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**Julie Beardsell**

**Managing culture as critical success factor in  
outsourcing**



***“I do not want my house to be walled in on all sides and my windows to be stuffed. I want the cultures of all the lands to be blown about my house as freely as possible. But I refuse to be blown off my feet by any.”***

**Mahatma Gandhi, 1921**

## ABSTRACT

Outsourcing was originally confined to peripheral business functions and mainly motivated by a cost saving logic, but has now developed into a routine strategic management business model that affects not only peripheral functions but impacts the core business of organizations. Industry research typically indicates that over 50% of firms believe that organizational culture fit is a key criterion in the selection of vendors for outsourcing; showing the need for outsource service vendors to become partners with their customers and to become an extension of them.

This paper explores the cultural paradigm for the strategic outsourcing of IT and business processes, exploring the impact that culture plays as an inevitable influencing factor in the global IT services landscape. The author supports the hypothesis that a cultural match between the firm and its vendors is critical to success in outsourcing and makes recommendations for further research in this field.

## JEL CLASSIFICATIONS

- D23 MICROECONOMICS  
Production and organizations – organizational behavior
- F16 INTERNATIONAL ECONOMICS  
Trade – trade and labor market interactions
- J22 LABOUR AND DEMOGRAPHIC ECONOMICS  
Demand and supply of labor – time allocation and labor supply
- J24 LABOUR AND DEMOGRAPHIC ECONOMICS  
Demand and supply of labor – human capital; skills
- L14 INDUSTRIAL ORGANIZATION  
Market structure, firm strategy, and market performance – transactional relationships; contracts and reputation; networks
- M14 BUSINESS ADMINISTRATION AND BUSINESS ECONOMICS  
Business administration – corporate culture
- M15 BUSINESS ADMINISTRATION AND BUSINESS ECONOMICS  
Business administration – IT management
- M54 BUSINESS ADMINISTRATION AND BUSINESS ECONOMICS  
Personnel economics – labor management
- O31 ECONOMIC DEVELOPMENT, TECHNOLOGICAL CHANGE, AND GROWTH  
Technological change; research and development – innovation and invention: processes and incentives
- O32 ECONOMIC DEVELOPMENT, TECHNOLOGICAL CHANGE, AND GROWTH  
Technological change; research and development – management of technological innovation and R&D

## ABOUT THE AUTHOR



**Julie Beardsell** has 20 years' experience in diverse business and technology-related fields, ten years of which have been gained at Europe's top international IT services providers where she specializes in leading large and strategic international outsourcing and client engagements. Julie is holder of a Master of Philosophy Business Research Degree (MPhil) from Northumbria University Business School and has a Teacher Certificate in Education from Portsmouth University, UK. She is in the final stage of completion of her Doctorate in Business Administration at Swiss Management Center University and is author of several publications.

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## INTRODUCTION

Culture is not a new phenomenon in business and there are few firms that work with people from only one culture. At the shallowest level, most Western businesses (even those based in one location) employ people from many cultural backgrounds. As Mahatma Gandhi (1921) stated, “I do not want my house to be walled in on all sides and my windows to be stuffed. I want the cultures of all the lands to be blown about my house as freely as possible. But I refuse to be blown off my feet by any.” Gandhi was not a *business* leader, yet he demonstrated ‘mastery’ in the art of *leadership*; his competencies being often very modest and effortless or so natural as to seem inconsequential at the time. Mahatma Gandhi was gentle, used no force, and yet showed us how not resisting could be a powerful force for change. His mastery did not even seem to be leadership for most of his career and yet from the beginning he was pursuing the creation of a new reality.

The new reality is that firms see the global financial crisis as an opportunity for change. Business models, such as outsourcing the management of information and communications technology (ICT) and business processes (BPO), provide a potentially powerful solution to achieve such change. Business drivers include concern for cost and quality, lagging technological performance, supplier pressure, access to special technical and application skills, and the need for innovation in the firm’s IT, service or product domains. Although the mix of factors driving the business case for outsourcing varies widely from one firm to another, a number of typical characteristics can be identified.

Firstly, the CXO’s concerns about cost, is a factor that drives the need to procure existing services for a reduced price without compromising quality. Secondly, failure to meet service standards or regulatory standards can force management to find other ways of achieving reliability and transparency particularly in out-of-control situations which the current IT department could not recover from. Thirdly, a firm under intense competitive pressure, which does not consider IT as its core competence, may find outsourcing as a way to delegate time-consuming, messy problems so it can focus scarce management time and energy on its core business, enabling it to better differentiate itself in the market. Fourthly, financial drivers such as liquidating the firm’s intangible IT asset, thus strengthening the balance sheet and avoiding a stream of sporadic capital investments in the future

can also be a driver, whereby outsourcing can turn a largely fixed-cost business into one with variable costs, which is especially important for firms whose activities vary widely in volume from one year to another or which face significant downsizing. Finally, outsourcing can transform the firm, enabling innovation through rapid funding of new systems development, new business models and new products and technologies. An outside vendor may be better positioned to provide the necessary innovative services, through its innovation culture and existing track record and credentials of delivering to other clients.

It is known that culture is a higher critical success factor in outsourcing than price, yet few business leaders give attention to cultural differences. Perhaps this is due to the relative intangibility of this subject. The consequences of such lack of attention are potentially disastrous for firms searching for cost-effective solutions for business innovation as their expectations of vendors will remain unmet and their ability to focus on core business processes and driving innovation in “what they do best“ will be hindered, ultimately resulting in loss of market share to those businesses who are better equipped to manage the cultural turbines that drive the winds of change across the global business landscape.

At a deeper level, the impact of globalization and labor cost differences between regions such as China and the United States of America means that many organizations either outsource parts of their business or are themselves outsourcing partners for other businesses in other parts of the world.

## PART I: Cultural dimension in outsourcing

### *What do we mean by culture?*

Culture (from the Latin *cultura* stemming from *colere*, meaning "to cultivate")<sup>1</sup> is a term that has different meanings. For example, in 1952, Alfred Kroeber and Clyde Kluckhohn compiled a list of 164 definitions of "culture" in *Culture: A Critical Review of Concepts and Definitions*<sup>2</sup>. However, the word "culture" is most commonly used in three basic senses:

1. excellence of taste in the fine arts and humanities, also known as high culture
2. an integrated pattern of human knowledge, belief, and behavior that depends upon the capacity for symbolic thought and social learning
3. the set of shared attitudes, values, goals, and practices that characterizes an institution, organization or group.

