

HYBRID MODELS AS A MIX OF SHARED SERVICES AND OUTSOURCING OR COULD HYBRID MODEL BE THE NEW MANAGEMENT BUZZ IN THE FOLLOWING TIMES?

Robert Marciniak

University of Miskolc, Hungary
H-3515 Hungary, Miskolc-Egyetemvaros
E-mail: szvmarci@uni-miskolc.hu

— Abstract —

The aims of shared services and outsourcing are very similar: improving processes and making more cost-efficient the operation. For a long term this two models had been competitors of each other because companies had to choose between them. Nowadays there are several solutions that allow of combining the benefits of these traditional models. These new solutions are the hybrid models. I focused on them in this paper.

In my research I analyzed some of corporate case studies to explore the main characteristics of hybrid models. I have striven to determine the connections among captive centers, outsourcing providers and hybrid models and how to make a distinction among them.

I differentiated the most common types of hybrid models (BOT, virtual captive) and made a comparison between them.

Key Words: *Shared Services, Captive Center, Hybrid Model, Outsourcing*

JEL Classification: M19

1. INTRODUCTION

1.1 Background of the research

In the last few years outsourcing, shared services and offshoring models passing through serious progress. While companies made separate strategies to use sourcing models until now these three models are connected tightly and constitute the corporate sourcing strategy in a portfolio approach. Among three models there are shared services in the focus of my research and in this paper I analyzed those new structures and characteristics.

Shared service model operates in shared service center that is an centralized organizational unit to deliver certain internal services mostly for the other organizational units or partly for other companies. (Bodnár,2006:277)

The shared service center model appeared in the 80's in the USA and until then there is high interest about it not only in the private sector but in the public sector as well. Nowadays 80% of the largest 2.000 companies apply shared service model to support some of their non-core functions. (Zinnov,2010:3)

The main goal of establishing shared service centers was cost-cutting but by now its judgment has been changed. Corporate leaders consider them as strategic business units to realize service and operational excellence. In line with it the service portfolio of shared service centers were also extended. These days centers include more complex and knowledge-based processes like R&D, sales or marketing which are closer to traditional core business. The most drivers for establishing of shared service center are the followings:

- improved services, reduced costs;
- standardized services and processes;
- diminished administration costs;
- supporting corporate strategy;
- grouping similar tasks and demolishing redundant processes;
- favoring progress;
- facilitating introduction of new technologies;
- improving working capital.

1.2 Justification of the research

In the last few decades there was a three-step progress up to the present model. Firstly companies created captive centers that delivered only internal services – like finance, HR, billing, procurement - for their own organization. Consolidating these processes and gaining cost-benefits captive centers get quickly popularity among large companies. Although this step of service provider's progress contributed to the success of many companies but there were several companies that faced such problems like non-competitive price in contrary to outsourcing providers or underutilization of resource capacities. The next step of this progress was when companies turned to the offshore service providers that took out under-performing captive centers and ensuring bigger cost-benefits and flexibility. But in offshore model there were also failures. Companies lost their valuable knowledge and get worried about the innovation. The third step of this progress was when the companies get to move to outsourcing providers. The problem is

similar because the innovation is also a lack and beyond these outsourcing providers there are offshore service providers as well who has not got the necessary knowledge background and experiences. (Aese,2011)

In case of the traditional delivery models companies have to poise between pros-and-cons of models and usually have to undertake some trade-offs. There are several dilemmas like it for example cost-cutting vs. losing control, dedicated resources vs. transient resources, outsourcing vs. remaining non-core functions, transaction-based vs. customer-tailored processes. Solving these dilemmas the leading companies use hybrid models more frequently where combining the back-office outsourcing with the captive centers under tight cooperation.

1.3 The purpose of the research

The aim of this research was to explore the types and the main characteristics of hybrid models. I collected some points of view to make distinction between the traditional models and hybrid models. And finally I analyzed the most frequent two types of hybrid structures.

1.4 Methodology

I collected 8 corporate case studies that are about hybrid models. In all of these case studies companies have own sourcing strategy with one or more hybrid solutions. I analyzed the case study and draw some conclusions from them.

2. CONCLUSION

The hybrid model alloys the benefits of traditional models and so it outperforms the “moving everything to the cheapest offshore location” model. Therefore there is no sense to treat outsourcing independently from shared services because the two models interweave organically in the company. (Gammage,2010)

In hybrid model the center of some services was moved (for example front-office function) to onshore or near-shore locations which are in time, culture and geographical close to the customers (like Middle-East Europe), and other services (back-office functions) to a cheaper, geographically, cultural distant location (like India, China or South-Africa) The previous one could be realized in a shared service center, the latter one with an outsourcing partner. So hybrid model is a mix of both model but is extended for different services. (Williams,2005:6)

On the onshore or near-shore locations companies deliver higher value-added services, while on low-cost, offshore locations there are more transaction-based global centers. The former one is closer to the customers and because of it the

service delivering need strong knowledge of local languages or regulatory. The latter one does not need such a deep cultural or legal knowledge.

