Shaping the Future of the Newspaper
ANALYSING STRATEGIC DEVELOPMENTS AND OPPORTUNITIES IN THE PRESS INDUSTRY

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Outsourcing

Cost savings and the newspaper's core competencies are prime considerations on whether or not to outsource advertising, printing, human resources, editorial, accounting and other roles

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1. Introduction

It seems like the whole corporate world is outsourcing, but is it right for the newspaper industry? Outsourcing has become one of the key tools in the strategic management toolbox since Gary Hamel and C. K. Prahalad developed their well-known idea of "core competency." They showed how important it is to know the one or two key things that your company does better than the competition, and consider letting other companies handle the rest.[1] This followed the Tom Peters and Richard Waterman landmark study of what makes an excellent company. In *Search of Excellence* found there were eight keys to excellence that were shared by all 43 firms and one of those was the "stay-with-the-business-you-know" approach.

But let's be clear about what outsourcing is and isn't. The most prevalent definition of outsourcing is the management and/or day-to-day execution of an entire business function by a third-party service provider. But it has been an over-used term and used erroneously to describe many business strategies. Outsourcing is not offshoring, which is more correctly defined as transferring work to another country. The financial services sector is at the forefront of this strategy with the offshoring of customer services to India. Another tactical strategy often described under the "outsourcing" category is out-tasking, which is more correctly defined as turning over a narrowly-defined segment of business to another business, typically on an annual contract (or sometimes a shorter one) with management still maintaining direct control.

The key element of outsourcing is transferring a significant amount of management control to an external supplier. Control lies at the centre of any outsourcing strategy and managers need to be very clear on the ramifications of shifting control to external suppliers.

Outsourcing also rings alarm bells outside the immediate realm of the corporation.
The familiar headlines such as *30,000 jobs a year go offshore* [2], make difficult reading for

(1) Hamel, G. & Prahalad, C.K. (1990)

(2) PA 25th January, 2006

many of our customer bases while our shareholders may cheer at the potential cost savings and anticipated increase in share value. Forrester, an American research firm, has estimated that by 2015, America is expected to have lost 74,642 legal jobs to poorer countries, and Europe will have 118,712 fewer computer professionals [3].

A poll of 7,300 senior executives for the March 2004 McKinsey Global Business Survey found that most executives think that outsourcing is better for the economy as a whole than for their own companies. The largest discrepancy occurs in North America, particularly in the United States, where the issue has become politically sensitive.

And whereas in the past the job migration was in low-skilled labour, we are now seeing offshoring of high-skilled jobs. The spread of the internet and the dramatic decrease in cost of telecommunications bandwidth enables businesses to outsource much more than low-skilled manufacturing functions. Politicians are equally quick to point out the upside to outsourcing for home industries – U.S. President George W. Bush on his recent India trip repeated a view widely shared by economists, that the benefits from globalization more than offset the damage from lost jobs due to outsourcing. "India's middle class is now estimated at 300 million people," he said. "That's greater than the entire population of the United States. And this middle class is buying air conditioners, kitchen appliances and washing machines – and a lot of them from American companies."

So outsourcing has become more commonly used or "grown-up" as McKinsey says in their February 2005 report [4]. "*When companies first started thinking about farming out nonstrategic functions – such as payroll, IT maintenance, facilities management, and logistics – their goal was to reduce costs. Today, however, these corporations regularly contemplate outsourcing core operations to third-party specialists in order to improve operational performance.*"

Over the past 20 years we've seen the range of outsourced business functions expand from low-skilled manufacturing to high-skilled value-added functions.

However, "grown-up" does not signify that all the problems associated with outsourcing strategies have been identified or learned. McKinsey goes on to say that almost 50 percent of outsourcing arrangements fail to deliver the expected value. That, they conclude, is because few companies have changed the way they make deals and that outsourcing is seen as a procurement procedure based on commodity-influenced purchasing. The reasons companies fail to deliver value are:

• Overestimated economic benefits of the deal

• Failure to establish the right baseline for price negotiations and performance tracking

• Unprepared to manage the transition and post-deal situation.

This concern is echoed in a major global survey conducted by Deloitte, *Calling a Change in the Outsourcing Market*. It found that many of the world's largest organisations that were quick to participate in information technology and business process outsourcing are scrutinising new outsourcing deals more closely, re-negotiating existing agreements, bringing operations back in-house and exploring new alternatives. The study reveals that 70 percent of participants have had significant negative experiences with outsourcing projects and are now exercising much greater caution in approaching outsourcing. One in four participants have brought functions back in-house after realising that they could be addressed more successfully and/or at a lower cost internally, while 44 percent did not see cost savings materialising as a result of outsourcing.

Peter Bars, Outsourcing Advisory Services Partner for Deloitte, said, "often, outsourcing for large companies has not been adding value. Service outsourcing has often failed to deliver on its promises in three key areas – standardisation, cost savings and complexity. There are fundamental differences between product outsourcing and the outsourcing of service functions, differences that were sometimes overlooked but have now come to the fore."[5]

(4) McKinsey Outsourcing Web Report, David Craig and Paul Willmott February 2005

(3) A world of work, *The Economist*, 11th November 2004

(5) Calling a change in the Outsourcing market. The Realities for the World's Largest Organisations. Deloitte, April 2005

Bars continued, "often outsourcing vendors and companies may have conflicting objectives, putting at risk clients' desire for innovation, cost savings and quality. Moreover, the advantages envisioned do not always translate into cheaper, better or faster services."