The term has evolved over the centuries and differs in meaning depending on the discipline such as sociology, cultural studies, organizational psychology and management studies. The third definition, listed above, is most relevant to the nature of culture in today's business organizations and most closely represents the nature of the "culture" referred to in this paper.

"Culture" in general is concerned with beliefs and values on the basis of which people interpret experiences and behave, individually, in groups and characterizes an organization. Cultures in business organizations are often referred to as "corporate cultures".

"Corporate culture" is one of those amorphous business concepts that leaders too often neglect because of its sheer intangibility. Yet culture, an effective culture, is arguably the most valuable intangible asset a company can own. It is known that partner expertise, collaboration and culture are higher critical success factors in outsourcing than price. Many firms today consider innovation to be

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<sup>1</sup> Harper, Douglas (2001). Online Etymology Dictionary.

<sup>2</sup> Kroeber, A.L. & Kluckhohn, C. (1952). *Culture: A Critical Review of Concepts and Definitions*. Vintage Books. New York.

highly important. Innovation is embedded in an organization's culture and is more successful in specific types of organizations than others. Culture unifies people's behavior, whether it be the kind of culture that results from a shared geographical or spiritual context such as may be found in India or in Hinduism, or the culture that results from a "way of working" established by such leading corporations such as IBM or Apple. Conversely, culture may also create barriers between people, thus nowadays, innovation faces the consequences of culture in a number of ways, particularly in terms of how people's beliefs and behavior can contribute or block the process of developing and implementing new ideas. Culture affects innovation because it shapes the patterns dealing with novelty, individual initiatives and collective actions, and understandings and behaviors in regard to risks as well as opportunities.

Culture is the very organization's DNA. It can be considered the firm's genes, personality, norms and values that often aren't captured formally in documents or processes. Yet culture is the cement that holds an organization together. It is the behavior that results when a group arrives at a set of - generally unspoken and unwritten - rules for working together – and such rules can be especially influenced by the organization's founder, executives, and other managerial staff because of their role in decision making and strategic direction. It is typically represented in groups through language, decision making, symbols, stories and daily work practices.

### ***Culture applied to outsourcing***

Outsourcing, in its simplicity, is concerned with a relationship developed between a client firm and a vendor or multiple vendors. Outsourcing can be characterized as an inter-organizational relationship (IOR) since two parties from different organizations work together and these organizations may have very different corporate cultures. Various theories and frameworks of IORs have been utilized in organizational economics, organizational theory, strategic alliance, and relationship marketing literature.

In the outsourcing of IT services, what generally takes place is a 'transition' from a human resource perspective in which a group of employees are divided up in split, which is typically three ways:

1. The IT staff that transfer to the IT services vendor.
2. The staff that remain behind at the demand-side organization.
3. The staff who are the users of the service.

This 'transition' is shortly followed by a 'transformation' whereby elements of the IT service are supplied by offshore staff from locations such as India, the Philippines or Suriname, where labor costs remain low compared to the costs of staff in Europe and the US.

The dividing up of such an organization, at best, can cause uncertainty for those directly affected, and at worst, can cause staff to seek employment elsewhere. In addition, it is often the case that a proportion of the staff to be transferred to the vendor are 'external' hires and due to the higher 'tariffs' that they can earn, such staff are the first to be replaced by staff from the vendor organization in an effort to reduce overheads, whilst ensuring that sufficient customer knowledge is 'captured' for satisfactory execution of the service contract.

Many companies that have gone through large scale outsourcing exercises towards the turn of the century, are finding that their flexibility is not as enhanced and that service levels have not improved to the extent that was expected. The problem for IT services providers is that in their efforts to manage the operational challenges that face them in delivering to the outsourcing contract, there is limited focus on the core and individual competencies required to shift the 'arranged marriage' away from the letters of the agreement, towards the entrepreneurial business partnership which was the intention of the two strategic partners when committing to the arrangement in the first place.

One of India's well-known firms doing outsourced work from America, Satyam Computer Services, is an example of how such a cultural blend is key, supplying services to its US clients via a supply chain sourced from Indian villages supporting businesses in Indian cities specializing in business process outsourced (BPO) services include the handling of US employee records.

In outsourcing, a feeling of intense disorientation can take place in the form of 'culture shock' or 'culture mismatch', which can occur at any stage of an outsourcing engagement, as early as shaping an outsourcing opportunity, through to the execution of the services defined in the contract, in which

parties from such countries as China, Ireland and The Netherlands might find themselves working together in a multi-vendor stakeholder relationship. There is an increasing need for those who interact with firms and individuals from other cultures to capture and assimilate information quickly in order to make valid and reliable decisions that are timely.

Contrast the sort of corporate culture of a large international financial services establishment, such as a major bank which has to be the antithesis of an older, more established culture, compared to that of an IT services provider; the latter being typically fast-moving, dynamic and fluid, and having highly adaptable structures designed to change rapidly as new customer demands arise. Unless an outsource firm has a history and previous existence before it became a service provider, its culture is by design less well-defined and embedded within the organization.

The potential for a clash of these two cultures is clear. If an outsourcing vendor and a prospective client company do not “walk and talk” the same cultural language from the beginning of the relationship, the two organizations end up working at cross purposes; the outsourcing firm doesn't fit into the corporate environment and the corporate environment can't work with the culture that the outsource firm brings to the client.

### ***The macro perspective***

Let's now briefly take a look at culture from the 'macro' perspective of globalization, what Friedman (2006)<sup>3</sup> aptly calls 'glocalization', being globalization of the local. Culture can be viewed in terms of how outward it is – the degree to which it is open to foreign influences and ideas; and conversely, in terms of how inward it is – the degree to which there is a sense of national solidarity and a focus on development and trust within the society for strangers to collaborate together.

The more a culture is at ease with absorbing global cultural influences, then the more easily it can benefit from global best practices by blending these with its own traditions. The fact that individuals in such nations as India and China can innovate without having to emigrate to the West, helps to

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<sup>3</sup> Friedman, T.L. (2006). *The World is Flat*. London: Penguin Books.

preserve the local culture, even though such individuals are likely to learn to speak English with an American accent, enjoy eating at a MacDonald restaurant in the shopping malls of New Delhi and wearing designer jeans and trainers instead of traditional Indian clothing such as a dhoti and kurta.