In the followings (Table 1) I compared the shared services, outsourcing and hybrid models with each other according to some points of view.

Table 1: Comparison of operational models

POINTS OF VIEW	SHARED SERVICE (CAPTIVE MODEL)	OUTSOURCING	HIBRID MODEL
OWNERSHIP	100% own property	no own property	optional property
CAPITAL INVESTMENT	high capital investment, all ensured by own	no initial investment	less capital investment initially and bigger flexibility through the process
RISK LEVEL	all risks are undertaken by own, no long-time commitment	shared risks, outcomes under agreements (costs, SLA-s)	no long-time commitment
IMPLEMENTATION SPEED	long implementation time (usually 6-9 months)	quick implementation (usually 1-2 months)	quick implementation (usually 1-2 months)
MANAGEMENT FOCUS	on the operational and administrative activities	free focus on strategy and business issues	enlarged strategy and business focus
LEVERAGE FACTOR	own environment	multi-user environment, best practice process model, platforms and cooperation	pressing to reduce costs
FLEXIBILITY	less flexibility	flexible pricing, ability to reduce size of operations	quick adaption to the changed business requirements
COST MANAGEMENT	long time cost reduction	high operational cost	transparent cost structure
CONTROL	total operational control	very small control	total operational control

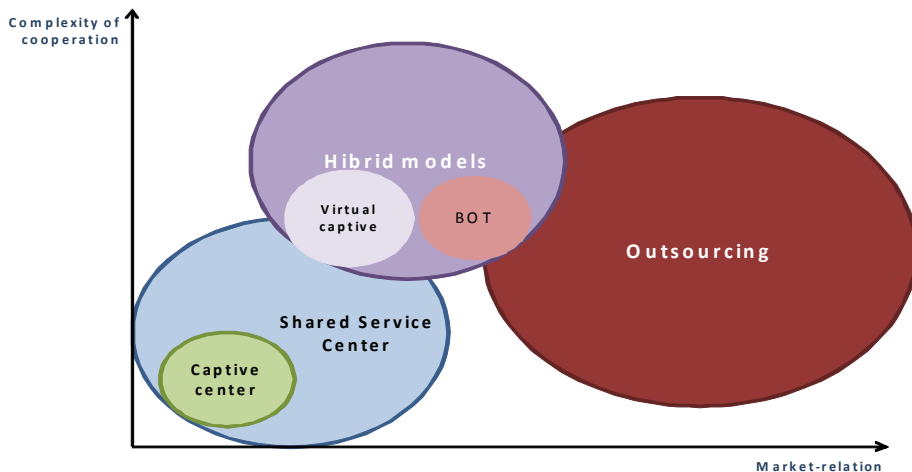
Source: own editing

One of the main results of hybrid solutions is that captive centers and outsourcing providers could see each other not as competitors but partners.

As any management trend has followers and protester so as hybrid models have. According to some researchers (Steer,2007) (Gammage,2010) it is obvious that in the future the thinking of companies will not be determined by choosing between captive center or outsourcing model but ever more apply hybrid solutions. But there are skeptic voices too. These latter researchers (Nikhil,2007) (Verma,2009) deem so that either the pure captive model or the outsourcing, the two ends of the theoretical solutions could be better than the middle-of-the road, the hybrid structures because there are a lot of questions about it. Without the answer for these questions the judgement could be real. One of these key issues whether partnering could counter difficulties that came up during the cooperation or the potential distinctness endangers the partnering in long term. Another question is how customers could evaluate the provider's endorsement. But there are some questions about attrition rates and information security. Could partnering ensure quicker career path than provider or how could prevent the data leak to other customers? It also do not clear how could we share accountability among parties. An outsourcing provider has empowering to improve the service and also do it in favor of its but in case of hybrid solution it is not clear which party has the responsibility. It also could be source of conflict if services have external customers but the center provide it for its own. How could the center make priority and for whom perform first and how.

There are more types of hybrid structures but the most known are BOT and virtual captive center.

