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EXPERIENCE MATTERS

What Risk Are You Taking?

Risk management is an important aspect of personal and business life. If you are attempting something for the first time, the risks of costly mistakes or even worse failure, are inevitably higher. The biggest mistake perhaps is is not learning from others who have experience of the challenges you are facing. This is where experience matters.

There are essentially two aspects to risk management in an outsourcing environment:

1. Prior and during the sourcing event
2. Post contract award

Firstly, we should look at 'what is risk?'

"There are risks and costs to action. But they are far less than the long-range risks of comfortable inaction"

John F. Kennedy

Today more than ever before we have seen Risk Management played out in our lives. Governments around the world wrestled to manage COVID19 the best they could. Early on some world leaders even tried to believe the virus didn't exist or was not as dangerous as was being made out, as the death toll rose, those views changed. Then it was a case of balancing risk, 'Lives vs Livelihoods', how much of the restrictions could be lifted, allowing businesses to operate, schools to re-open etc. The success or failure of the decision would be measured by infection rates and sadly the number of deaths.

This is a generic view of what risk is and can be extrapolated into an outsourcing context. Of course, all risk needs to be managed otherwise a risk soon turns into an issue and can become an immediate problem.

There are many definitions of risk management, and some are listed below:

Risk Management is the identification, assessment, and prioritisation of risks followed by an agreed set of actions to minimise, monitor, and control the probability and impact of unfortunate events.

Risk Management's objective is to assure uncertainty does not deviate the endeavour from the business goals.

Source: Wikipedia

The combination of the probability of an event and its consequence. Consequences can range from positive to negative. All organisations have objectives at strategic, tactical and operational levels - anything that makes achieving these objectives uncertain is a risk.

Source: Institute of Risk Management

Risk Management - Prior and during the Sourcing Event

The Chartered Institute of Purchasing and Supply recommends analysing risk using the P.E.S.T. model: Political; Economic; Social; Technological

These are highly relevant factors, as today many outsourced services are delivered using a global delivery model by organisations based all over the world. Each country will have its own risks that can be explored using the above model. Advisors such as Gartner and Forrester will update their view of the P.E.S.T. landscape on a regular basis, depending on world events.

P.E.S.T. Model – Examples of Outsourcing Considerations

Political • Political stability • Government policy • Trading conditions • Employment law • Tax law • Environmental conditions • Wars or conflicts	**Economic** • Economic trends • Exchange rates • Inflation rate • Growth rate • Interest rate • Specific Industry factors
Social • Human rights • Male and female equality • Employment rights • Health and Safety • Social conditions • Ethical issues • Language	**Technological** • Rate of technology change • Global communications • Infrastructure • Innovation • Maturity of market and service offering • IPR law

As the world changes at an increasingly fast rate, risk should be established at the time of the sourcing event and reviewed regularly during the term of the contract.

Risk Management – Post Award

There are many categories of risk, post award, however there seems to be a consensus with regard to the most common. The table below identifies what many consider to be the top eight outsourcing risks. To effectively manage these risks the key is to make sure the governance of the outsourcing environment is such that capturing the risk is straightforward and presented to the appropriate part of the organisation who can take steps to mitigate the risk occurring. Management of a single risk register is crucial, there may be different classifications of risk, and a single version of the truth provides the most effective overall control.

Risk Categorisation	**Description of Risk**
Commercial/ Financial	All risks are important, however one of the most important is commercial / financial risk; quite simply where the outsourcing deal does not deliver the required/forecast savings. This can occur with over-stated savings or unexpected hidden costs. Also, currency fluctuations should be guarded against where possible.
Loss of Business Knowledge	Some IT organisations are guilty of 'over outsourcing'. Typically, too many roles are outsourced, leaving the business exposed to over reliance on supplier knowledge. This is particularly true with regard to the Business Analyst role.
Process Capability Gap	Many organisations are not as advanced in process maturity as the global IT service providers, who can boast top-level certification in CMM, Six-Sigma and ISO standards. There is a risk that the client organisation, due to its own lack of process discipline, will not achieve the possible cost savings.
Change Requests	Quote low, win the business and make up the difference and more, with change requests. Certainly, this is an approach adopted by some organisations over the years, which is why it is so important for the client to ensure that the scope of the original outsource is fully understood and that assumptions/out of scope statements as stated in the supplier's tender response are subjected to impact assessment.
Delivery Failure	'Under promise and over deliver' has always been my approach to life, but unfortunately the supplier community does not always adopt this strategy. They can be guilty of making delivery claims in their sales pitch, which they cannot possibly achieve. The client suffers when SLA's are not met and the service delivery is not of the required standard. The client needs to fully assess the impact of supplier failure and the resultant challenges it gives the business.
Culture	This risk is less important today than it was 10–15 years ago, as the outsourcing industry continues to mature around the world. However there are still cultural issues with the companies based outside Europe/US. It is important that the client is mindful of these and takes effective steps to manage the risk.
Regulation	Regulation is an increasing aspect of business life especially following the financial crisis of 2008, however regulation also applies to utilities and other sectors. In recent years regulation has proliferated to address risks around for example information security, resilience and increasingly the ESG agenda (environmental, societal and governance) Demonstrating accountability and transparency are key aspects of this potential risk.
Key Personnel	This was a significant issue/risk, particularly in India, in the boom times of 2004–2007. People were switching employers on a regular basis, chasing salaries being offered mainly by the MNCs. Whilst this practice has since calmed down, it is important to recognise that you may have some key supplier employees servicing your account and you should make sure the contract monitors and controls Key Personnel Turnover. However, do not lose sight of the fact it is down to the service provider to manage their resources in an outcome based service.

Questions for Outsourcing Decision Makers

1. *How does our organization ensure a comprehensive risk assessment is conducted prior to and during the sourcing event to identify potential risks associated with political, economic, social, and technological factors in the global outsourcing landscape?*

2. In light of the post-award risk categories identified in the article, how can we establish a robust governance structure to capture, monitor, and address risks effectively, ensuring a single version of truth for risk management across the outsourcing environment?

3. To mitigate the risk of over-reliance on supplier knowledge and ensure a smooth transition during outsourcing, how can our organization strike the right balance between outsourcing roles and retaining critical business knowledge in-house, especially in areas like business analysis and process capability?

If you want to discuss these questions, or any other outsourcing challenges please do email us at experiencematters@ascea.co.uk and we can set up a call with you.

This article has only summarised many of the key aspects of Risk Management. Ian Hucker has written a short book; IT Outsourcing – A Practical Guide to Risk Management, details of which are below