Indians and Chinese are increasingly demanding better products and services at affordable prices. It was not so long ago that 'Made in Japan' was synonymous with cheap quality, the question is to what extent 'Made in China' and 'Made in India' can make the shift in focus from low-cost production and copying to a focus on low-cost innovation of their own. As US companies send knowledge and work to India, it will only be a matter of time before Indian companies create a turn around and start using their earnings and knowledge to invent new products and services that poorer Indians can use to lift themselves out of poverty into the middle class, thus 'enjoying' the benefits of middle-class American products on Indian soil. We are already seeing such examples in the production of cheap Indian made cars targeting poorer Indians.

Thanks to Internet and the 'download culture', satellite and TV through which the media makes available content from all major cultures to homes across the globe, particularization now seems to be as strong as homogenization. So global is only really interesting, if it 'absorbs' local culture. Each culture can add its own flavor to a single phenomena, for example, if we take a flat piece of dough called pizza, then in Japan one can find sushi pizza, in Bangkok we can find Thai pizza and in Indonesia, pizza ayam.

When China scrapped its intolerant form of communism, then the more tolerant 'laissez-faire' approach provided a positive environment for commercial and industrial prosperity. Similarly, India, when left to its own devices, prospers through its Hindu religion which teaches about the value of tolerance. Such tolerance is a crucial factor in effective collaboration between organizations.

### ***Avoiding the outsourcing 'Titanic'***

Cultures are not wired into our human DNA, but are a product of the context – geography, education level, leadership, and historical experience of society. Culture is influenced by these factors and can change, as seen so vividly in the cases of Japan and Germany which went from highly militarized

societies to highly pacifist and democratic societies during the past half century. Consider the differences in culture between Muslim Spain; which has historically exercised extreme tolerance; and Muslim Saudi Arabia, which is one of the most intolerant societies. U.S. companies can experience a culture shock of sorts when working with Indian employees educated and trained there, and often American businesses don't immediately enjoy the expected benefits of an offshore engagement. The reason isn't a lack of motivation, intelligence or effort on behalf of India-based workers. In fact, analysts say Indian workers are extremely ambitious and often job hop for more pay, causing the attrition problems many offshore providers are currently experiencing. Instead U.S companies run into management problems due to a deep cultural divide between North American-based businesses and the Indian talent pool.

Indian culture often calls for putting relationships before business. Typically, Americans meet and "get right down to business" and discuss more personal topics when business is finished -- which often doesn't happen because there is another business function that becomes more critical to the U.S. worker. But a traditional Indian gathering of managers and employees or business partners might put more emphasis on the interpersonal relationships upfront and address business as a secondary priority.

The most powerful elements of culture are those that lie beneath the surface of everyday interaction and it is often these 'unseen' elements that are underlying factors in cultural clashes. These elements are called 'value orientations'. Value orientations are preferences for certain outcomes over others; e.g., private space over public space, deductive thinking over inductive thinking, and so on. All of these are key components in our individual and national identities. Yet the danger of collision is in what's below the water's surface. This is illustrated in the Iceberg Model seen below.