So if the old world view of outsourcing as a tactical solution for non-essential (or non-core) functions has changed to the view that outsourcing must go beyond short-term cost savings to unlocking long-term value, then how should organisations approach this challenge?

McKinsey states that given the size, the degree of complexity, and the importance of outsourcing deals to a company's overall portfolio strategy, senior executives would be wise to apply the same rigorous approach to these agreements as they would for mergers, divestitures, and joint ventures. Both the customer and the vendor must find the relationship valuable over the longer term. But shared value will also mean shared risk.

If total transfer of assets including people, systems, intellectual poperty, buildings, etc. is the goal then this is divestiture and managers should carefully consider whether this is appropriate – it can be difficult to bring back any of these elements in-house at some later date.

McKinsey advises structuring a deal from a joint-venture perspective where both parties share ownership and control of assets and align incentives to make both benefit from the deal. Short-term focus on the cost-savings can make for ineffective and potentially destructive post-deal management.

Failure to consider the personnel issues such as the transfer of staff to another organisation, roles and responsibilities, and failure to communicate with all levels of management on the objectives of a deal and new structure can seriously undermine any long-term value. And these issues are critical. What is happening with outsourcing is a radical change to business boundaries – not least is the people issue. An employee will suddenly find their employer of many years is now an external supplier and that in turn he/she may be shifted to work on another contract, so where do loyalties lie? And further, is valuable intellectual capital seeping away from the organisation?

Whatever the risks and potential pitfalls, outsourcing is here to stay. The newspaper industry has only recently been tentative in moving into outsourcing what were once considered core competencies such as editorial, advertising and circulation. But the trend is gaining momentum and as the analysis of last year's survey shows there is strong interest amongst newspaper executives on active pursuit of outsourcing opportunities. Looking at case studies from both inside and outside the newspaper industry will show how it's being done and will help newspaper executives to fully consider the possibilities, and importantly, what strategy delivers value in the long term.

2. Case Study

Company: BBC
Location: Worldwide, based in London
Function: HR

Companies have in the past been nervous about outsourcing human resources (HR). Potential candidates will often receive their first impressions of a company's employee relations and management policies through the HR function. Some recruitment companies have issued warnings that an outsourced HR function can cause the industry difficulties in dealing with end users and candidates. In addition businesses may often have to deal with a more fluid, less hierarchical organisation of workers within their own company and a more complex network of managing partners, suppliers and customers.

Recently the BBC's decision to outsource a large part of the HR function and move a number of services on-line has hit the headlines. Through this process the BBC expects to save more than £50m after awarding the firm Capita a 10-year HR outsourcing contract worth around £100m.

The outsourcing supplier, which beat rivals Accenture and Xchanging to the deal, will deliver recruitment, pay administration (excluding pensions), some aspects of staff development, occupational health and a number of other HR-related services. Speaking to *Personnel Today** after the deal was announced, Stephen Dando, director of BBC People, said that Capita emerged as the clear winner after the three suppliers went through a "rigorous evaluation" against 20 criteria, including plans for staff transition, the use of technology and the role of HR.

Anthony Hesketh, director of the centre for performance-led HR at Lancaster University Management School, said choosing Capita was "clear evidence of the BBC sticking to its guns on delivering cost reductions". Dando, who left the BBC to join Reuters as group HR director in April, admitted that cost-cutting was a key driver for the HR outsourcing deal, but insisted it was not the prime factor. "Value for money is a big part of the reality of the

* *Personnel Today* 21st February 2006

BBC and rightly so," he said. "This deal offers substantial savings, but every bit as important is that the deal allows us to re-purpose BBC People as a function that can deliver strategic advantage in the years ahead."

The HR shared-service centre for the new arrangement will be located in Belfast, currently one of the Capita centres for BBC activity. Around 260 BBC jobs will be transferring to Capita and 100 new jobs will be created in Belfast. Stephen Davies, programme director for HR outsourcing at the BBC, said the terms went "well beyond" those required under Transfer of Undertaking (Protection of Employment) Regulations. He said that any staff not wishing to relocate to Belfast would be offered redeployment opportunities at other, nearer, Capita locations.

Fact Box

The Capita Group www.capita.co.uk is the UK's leading professional and support service organisation. Capita was named Best BPO provider 2004 at the inaugural National Outsourcing Association Awards.

Capita Financials (2005)

- Turnover (continuing operations): £1,436 million
- Gross profit (continuing operations): £177.2 million
- Staff: in excess of 25,000

The British Broadcasting Corporation is the state run television company in the UK. It is funded mainly through a licence fee.

BBC financials (2004/2005)

- Group Income: £3,853 million
- Group Operating Deficit: £238 million
- Group employees: in excess of 27,000