hardware, to stay away from heavily commoditized businesses, and go to higher value segments. We do the same in software. And in IT services, similarly, we spend much of our time in higher value kind of work. So in process work—in this case, business process outsourcing—we're trying to do the same.

Now, you do have to have base capability. You have to be able to run a factory. We think the value agenda requires that as well. But if we weren't leveraging all these research guys, we wouldn't be taking advantage of what it is to be part of the IBM company. We wouldn't be giving our clients the benefit of dealing with us as a distinctive choice in the marketplace, compared to some of the other options they've got. It's not for every deal, not for every client, but we think there's a good subset where it matters.

SSON: So, it's about a cultural approach, at IBM?

John Lutz: I'd say broadly that's correct. When it's required as part of a deal we can certainly offer factory kind of capability, but our bias is towards helping clients who are themselves pursuing high value orientation in their industry and our bias is to help them in that innovation agenda, not just be faster and cheaper. **SSN**

About John Lutz

As General Manager of IBM's Managed Business Process Services, John leads IBM's business process outsourcing and transformation efforts. Through these services, IBM combines deep industry knowledge, process know-how and leading technology to improve the efficiency and costs of high-pain, high-cost, back-end business processes such as human resources, finance and accounting, supply chain and customer relationship management. Prior to this role, John was General Manager of IBM's Global Financial Services organization, responsible for IBM's overall relationship with major financial services firms around the globe.