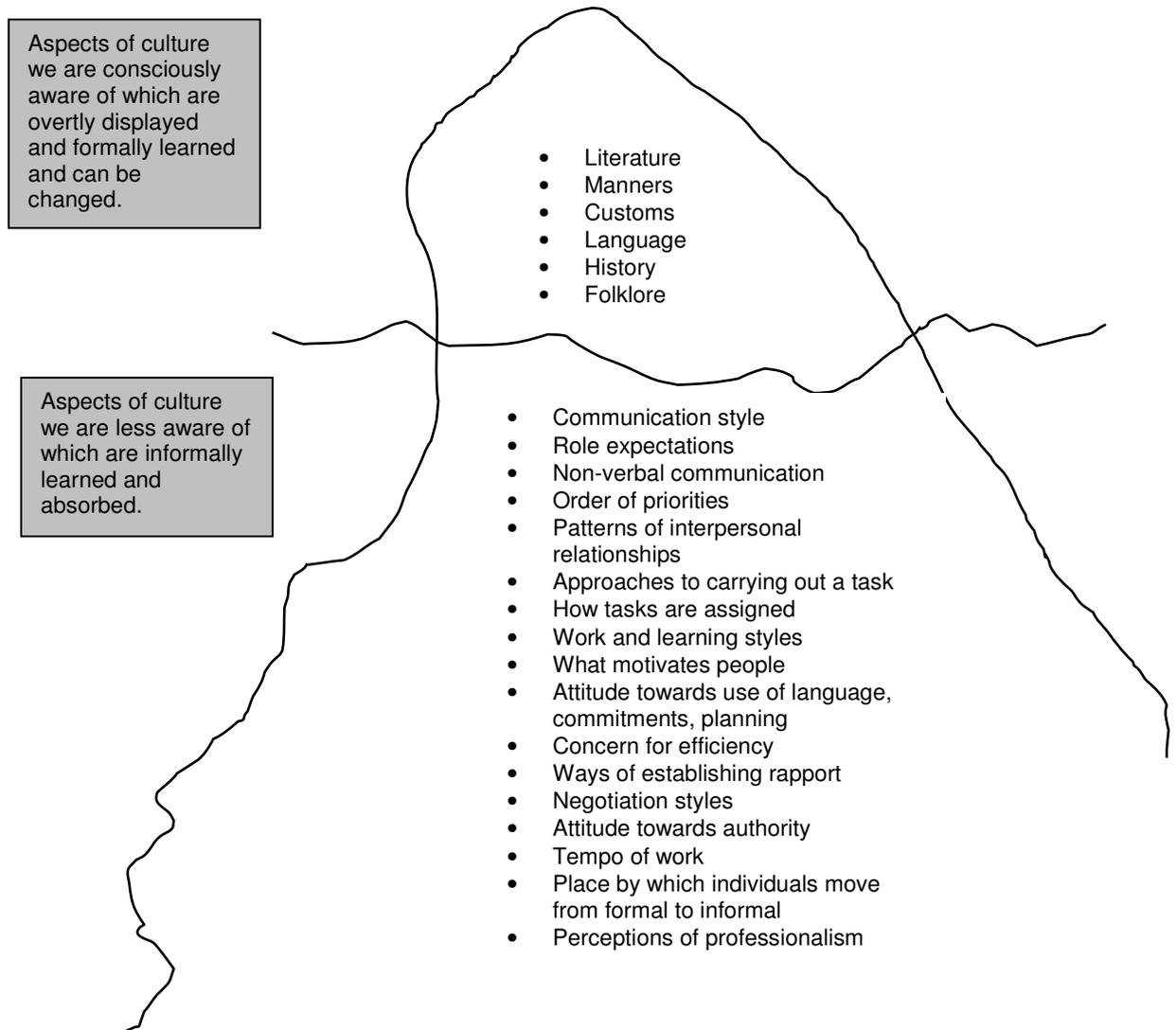


Figure 1: Iceberg Model of Culture

### ***Dimensions of cultural differences***

Geert Hofstede (1980)<sup>4</sup> conducted surveys beginning in 1980 of more than 60,000 IBM employees in at least 40 countries, to develop four dimensions of cultural differences:

<sup>4</sup> Hofstede, G. (1980). *Culture's Consequences: International differences in work-related values*. Thousand Oaks, California, USA: Sage Publications.

1. Power Distance Index (PDI) focuses on the degree of equality, or inequality, between people in the country's society. A High Power Distance ranking indicates that inequalities of power and wealth have been allowed to grow within the society. These societies are more likely to follow a caste system that does not allow significant upward mobility of its citizens. A Low Power Distance ranking indicates the society de-emphasizes the differences between citizen's power and wealth. In these societies equality and opportunity for everyone is stressed.
2. Individualism (IDV) focuses on the degree the society reinforces individual or collective, achievement and interpersonal relationships. A High Individualism ranking indicates that individuality and individual rights are paramount within the society. Individuals in these societies may tend to form a larger number of looser relationships. A Low Individualism ranking typifies societies of a more collectivist nature with close ties between individuals. These cultures reinforce extended families and collectives where everyone takes responsibility for fellow members of their group.
3. Masculinity (MAS) focuses on the degree the society reinforces, or does not reinforce, the traditional masculine work role model of male achievement, control, and power. A High Masculinity ranking indicates the country experiences a high degree of gender differentiation. In these cultures, males dominate a significant portion of the society and power structure, with females being controlled by male domination. A Low Masculinity ranking indicates the country has a low level of differentiation and discrimination between genders. In these cultures, females are treated equally to males in all aspects of the society.
4. Uncertainty Avoidance Index (UAI) focuses on the level of tolerance for uncertainty and ambiguity within the society - i.e. unstructured situations. A High Uncertainty Avoidance ranking indicates the country has a low tolerance for uncertainty and ambiguity. This creates a rule-oriented society that institutes laws, rules, regulations, and controls in order to reduce the amount of uncertainty. A Low Uncertainty Avoidance ranking indicates the country has less concern about ambiguity and uncertainty and has more tolerance for a variety of opinions. This is reflected in a society that is less rule-oriented, more readily accepts change, and takes more and greater risks.

A fifth dimension was added later based on a questionnaire designed by Chinese scholars:

5. Long-Term Orientation (LTO) focuses on the degree the society embraces, or does not embrace long-term devotion to traditional, forward thinking values. High Long-Term Orientation ranking indicates the country prescribes to the values of long-term commitments and respect for tradition. This is thought to support a strong work ethic where long-term rewards are expected as a result of today's hard work. However, business may take longer to develop in this society, particularly for an "outsider". A Low Long-Term Orientation ranking indicates the country does not reinforce the concept of long-term, traditional orientation. In this culture, change can occur more rapidly as long-term traditions and commitments do not become impediments to change.

Recently, corporate culture has been acknowledged to be a significant determinant of organizational behavior and performance. The press and the mass media often make references to a specific corporation's culture, such as the HP Philosophy, the IBM Way, and 3M Value, and attribute each company's competitive advantage to its culture. Furthermore, several books and various case studies have focused on corporate culture to explain how it works, how it changes and evolves, and how it influences behavior and corporate performance, for example, Deal and Kennedy (1982)<sup>5</sup>, Schein (1985)<sup>6</sup> and Collins and Porras (1994)<sup>7</sup>.

There are a few exceptional works such as Denison (1984)<sup>8</sup>, Gordon and DiTomaso (1992)<sup>9</sup>, Kotter and Heskett (1992)<sup>10</sup>, and Sorensen (2002)<sup>11</sup> which report that corporate culture and cultural strength are associated with superior performance.

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<sup>5</sup> Deal, T., & Kennedy, A. (1982), *Corporate Cultures*. Addison-Wesley: Reading, MA.

<sup>6</sup> Schein, E.H. (1985). *Organizational Culture and Leadership*. San Francisco: Jossey-Bass Publishers.

<sup>7</sup> Collins, J.C., & Porras, J.I. (1996, September-October). Building Your Company's Vision. *Harvard Business Review*. Massachusetts: Harvard Business School Publishing.

<sup>8</sup> Denison, D.R. (1984). Bringing Corporate Culture to the Bottom Line. *Organizational Dynamics* 13, 5-22.

<sup>9</sup> Gordon, G. G., & DiTomaso, N. (1992). Predicting Corporate Performance from Organizational Culture. *Journal of Management Studies* 29, 783-798.

<sup>10</sup> Kotter, J.P., & Heskett, J.L. (1992), *Corporate Culture and Performance*. New York: Free Press.

<sup>11</sup> Sorensen, J.B. (2002). The Strength of Corporate Culture and the Reliability of Firm Performance. *Administrative Science Quarterly*, 47, 70-91.

Firm-specific capital, which is also called 'organizational capital', is an asset specific to and embedded into an organization, and includes employees' skills and know-how that have use only within a particular firm, information on each employee's aptitude for a particular job, experience in coordinating diverse production technologies, and the goodwill of customers. Firm-specific capital usually has the following characteristics: it is a productive resource unique to a particular firm and not transferable to other firms; it ceases to be productive when the firm is dissolved; and according to Iwai (2002)<sup>12</sup> and Lev and Radhakrishnan (2005)<sup>13</sup> it is accumulated through investment. Corporate culture has these three characteristics of firm-specific capital; it is hard to imitate; it disappears with the demise of an organization; and it is accumulated through the learning and education of employees.

