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## What Is Strategic Sourcing?

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## INTRODUCTION

The terms ‘strategic sourcing’ and ‘sourcing strategy’ are in wide use in sourcing circles, but there is little shared understanding of precisely what they mean. The result is not just linguistic confusion. By not clearly identifying and distinguishing what makes an approach genuinely strategic, companies run the risk of ending up with a series of tactical operating models that may deliver short-term cost benefits but that lock in existing inefficiencies and fail to address the root causes of poor performance. The strategic approach in contrast results in an alignment between sourcing options and business objectives, and in our experience, it leads to more significant and sustainable benefits for the company. This paper describes strategic sourcing, proposes a standard set of definitions, explains what distinguishes strategic from tactical sourcing, and indicates why we think that the former approach can be a significant differentiator for companies as they strive to enhance their competitive advantage.

### WHAT IS STRATEGIC SOURCING?

Strategic sourcing goes beyond the simplistic formula of ‘outsourcing what isn’t core’. Instead, a strategic approach to sourcing connects the company’s operational base to its business aspirations. It ensures that the service delivery model is not only aligned with, but can also help to drive forward, the critical operational and information technology (IT) aspects of the business strategy. This approach means going back to basics by considering the direction in which the business is heading and using sourcing options to help take it there.

A well-constructed sourcing strategy should address three fundamental questions:

- Where are we? How effective and efficient are our current capabilities?
- Where could we be? What are the incremental opportunities?
- How can we get there? What is the roadmap that will allow us to move forward?

Like many things in business, ambition is a moving target. Developing and implementing a strategic sourcing strategy is complicated by changes in executive leadership, market pressures, shareholder expectations for near-term results, and the like. Yet, when designed and implemented properly, the benefits of sourcing programmes are compelling.

A sourcing strategy is a process, not an isolated decision. It continuously:

- Balances internal and external activities, services and know-how;
- Aligns business strategy, business processes and IT services; and
- Balances the results that must be achieved and the future options available.

In today’s fast moving, competitive environment, all major projects need to be aligned with corporate objectives. Sourcing has the potential to deliver significant benefits, but large projects require substantial effort and often result in considerable change in the organisation. These projects demand resources and management attention that, depending on corporate priorities, may be better directed elsewhere. Good contracts often founder because alignment with the corporate operating model is not adequately addressed. All of these factors should be considered prior to initiating sourcing activities.



## STRATEGY AND OPERATIONS

In broad terms, the two key questions a company faces are what to do and how to do it. One way to address these questions is through a consideration of the interaction between four distinct views of the company. At the highest level is a **corporate** or **enterprise strategy**. This is a clear statement of the company's target proposition, and what makes it unique and differentiating. Determining the corporate strategy will involve a number of choices; for example, around the product or service offered and the market segments targeted. The corporate or enterprise strategy will inform the strategies of individual business units in the company.

The corporate strategy is an outward-looking view. It in turn informs — and is informed by — an **operating model**, which is an internal view of the way the company should be structured, for example into functional areas or business processes, in order to best meet the requirements of the corporate strategy.

The next level of detail is a **sourcing model**, which specifies the internal or external organisations or groups that will perform the activities needed to deliver the functional areas or business processes set out in the operating model. Finally, and supporting the sourcing model, a **service delivery framework** provides a detailed mapping of how and to what level of quality each of the required services are to be delivered, and how the supply and demand of these services will be managed.

In summary, then, the **corporate strategy** sets out what the company is trying to achieve; the **operating model** sets out how it will organise itself to do this; the **sourcing model** defines who will be re-

sponsible for performing the required activities; and the **service delivery framework** shows how these activities will be efficiently delivered to the required level of service.

## TURNING THE SOURCING MODEL INTO A SOURCING STRATEGY

Typically, separate business units and geographies — and often individual functional units within these — will have their own distinct sourcing models. In order to transform such discrete or tactical sourcing into a *sourcing strategy*, two conditions are required.

First, the distinct areas within the sourcing model must be *joined up* across business units, functions and geographies into a single, coherent picture. Second, and most important, the joined-up sourcing model must be *aligned with the enterprise strategy* — and hence the operating model — in particular, the objectives for growth and change implied by the enterprise strategy.

Such a joined-up approach will lead to a clear framework for sourcing across the company, consisting of a series of guidelines and decision trees that will enable specific business activities to be categorised and evaluated, and thus each aligned to a set of well-defined sourcing options. This in turn will determine the optimum sourcing state at the local or business unit area.

Many sourcing approaches are available: not just external options such as outsourcing or offshoring or even insourcing, but also internal reconfigurations to shared services or centralised utilities centres or decentralised competence centres. Through a wide



consideration of these various sourcing approaches, the strategic sourcing process ensures that the local sourcing state, and hence the local service delivery model, is not only aligned with the critical operational aspects of the business strategy, but also can help drive them forward. Further, it will be a straightforward and transparent matter to ensure that each local sourcing state is flexible and responsive to the changes in operating model or enterprise strategy.