Figure 1: Group hybrid models according to market-relation and complexity of cooperation



Source: own editing

In case of BOT (Build-Operate-Transfer) the service was outsourced to a third party but after in advance determined time the service will be bought back and operate in a captive center forward. The essence of BOT is that service customer own the facilities and infrastructure while the provider improves and operates it, employs the staff but do it all only for short term (usually 3-5 years) and after it a hand it over. During the time of agreement the two parties cooperate tightly and control the processes mutually. At the time service transmission the provider will be compensate properly.

The benefits of BOT model could come up mostly when companies think about offshore operations and want to move their functions to a distant, not-known location as India. In these situations it is important that company has to do it alone without helping of any partner or could find one which knows the local market well. This partner could be either a consultant company or an outsourcing provider. Those companies which do not want to outsource their function for good and all but is in the initial part of offshore operation BOT could be ideally.

For the customer this solution could cut the learning curve down, help in functioning without coping with the destination country's regulation, finding the appropriate investment venue and doing the staff recruitment and training. When a company wants to enjoy the benefits of offshoring and rightsizing without of investment risk then this solution could be perfect.

But for the service provider the model could bring important benefits like guaranteed and continuous revenue for a determined term. While the computability is very important for the companies, so if they can achieve it then they could use this safe term to improve other business areas. At the end of agreement the service provider will be compensate for the improving of business and transmission of it fairly. For the outsourcing providers it means an additional business area. But learning opportunity could be also important for the providers. Through the cooperation they can get to know the client's processes, learn how they could contribute and finally how they could improve their own processes on the base of collected experiences. The function of medium term is to make the agreements transparent. According to the experts the shortest agreement time is one year. It is the minimum term that could ensure benefits for both parties.

But not everybody are convinced the unambiguous benefits of BOT. (Aggarwal,2005) It is very hard to attain that both party could share in benefits of cooperation equally. It is also problematic issue the transmission of key employees. The accordingly trained and exercised staff is the key of this industry. And the transmission of it could be dramatic for the providers. Because of it many

times the providers want to convince the customer to choose outsourcing rather than BOT.

The other popular hybrid solution is virtual captive model that alloy the benefits of captive offshoring and outsourcing models. Actually virtual captive model mean such a captive center that is operated by third party accordance with an operational agreement. In case of virtual captive center the customer and the provider make an agreement. The provider ensures - over the relevant services - the assets, IT infrastructure, staff recruitment and training and remains dedicated resources for the customers. The customers keep the control over the processes and technologies that generate captive-like environment. The term came from the cooperation of Wachovia and Genpact that was signed for 7 years in 2005. (Nikhil,2007) Until then several similar agreement has been concluded.

Virtual captive center is the best solution if any traditional model could not satisfy the customer's special needs in appropriate way. Advantages of the model that there is smaller financial risk at the initial investment and local presence and experiences of provider could decrease the time necessity and operational risks of operation improvements. It also ensures bigger flexibility and continuity in human resource, transparent pricing during the agreement time and remain the full managerial control.

This hybrid solution could be rational those medium-sized companies that have not enough experiences or late adopter in outsourcing and so there is lack of maturity or size to establish an own center. But it could be also an important point of view that virtual captive could simplify recruitment and reduce staff attrition if the company name is not well-known in the relevant geographic area. Avoiding the considerable cost of infrastructure and operation is also crucial factor because it could diminish the potential cost-benefits. The virtual captive center could be an exit strategy for those captive centers that are not viable. It is still better to cooperate with a third party provider than operate further a center with irrational costs.

The highlighted two hybrid models were compared according to some points of view in the following table.

Table 2: Comparison of hybrid models

POINTS OF VIEW	VIRTUAL CAPTIVE CENTER	BUILD-OPERATE-TRANSFER (BOT) MODEL
SERVICE DELIVERY	the risk of service-providing are treated in a more cooperative way	providers own the risk of under-performing
PRICING	continuous management of several special cost elements	related to outsourcing market-like pricing
IMAGE	usually under the customer's name	own image
HUMAN RESOURCE	customer have voice in the HR management	provider is responsible for staff recruitment, training and retention
GOVERNANCE	less governance than a traditional captive center but larger than in outsourcing	more simpler and linear governance structure
TERMINATION	customer bear the costs	in case of profound agreement there is clear pricing
OPERATIONAL RISKS	risks and operational loss above a certain level are shared	providers own risks

Source: own edition

Although more of these benefits could attain by BOT and other hybrid solutions but the main asset of virtual captive is the strong customer's control above the offshore operations. The other main difference between the BOT and virtual captive centers is the lack of service transfer after certain, in agreement fore-fixed term. So in this view BOT could realize as a long-term virtual captive center. Although virtual captive center needs a bigger initial expenditure than a pure outsourcing agreement, but it is more cost-effective than a traditional captive center operation.

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