If we regard corporate culture to be firm-specific capital and valuable in enhancing performance, we can assume that strong-culture firms have an incentive to maintain and utilize the culture rather than build a new (different) culture. Preserving corporate culture and sustaining the organization in which the culture is embedded can increase the firm's value via two effects. First, it raises current performance. The firm takes advantage of its accumulated culture to operate efficiently. Second, it improves future performance. Observing that the culture and the organization continue to exist, the employees are encouraged to make culture-specific investments which facilitate further accumulation of organizational capital.

Therefore, strong-culture firms can be assumed to adopt policies that preserve the culture and the organization, and maximize the benefits emanating from the culture. In large IT services firms, the culture of the company can be weak and very difficult to characterize, due to the fact that the firm has grown through taking over IT staff from other organizations as a result of large outsourcing deals. In such cases, there is typically no common cultural blood group, but a mix of subcultures.

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<sup>12</sup> Iwai, K. (2002). The Nature of the Business Corporation: Its Legal Structure and Economic Functions. *Japanese Economic Review*, 53, 243-273.

<sup>13</sup> Lev, B., & Radhakrishnan, S. (2005). The Valuation of Organization Capital. Corrado, C., Haltiwanger, J. & Sichel, D. (eds). *Measuring Capital in the New Economy*, 73-99. The University of Chicago Press, Chicago.

## PART II: Cultural understanding through leadership and holistic approaches

### *The cultural web*

The stronger an organizational culture, the greater the impact it can have on behavior; however, the stronger the culture, the more difficult it is to change. Unfortunately, the environment changes, and values that fit the environment today may be inappropriate tomorrow. What can an organization do to keep the positive aspects of a strong culture and still reduce the risk of becoming extinct by not changing its culture fast enough to accommodate environmental shifts?

Cultural change is a form of organizational transformation, that is, radical and fundamental form of change as it involves changing the basic values, norms and beliefs, among members of the organization in order to improve organizational performance. Keeping the positive aspects of a strong culture or “the way we do things around here” requires a change approach. The most important change often needs to come from an organization’s leaders. A useful tool for understanding culture is the ‘Cultural Web’ developed by Johnson and Scholes.

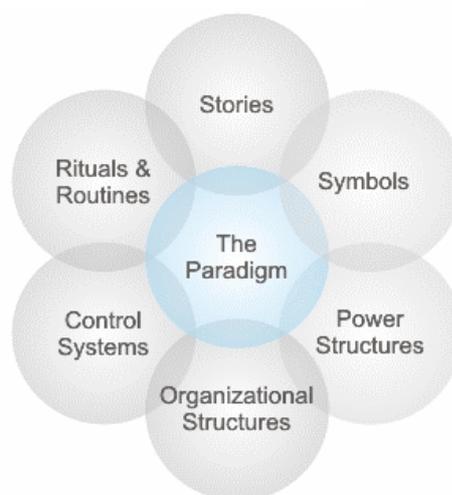


Figure II: The Cultural Web (Johnson and Scholes)

In the cultural web, culture is described as the mix of routines and rituals, stories, symbols, control systems, power structures and organizational structure that form the paradigm of the organization.

1. Stories – The past events and people talked about inside and outside the company. Who and what the company chooses to immortalize says a great deal about what it values, and perceives as great behavior.
2. Rituals and Routines – The daily behavior and actions of people that signal acceptable behavior. This determines what is expected to happen in given situations, and what management values.
3. Symbols – The visual representations of the company including logos, how plush the offices are, and the formal or informal dress codes.
4. Organizational Structure – This includes both the structure defined by the organization chart, and the unwritten lines of power and influence that indicate whose contributions are most valued.
5. Control Systems – The ways that the organization is controlled. These include financial reward systems, quality systems, and rewards (including the way they are measured and distributed within the organization). The control systems emphasize what is important in the organization by focusing attention and activity, for example, performance appraisal systems.
6. Power Structures – The pockets of real power in the company. This may involve one or two key senior executives, a whole group of executives, or even a department. The key is that these people have the greatest amount of influence on decisions, operations, and strategic direction. The formal organizational structure, or the more informal ways in which the organization works, reflect power structures and delineate important relationships.

The paradigm is the set of assumptions, held in common and taken for granted in an organization, which lies within the cultural web which bonds these assumptions to the day-to-day action of organizational life.

To keep the positive aspects of a strong culture and still reduce the risk of becoming extinct by not changing its culture fast enough to accommodate environmental shifts, an organization needs to develop a 'current state' view in order to understand where the organization is at a particular moment in time. It then needs to understand its 'future state' view of where it needs to be in terms of the organization's desired culture. It is then possible to understand the transition that needs to take place on a practical level between the existing organizational paradigm and the future paradigm and the speed of change required in order to accommodate environmental shifts.

Matters can become difficult if an organization builds a project around a focus of preserving the positive aspects of an organization's culture. It can appear that the organization is then promoting certain aspects of a culture for the sake of it. One school of thought suggests that building a cultural transformation program to deliver cultural change. Another school of thought, which is considered to be more successful, suggests that building a case for change in the business to achieve a business outcome, provides a shift in organizational culture based on the "result of what we do", not "what we do being a result of an attempt to change current culture".

It is also important when recruiting new staff, to ensure new staff fit the positive aspects of the cultural requirements of behaviors and beliefs. An organization that decides that a united global organization is important, may decide to recruit only new staff that have strong fluency in English language skills or recruit a certain percentage of employees from abroad to reinforce its global culture.

### ***Understanding levels of culture***

When working with individuals from a variety of cultural backgrounds or when working in foreign countries it is important to recognize the importance of culture as a strong driver of behavior. Culture influences how people observe and interpret the business world around them.

### Levels of Culture

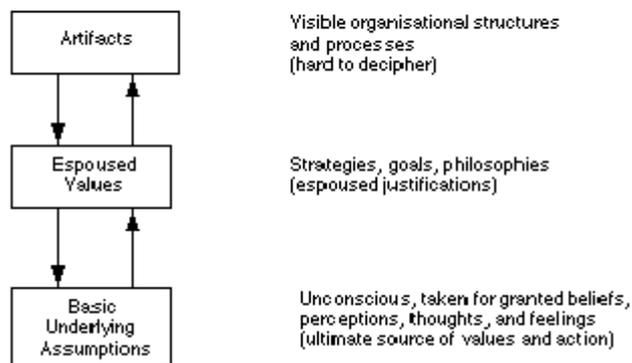


Figure III: Levels of culture (Edgar Schein)

Edgar Schein<sup>14</sup> argues that the pattern of basic underlying assumptions can function as a cognitive defense mechanism for individuals and the group; as a result culture change is difficult, time consuming and anxiety provoking. Cultures are deep-seated, pervasive and complex and it can be extremely difficult to bring the assumptions to the surface. He uses Lewin's<sup>15</sup> three-step approach to discuss change - unfreezing, cognitive restructuring and refreezing.