## **BENEFITS FROM STRATEGIC SOURCING**

The tactical approach to sourcing is characterised by service models at the business or functional levels that pull in opposing directions, a lack of standardisation and consequently waste of supply or purchasing leverage, and the appearance of unexpected dependencies and risks across the business. The result is a dysfunctional operating model that locks in existing inefficiencies without addressing the root causes of poor performance or the future needs of the business. One unfortunate consequence of the

growth of outsourcing to encompass not only IT but also business processes and increasingly higher-value knowledge processes is that the tactical approach is becoming more prevalent. And the silo mentality that accompanies distributed organisations further exacerbates the problem.

In contrast, by connecting a company's operational base to its business aspirations, the strategic sourcing approach has two advantages. First, and most important, it shifts the emphasis from short-term cost-cutting and process efficiency to a focus on the strategic change imperative and long-term value creation of the enterprise as a whole. This shift in emphasis does not mean that significant cost improvement cannot be achieved. On the contrary: the second key advantage of the strategic approach is that by creating an opportunity to identify the optimum service framework across the company, scale economies can be maximised and more significant and sustainable cost savings delivered than via the tactical approach.



## THE 10 GOLDEN RULES OF STRATEGIC SOURCING

1. **Avoid a piecemeal approach:** Leverage sourcing as an integral component of your overall business strategy.
2. **Be strategic:** Ensure that your service delivery model is not only aligned with, but will also drive forward, the enterprise's ambitions.
3. **Take a holistic, enterprise-wide approach:** This will maximise economies of scale, avoid duplication and ensure continuity of standards.
4. **Sourcing is not synonymous with outsourcing:** Review your present operating model and create a roadmap for future requirements that considers all of your options both internal and external, while balancing value, risk and speed.
5. **Sourcing is an ongoing process, not an isolated decision:** By deploying flexible services from wherever they are best provided, you can quickly and effectively respond to changing market conditions.
6. **View service providers as partners:** By keeping service providers informed of business goals and constraints as they evolve, and by structuring the relationship so that it is beneficial to both sides, your partners can innovate and transform in order to provide long-term value.
7. **Ensure buy-in:** Executive sponsorship, centralised management and company-wide support are vital for success.
8. **Identify the changes necessary to move to the new model:** Communicate a compelling vision of the future that conveys the competitive advantage for the company and the opportunities for employees.
9. **Service Management & Governance:** Develop a corporate Service Management & Governance function with the skills and systems needed to drive effective sourcing strategy, execution and management.
10. **Seek independent advice:** Develop an informed perspective on your current operating costs and performance vis-à-vis the market and the future potential of your target operating model.



## CONCLUSION

Strategic sourcing is an instrument for flexibility. Neither a rigid decision nor a static contract, sourcing should and increasingly is being viewed as a “top-down” tool to connect strategy with implementation. It means moving away from providing services, on a function-by-function or business-unit-by-business-unit basis, to managing services on a company-wide scale. Designing and implementing service propositions that capture enterprise scale and maximize synergies is not easy and requires that a company addresses interconnected needs and capabilities across often far-flung global operations. However, financial services firms and companies across all industries that can move in this direction will enjoy better performance and cost efficiencies than organisations which persist with a function-by-function approach and redundant, subscale services.

Many executives fall into the trap of thinking of sourcing initiatives as merely tactical or technical projects rather than long-term, significant strategic programmes that fundamentally change the profile of the organisation. It is vital that companies do not underestimate the strategic value of their sourcing relationships as the foundation for ongoing success.

## LOOKING FOR A STRATEGIC PARTNER?

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## ABOUT THE AUTHORS:

**Mr. Rawlinson** possesses broad-based experience in business-to-business and information technology (IT) sourcing from client, consultant and service provider perspectives. Tony brings TPI's clients a wealth of business process outsourcing (BPO), IT outsourcing (ITO) and global service delivery expertise with his proven ability to identify and implement new strategies to improve business performance and to provide a strong understanding of business drivers, industry trends, regulatory frameworks and technology enablers.

Prior to joining TPI, Tony was an EDS Client Executive in the United Kingdom and Ireland. He effectively managed client relationships, renegotiated contracts and led the development of a new strategic operating model with fresh approaches to data capture and onshore and global service delivery processing.

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Prior to joining TPI, David worked at Barclays Bank PLC as a Senior Program Manager responsible for directing major initiatives to cut costs and improve customer service in retail banking through a mix of process redesign and reengineering, technology solutions and strategic outsourcing. While in the Group Strategy and Planning team, he carried out a number of projects, including working with board-level sponsorship to guide the bank's approach to corporate governance.

David holds a Bachelor of Arts degree in Physics and a Master of Arts degree in Atomic Physics from the University of Oxford. In addition, he earned two doctoral degrees; one in Atomic Physics from the University of Oxford and another in the history and sociology of science from the University of Pennsylvania.

**ABOUT TPI:** TPI, a unit of Information Services Group, Inc. (ISG), is the founder and innovator of the sourcing advisory industry, and the largest sourcing advisory firm in the world. We are expert at a broad range of business support functions and related research methodologies. Utilizing deep functional domain expertise and extensive practical experience, TPI's accomplished industry experts collaborate with organizations to help them advance their business operations through the best combination of outsourcing, offshoring, shared services and internal service optimization. For additional information, visit [www.tpi.net](http://www.tpi.net).

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