The standardization myth: the truth about knowledge management in offshore service delivery

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Think business process offshoring and the imagery is usually one of standardized, routine activities that can be well documented. While this may well have been true in the past, that era is now officially over. In a recently completed study, we found that the offshoring industry has evolved to the point that on average, whether a process is standardized or not matters little for its being offshored successfully- what matters is whether the links to other processes are standardized or not. We also found some very interesting solutions in use by companies to deal effectively with the cases when these links were not standardized.

Our study is based on a survey of offshored business processes executed from India, augmented with interviews of several managers both from the client and vendor firms. We statistically analysed data on a 127 offshoring projects involving call centres, IT maintenance and back office services. The survey respondents were managers responsible for transitioning the process and for day-to-day operation in steady state.

Our analysis revealed that there are two key knowledge management problems that arise in the offshoring of services. When moving a software maintenance process from London to Bangalore, for instance, not only must the Indian employees learn to do what the maintenance engineers in London were doing (the knowledge replication problem), but also how to connect with other employees in London whose work is interdependent with software maintenance – such as the software users (the coordination problem). When processes are standardized and documented, knowledge replication is easier; when the links between processes (such as hand-offs and specs) are standardized, coordination is easier.

The following schematic clarifies the difference between the knowledge replication problem and the coordination problem. Knowledge replication effort deals with ensuring that the offshore personnel know how to execute the process. Unsurprisingly, knowledge replication effort is minimized when process knowledge is standardized and well documented, rather than left largely tacit and unarticulated in the minds of the employees currently executing the process. ¹

¹ Also see Gabriel Szulanski and Sidney Winter’s “Getting it right the second time”, HBR January 2002.
Coordination, on the other hand, pertains to how the focal process interacts with its surroundings. Coordination effort is likely to be minimized when interactions between the process and its surroundings are accomplished easily. When collocated, such interactions are often ad-hoc and done face-to-face, particularly when exceptions were encountered. When sharing physical space, ad-hoc face-to-face interaction is the cheapest and easiest means to achieve coordination. However, such problem-solving by walking over to the next cubicle is not possible when the process is offshored. Coordination across geographic distance is therefore easier when links between processes are minimized, standardized and well documented. At one extreme, a fully black-boxed process has few linkages and generates few coordination challenges when offshored. At the other extreme, tightly linked processes with non-standardized interaction patterns make ongoing coordination both necessary and particularly challenging because it must occur across geographies.

While both knowledge replication and coordination related challenges can create significant organizational overhead, and may eat up between 15 - 25% of the gains from wage arbitrage in offshoring\(^2\), we found that the current state of the industry is such that coordination related problems are the critical ones. Most firms in our sample had extensive transition/migration processes and on average seemed to have learnt how to deal with knowledge replication issues fairly effectively, even when the processes were not very standardized. The knowledge replication strategies we observed included offshore personnel closely observing current process experts at work and working under their supervision for some time, efforts in process mapping and documentation, and occasionally tests and exams to determine the level of understanding of offshore personnel.

However, we also found that firms continued to face significant challenges in dealing with coordination problems. While process standardization did not impact process performance post-offshoring, a one standard deviation decrease in standardization of linkages resulted in a decrease in post-offshoring performance by 0.2 standard deviation.

The study’s results have broader implications for what is potentially “offshore-able”. Many think that offshoring is pertinent to “routinized and standardized” tasks- in

\(^2\) “Offshoring: is it a win-win game” by McKinsey global institute, 2003
which knowledge can be replicated easily, and that “high value added creative (non) standardized work” is immune to offshoring. However, industry practice seems to have evolved towards dealing with knowledge replication issues quite effectively, so that the lack of standardization no longer poses the critical hurdle to offshoring. Indeed the movement of jobs such as asset pricing, equity research and contract R&D demonstrate this quite clearly. In the near future, concerns about knowledge replication may in fact become moot as the off-shoring of services begins to move away from a model of “service delivery” towards “content development”, where the client cares about the outcomes, not about high fidelity replication of how processes used to be run onshore. As the industry moves in this direction, we expect that the problem of ensuring ongoing coordination will gain prominence. Both clients and vendors will need to change their emphasis on how to select processes for offshoring, as well as how to manage offshored processes.

In our research, we also observed substantial variation across projects in their effectiveness at managing coordination between onshore and offshore locations. After controlling for process characteristics such as size, type, standardization etc., we found that the best offshored process performance was almost four times better than the worst process performance.

We found companies using two generic strategies to manage the challenge of ongoing coordination: separation and integration. A separation strategy involves investment (before offshoring) in black-boxing, in order to redesign the processes such that the offshore and onsite locations have minimal interactions. In contrast the integration strategy involves facilitating interactions between the onsite and offshore locations in a manner that attempts to overcome the constraints posed by distance. Within the integration strategy, there are also two clearly different approaches possible. The first places emphasis on facilitating communication across locations using IT tools such as email, telephone and video-conferencing. The second, interestingly places less emphasis on building communication channels, and more on building “common ground”- shared understanding across locations by means such as shared decision making procedures, shared vocabulary and the ability to observe work in progress across locations. Such common ground appears to help onsite and offshore employees coordinate without the need for extensive communication- minimizing the use of videoconferencing and travel.
Our statistical analysis suggest that while each of the coordination strategies we discussed above—black-boxing, communication channels and common ground—are useful, surprisingly the relatively “low tech” mechanisms for building common ground—such as having standardized decision making procedures, ability to inspect work in progress and having a common vocabulary may be the most effective. While these are not technology intensive solutions, this does not mean they are easy. Obstacles to the creation of common ground include a lack of transparency of decision making procedures across locations, the absence of uniform work environments (eg. technologies, software, platforms), an over-emphasis on cultural differences and under emphasis on cultural similarities, and over-reliance on communication using email and telephone without making taking efforts at building a basis of shared understanding (such as through the creation of opportunities for individuals to get to know each other).

If anything, our results suggest that firms in our sample tend to over-invest in conventional communication channels and could do better by investing more in building common ground. The resulting economies in terms of minimizing costly IT investments and lower travel are obvious. The “soft factors” underlying mutual understanding and a shared world view among onsite/offshore personnel may in fact have fairly “hard” economic consequences by limiting the need for travel and avoiding costly coordination failures.