Individuals need to consider the extent to which they should impose their own culturally based behavior upon others and to what extent this is considered acceptable or not by those with different cultural backgrounds. You can prepare yourself for working in foreign countries or working with individuals from different cultural backgrounds by first taking time out to gain a better understanding of the cultural diversity in the workplace. There is much literature and training material on this subject. Large multi-national businesses often consider it important to provide cultural training courses for executives who spend time working overseas, particularly when the goal is to bring about a change in business practice in the workplace of the foreign country, for example, the roll-out in the Asia Pacific region of a new document management system designed by Europeans for an international legal firm.

Preparation is particularly important as we are increasingly confronted with globalization, the consequence of which is that you are much more likely to be working with others from a variety of cultural backgrounds. Such preparation can include understanding the different levels of culture, as

<sup>14</sup> Schein, E.H. (1985). *Organizational Culture and Leadership*. San Francisco: Jossey-Bass Publishers.

<sup>15</sup> Lewin, K (1951). *Field Theory in Social Science*. New York: Harper and Row.

examined by Schein, that are important to the country or to the nationality of the people relevant to the workplaces in the outsourcing engagement.

In addition for understanding different countries' cultures, it is important to understand the cultural context, which is a subject worthy of exploration in its own right, but not addressed further in this paper. Not only this, it is important to make the connection with how cultural context will impact behavior in practice and show tolerance towards this. Examples of how one can exercise good preparation include the following:

1. Learn as much as possible about local and business cultures.
2. Make an attempt to learn the local language, or at least some words that can be used for expressing gratitude to one's host.
3. Dress conservatively, or at least appropriately, especially of importance for women to observe in Asian countries.
4. Be patient and allow time for mutual understanding.
5. Take cues from those around you.
6. Take advantage of opportunities to socialize with those around you from other cultures.

What is most important is to view cultural diversity as a fascinating opportunity and to take time to understand the assumptions, values, beliefs, communication styles, management philosophies, and decision-making processes that are different from our own. The challenge is not to make judgments and label them, but to stop and ask the question, "That's interesting, why is it that way?" Then one begins to see the benefits of the preparation for cultural understanding.

It is important to regard cultural values in terms of their strengths, as not all aspects of culture of equally important and it is easy to become overwhelmed by the number of specific assumptions, values, beliefs, rules behaviors and customs that exist in a workplace.

Most companies identify a set of core values that are important to the organization, which are widely shared and deeply held by its employees. Understanding the core values of a company is important when looking around for a new job, because if your own values do not match those values you want in

an organization you work for, then there will be a clash and you may decide that you made the wrong choice of employer.

The dynamic values, which run throughout an organization should unify a diverse team of people and form the basis for actions, attitudes, behavior and ultimately success. It drives the way the organization interacts with clients, alliance partners, suppliers, shareholders, communities, and with each other.

Some cultures assume people are fundamentally good, while others assume they are inherently evil. When considering McGregor's<sup>16</sup> X-Y theory which suggests that there are two fundamental approaches to managing people. Many managers tend towards theory X, and generally get poor results. Enlightened managers use theory Y, which produces better performance and results, and allows people to grow and develop.

### ***Exploring holistic approaches***

Developed in the early 1980s by Tom Peters and Robert Waterman<sup>17</sup>, the McKinsey's 7-S model is still a valuable framework which can be applied to outsourcing.

The McKinsey 7-S model involves seven interdependent factors which are categorized as either "hard" or "soft" elements:

1. "Hard" elements (Strategy, Structure, Systems) are easier to define or identify and management can directly influence them: These are strategy statements; organization charts and reporting lines; and formal processes and IT systems.
2. "Soft" elements (Shared values, Skills, Style, Staff) on the other hand, can be more difficult to describe, and are less tangible and more influenced by culture. However, these soft elements are as important as the hard elements if the organization is going to be successful.

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<sup>16</sup> McGregor, D., & Cutcher-Gershenfeld, J. (1960). *The Human Side of Enterprise*. McGraw-Hill.

<sup>17</sup> Waterman, R.H., Peters, T.J., & Phillips, J.R. (1980, June 3). Structure Is Not Organisation. *Business Horizons*. 14-26. Elsevier.

The way the model is presented below depicts the interdependency of the elements and indicates how a change in one affects all the others.

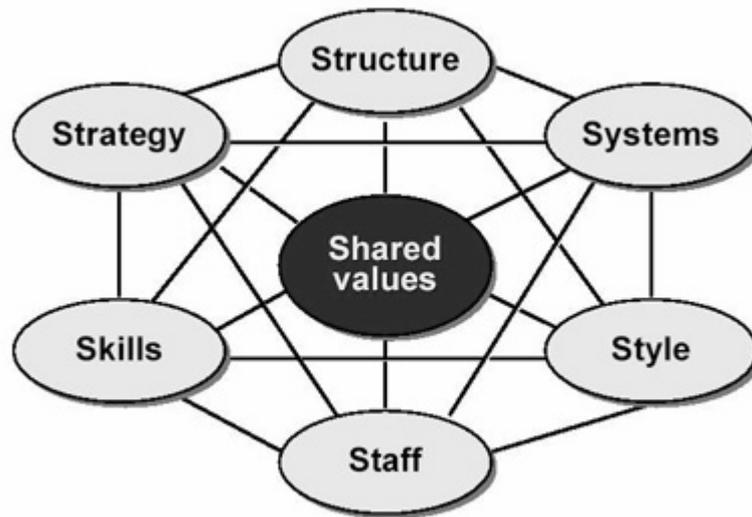


Figure IV: McKinsey 7-S model (Waterman)

Placing Shared Values in the middle of the model emphasizes that these values are central to the development of all the other critical elements. The company's structure, strategy, systems, style, staff and skills all stem from why the organization was originally created, and what it stands for. The original vision of the company was formed from the values of the creators. As the values change, so do all the other elements.

A value is an enduring belief that a specific mode of conduct is personally or socially preferable to another. Shared values not only apply to individuals, but are also central to organizations. What is not illustrated in this model is how to apply it in a typical organizational context or in the context of outsourcing. This is an area worthy of further research.

However, let's look at each of the elements specifically:

1. Strategy: the plan devised to maintain and build competitive advantage over the competition.
2. Structure: the way the organization is structured and who reports to whom.
3. Systems: the daily activities and procedures that staff members engage in to get the job done.

4. Shared Values: called "superordinate goals" when the model was first developed, these are the core values of the company that are evidenced in the corporate culture and the general work ethic.
5. Style: the style of leadership adopted.
6. Staff: the employees and their general capabilities.
7. Skills: the actual skills and competencies of the employees working for the company.

The model is based on the theory that, for an organization to perform well, these seven elements need to be aligned and mutually reinforcing. So, the model can be used to help identify what needs to be realigned to improve performance, or to maintain alignment (and performance) during other types of change.

Whatever the type of change - restructuring, new processes, organizational merger, new systems, change of leadership, and so on - the model can be used to understand how the organizational elements are interrelated, and so ensure that the wider impact of changes made in one area is taken into consideration.

You can use the 7-S model to help analyze the current situation (Point A), a proposed future situation (Point B) and to identify gaps and inconsistencies between them. It's then a question of adjusting and tuning the elements of the 7-S model to ensure that your organization works effectively and well once you reach the desired endpoint. To this end, the model can be applied to an outsourcing context, for example the management of a cultural transformation from Point A to Point B, where a shift in cultural understanding is required between client and service provider organizations. Equally, such a model is applicable for achieving cultural synergy in multi-vendor outsourcing and in delivery models with a supply chain involving several culturally dispersed parties.

As illustrated in Figure IV, the interconnecting center of the McKinsey's model is: Shared Values. The establishment of central beliefs and attitudes can play a key role in improved planning of the allocation of a firm's scarce resources over time. From an implementation perspective, those responsible for the sourcing and management of vendors can apply this diagnostic tool to create value as follows:

1. Align vendors and processes during the outsourcing transition and transformation phases.

2. Determine how best to implement a proposed strategy, for example, an innovative architectural blueprint for the organization.
3. Improve performance of the outsourcing engagement through focus on key performance indicators (KPIs).
4. Examine the likely effects of future changes on the outsourcing engagement.

It is known that groups (and organizations) operate best through consensus and unity of purpose and action, which means that a group's values must match those of the organization in its entirety and according to Collins and Porras (1996)<sup>18</sup>: "It is values that define the enduring character of the organization".

Value conflicts are inevitable in the process of decision-making. Sometimes, membership in a group or organization places constraints on individual values and groups or organizations face conflicts between their own clearly articulated values. What needs to be remembered is that 'action' is the final test of a value, so management should look out for examples of the desired action, and encourage repeated action, as a means to prevent future conflicts on the battleground and enforce the desired behavior.

### ***Leading innovation by cultural example – IBM and Apple***

IBM has adopted the Cultural Orientation Model (COM) developed by TMC (see Figure V), which is based on common tendencies of the people on a number of dimensions or values. Blake, Walker and Walker (2003)<sup>19</sup> selected ten variables and thirty-six relevant orientations attaching to those variables that have been of practical value to international business people in distinguishing between cultures and guiding key decisions.

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<sup>18</sup> Collins, J.C., & Porras, J.I. (1996, September-October). Building Your Company's Vision. *Harvard Business Review*. Massachusetts: Harvard Business School Publishing.

<sup>19</sup> Walker, D., Walker, T. & Schmitz, J. (2003). *Doing Business Internationally: The Guide to Cross-Cultural Success*. 2<sup>nd</sup> Edition. New York: McGraw Hill.



Figure V: Cultural Orientations Model (TMC)

According to Joshi (2006)<sup>20</sup> it is very important to appreciate how different innovative enterprises establish their position in the market place. Most innovative firms have some universal factors to their success, irrespective of their years of existence or their size. In the Time magazine cover story (October 24, 2005) on Steve Jobs and the Apple video iPod it said: “Apple employees talk incessantly about what they call ‘deep collaboration’ or ‘cross-pollination’ or ‘concurrent engineering’. Essentially it means that products don’t pass from team to team. There aren’t discrete, sequential development stages. Instead, it’s simultaneous and organic. Products get worked on in parallel by all departments at once – design, hardware, software – in endless rounds of interdisciplinary design reviews.”

Apple is not Apple because of its technology. Apple is Apple because of the fervor with which its employees believe in the corporate mission. “Every employee carries an iPhone. Every employee has a MacBook/Pro. And every employee seems ecstatic to be doing so. Not every view of Apple is as rosy, of course, but I think the broadbrush characterization fits.”

<sup>20</sup>Joshi, M. (2006, July 5). *Gardening the culture to innovation*. SSRN Working Paper Series. Lucknow, India. <<http://ssrn.com/abstract=913266>> (Accessed on 01 June 2009).

The example of Apple, underscores the fact that the inspiration for technological breakthroughs is not always solely routed in technological knowledge. A culture beyond this is necessary which includes learning. Friedman (2006)<sup>21</sup> argues that one of the reasons why America has always been a leader in innovation of new products and services – from IBM to iPods – is that American has always valued both technology and liberal arts. “In our justifiable desire to leave no child behind, we need to make sure that we don’t leave art and music and theater and literature classes behind as well. It would undermine a critical source of our economic strength...”

“If you look at Apple, they’re very good at generating good ideas. They’re very good at bringing those ideas to market and they are also very good at monetizing (them). They are able to further expand the product offering, with different extensions and different versions,” he says, noting Apple’s iPod and iPhone products.

The same corporate feeling is present at Microsoft and Google. People believe in these employers. And, if Mike Olson is any indication, Oracle has the same general feeling. These companies are winners because their employees fundamentally believe in their products and the companies’ mission.

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<sup>21</sup> Friedman, T.L. (2006). *The World is Flat*. London: Penguin Books.

## **PART III: Cultural leadership success factors in outsourcing**

Regardless of the 'type' of outsourcing that is in question, be it business process outsourcing (BPO), application outsourcing, infrastructure outsourcing, bundled outsourcing, on-, near- or off-shoring delivery based outsourcing; some generic success factors for the engagement can be identified:

1. **Research to understand culture** – Before embarking on the outsourcing engagement, executives should do their homework and ensure that there is a strong understanding of the cultures and related management practices associated with the organizations involved in the engagement. For example, both compensation and benefit practices differ considerably across cultures, often on the individual-group dimension. What may be considered appropriate senior management compensation in a highly individualistic culture may be considered offensive and unacceptable in a highly group-oriented country. A mismatch in culture can cause failure in outsourcing. However, executives need to be aware that each party may feel that it is inappropriate to bring out their feelings in the open, as illustrated in the Iceberg model and if the culture of others is not respected or ignorance of another culture is shown, then this can be disastrous for the outsourcing engagement.
2. **Leadership of cross organizational and virtual teams** – Leaders need to be adept at leading and communicating across geographic and cultural boundaries, demonstrating an understanding of the role of leadership in translating and communicating both within and between vendors and between the corporate entity and its local subsidiaries. The study of cultural differences can help global outsourcing leaders to both create and interpret policies at both local and corporate levels with a higher chance of success across organizational and geographic boundaries.

The Internet has become an enabler for companies to issue requirements to service providers across the globe at a speed never before possible. This is precisely the reason why teamwork applies somewhat differently in outsourcing to traditional business models. One programmer, say from India, can be working with another from somewhere in Europe. This is referred to as "virtual collocation" applies to having teams from several geographical locations working on a common project or service towards a common goal.

Learning how to lead global teams and measure obstacles and progress is important. Team members can discuss how their preferences influence their work on the team and how each person can help reach the team's objectives. Management style can be discussed amongst team members to understand why some members of teams would prefer for the team to perform like a leaderless jazz band (high individuality) and others like an orchestra with a conductor (group orientation and high power distance). In this way, differences in cultural preferences can be leveraged to improve creativity and performance in the outsourcing engagement.

For leaders to develop cross-cultural competence, it is crucial for individuals and organizations to possess extremely good communication, negotiation and mediation skills including the art of listening and the ability to adopt an open, receptive attitude, based on both an insatiable curiosity and desire to learn from and about others.

3. Outsourcing Governance – Critical to the success of outsourcing is strong governance. Attention needs to be paid to the cultural landscape against which the governance model or framework has to be implemented, otherwise there is a risk of 'culture shock' and that the execution of the outsourcing contract will be carried out on the basis of each letter written in the agreement, as opposed to the entrepreneurial or innovative intention which formed the foundation of the outsourcing in the first place.
4. Development of competencies for outsourcing – Understanding how cultural dimensions interact with global competencies is a dimension that mediates how competencies are both interpreted and rewarded. To form the foundation for developing cross-cultural competences, it is crucial for individuals and organizations to possess extremely good communication, negotiation and mediation skills including the art of listening and the ability to adopt an open, receptive attitude, based on both an insatiable curiosity and desire to learn about others.

For the execution of global outsourcing engagements, global functions should be filled by individuals adept in culture, for example, human resources needs to consider training/learning approaches/methodologies (brainstorming [individualism] vs. small group discussion and

presentation [collectivism]; lecture [high power distance] vs. participative approaches [group discussions]; compensation and benefits: individual vs. group rewards).

5. Understand culture's influence on content specific factors in business – Understanding how the law, finance, marketing, brand identification, and related business areas are influenced by cultures is an important success factor, particularly bearing in mind the growth in business process outsourcing (BPO) where unique understanding of the specific business processes is required, for example, the execution of a payments system may involve a more complex process in one country than another, due to the number of individuals who need to give authorization of the payment. Culture will have an impact on management's decisions about authorizations and span of control.

## CONCLUDING COMMENTS

Culture is a powerful human reality that is an integral part of what it means to be a human being in a specific place at a given point in time. People cannot escape from being cultural creatures and having favored value orientations embedded into their ways of doing and thinking. Culture is complex and applies to individuals, groups and corporates. A cultural match between the firm and its vendors is critical to success in outsourcing, yet in practice, few leaders are adept at managing people of different cultures and understanding the influence that culture plays in influencing the success of an outsourcing engagement.

We learn from Iwai, Lev and Radhakrishnan that corporate culture has the three characteristics of firm-specific capital; (1) it is hard to imitate; (2) it disappears with the demise of an organization; and (3) it is accumulated through the learning and education of employees. Large outsourcing engagements typically involve the transfer of people from one organization to another, they typically involve blended delivery models in which low-cost staff are sourced from offshore locations, and they are typically complex by nature, involving a cocktail of expectations, defined and undefined services, unfinished projects, delivery challenges and staff transfers. In the midst of this, skilled specialists are brought together to work in virtual teams across organizations and geographies. The reality is often that they have little time to introduce themselves, let alone take time to understand each others culture, before the pressure of the engagement gets underway.

The good news is that the forces of globalization and Internet technology are driving the need for cultural understanding on a broader, macro scale. In addition, holistic approaches can be applied on both individual and organizational levels, such as the shared values of the McKinsey 7-S model and the best practices of cultural and innovative conglomerates such as IBM's application of the Cultural Orientation's model and Apple's strong innovation corporate culture; combine to provide a footprint which can be followed by participants of the outsourcing services engagement model on local and global levels.

Cultural differences tend to determine management style. For instance, a participative managerial style may be successful in one culture but not another, because of different cultural values in relation

to such variables as power, individualism, competitiveness, and so on. Strong leadership is therefore key in encouraging cultural change and enforcing the positive aspects of existing culture, as key success factor in outsourcing.

There is much more to discover relating to culture. Worthy of further research are such topics as:

1. how culture influences the enablement of innovation through the outsourcing business model,
2. the influence of culture on outsourcing governance and the application of methodologies and tooling in the outsourcing services supply demand relationship, exploring such models as the Kraljic matrix from a procurement perspective,
3. the applicability of culture to supply chain theory, drawing upon examples from the logistics industry and the work of Hansen and Birkinshaw who state that success in innovation is dependent on the reliability of the weakest link in the innovation value chain,
4. the impact of culture on leadership styles.

Gandhi stated, "I want the cultures of all the lands to be blown about my house as freely as possible." This paper reveals how cultural influence is possible in the context of an outsourcing services engagement, but to be successful, strong leadership and tolerance are required.

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