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The Influence of Perceived Risk and Perceived Usefulness on Manager's Attitude Towards Business Process Outsourcing

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ABSTRACT

Although the financial services industry is a large buyer of outsourcing services, it still lags behind other industries especially regarding business process outsourcing (BPO). This research in progress asks why. The main hypothesis is that subjectively perceived risk is decisive for senior management's attitude towards BPO. A causal model will be developed, derived from Perceived Risk Theory and a review of the literature on the usefulness of outsourcing. Using the model, the influence of different risk and utility facets on the attitude towards BPO is assessed. The next research step will be an empirical test of the model.

Keywords

Perceived Risk Theory, Business Process Outsourcing

INTRODUCTION

The outsourcing industry has grown rapidly. Especially business process outsourcing (BPO), defined as "outsourcing one or more specific business processes together with the IT that supports them" (Halvey and Melby 2000) is increasingly seen as a major trend of great theoretical and practical relevance (Lacity, Willcocks and Feeny 2004). Yet, research on BPO is characterized by a "virtual absence of academic publications on the topic" (Rouse and Corbitt 2004, p.2).

This research aims to contribute by tackling the question: Why is the development of the BPO market lagging behind the constantly quoted growth expectations? The German banking sector has been chosen as research object because of the substantial importance BPO plays in the current restructuring of its value chain (Kumar and Hillegersberg 2004; Lammers, Löhndorf and Weitzel 2004). Several studies show that despite the frequent expectation that BPO is beneficial, the adoption rate in the German banking industry is surprisingly small (Bongartz 2004; Lamberti and Pöhler 2004).

This research is driven by the hypothesis that the risk, senior management associates with BPO, is negatively influencing their attitude towards BPO, thus a major inhibitor to the decision to adopt. To the current date no methodological approach allows to assess the impact of BPO on the corporate risk structure in an objective, complete and consistent way (Gewald and Hinz 2004), therefore the subjective perception of the associated risks is assumed to be of great influence.

To challenge this proposition, Perceived Risk Theory (PRT) is applied to analyze the influence of perceived risk (PR) on senior managers' attitude towards BPO. Furthermore a construct of perceived usefulness (PU) will be developed to reflect the interrelation of risk and utility, as none of these constructs can be viewed in isolation (Jurison 2002). A structural equation model (SEM) will be developed and empirically tested using the partial least squares (PLS) methodology (subject to research in progress).

The outcome will shed light on the relationship between risk and usefulness of BPO as perceived by senior managers in German banks, enabling outsourcing service providers to better address the needs of their clients and managers to gain a deeper understanding of the driving forces within the decision process. From a theoretical point of view this research investigates the role of risk as an inhibitor and usefulness as an enabler on the decision whether to outsource business processes, contributing to the understanding of the corporate outsourcing decision.

REVIEW OF THE LITERATURE

Research on Perceived Risk

In marketing research PR has been studied as it affects consumer purchase behavior because of uncertainty about a product or service resulting from imperfect information (Bauer 1967). The expectation of losses associated with a purchase acts as an inhibitor to buying behavior (Peter and Ryan 1976). In information systems (IS) research PR has mainly been studied to explain its effect on system adoption (Featherman and Wells 2004).

Featherman and Pavlou utilized PRT and the Technology Adoption Model (TAM) to predict e-services adoption, and detected a strong inhibiting influence of PR on TAM's criterion variables (Featherman and Pavlou 2003). Featherman found that a general measure of PR reduces PU and adoption intentions (Featherman 2001). Pavlou confirmed that PR reduces the individual's intention to close a transaction (Pavlou 2001).

Research that applies PRT to the adoption of outsourcing is scarce. Benamati and Rajkumar conducted a survey of IT decision makers to test the applicability of the TAM to explain application development outsourcing adoption (Benamati and Rajkumar 2003). In their model they treated the constructs *influence of external environment*, *prior outsourcing relationship* and *PR of outsourcing* as antecedents to the TAM. It is noteworthy, that they did not use PR in its original theoretical framework (comprising of six risk facets), but utilized three risk types derived by literature, namely project management risk, employee risk and relationship risk. They found strong evidence for the applicability of TAM, former outsourcing relationships and the role of PR. Their conclusion was that more research is necessary to understand the antecedents of the TAM and to widen the view for other types of outsourcing.

Research on Risk in Outsourcing

Outsourcing has gained a reputation of being risky business, not just occasionally resulting in unwanted outcomes or the re-integration of the outsourced services back into the internal organization. But as Aubert et al. stated, outsourcing is just as risky as other uncertain business ventures (Aubert, Patry and Rivard 2002). However, the numerous studies conducted on the risks of outsourcing (for an overview see (Gewald and Hinz 2004)) imply that outsourcing is far away from being a risk free choice. Therefore, the role of risk decision-makers associate with the option to outsource is expected to be of major influence on the decision to outsource.

Figure 1 shows a listing of the commonly quoted risks of BPO (based on (Gewald and Franke 2005) who provide a detailed description and discussion of these risks).

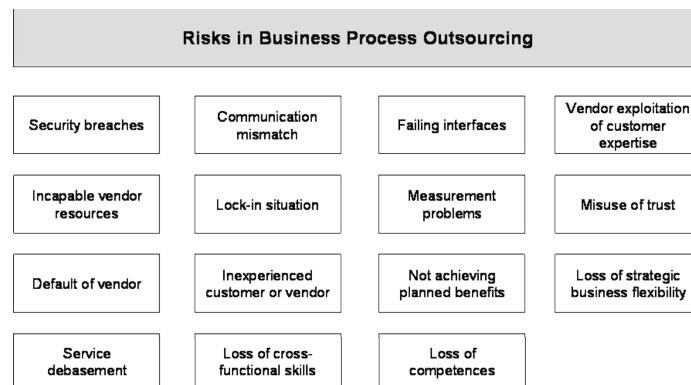


Figure 1: Common Risks of Business Process Outsourcing

Research on the Usefulness of Outsourcing

Numerous studies have been conducted to analyze why corporations chose to outsource parts of their business. Four criteria were cited repetitively, namely cost reduction, access to specialized resources, focus on core competencies and quality improvement. Table 1 depicts some studies exemplarily:

Cost Reduction	Access to specialized resources	Focus on Core Competencies	Quality Improvement.
(Lacity and Hirschheim 1993)	(Duen 1992)	(Grover, Cheon and Teng 1994)	(Lacity and Willcocks 1998)
(Ang and Cummings 1997)	(Quelin 2000)	(Quinn and Hilmer 1994)	(Lacity and Hirschheim 1993)

Table 1: Major Reasons to Outsource

A recent study of the European Central Bank, incorporating the statements of 82 individual banks from 19 European countries, confirmed these major reasons to outsource within the banking sector (European Central Bank 2004).

The Relationship of PRT and PU

Featherman and Pavlou found strong empirical evidence supporting the hypothesis of adverse influence of perceived risk on perceived usefulness (Featherman and Pavlou 2003). Other studies found perceived risk to negatively influence the attitude towards adopting a new service or technology. Circumstances like uncertainty (Cunningham 1967), discomfort and/or anxiety (Dowling and Staelin 1994) or trust/privacy issues (Pavlou 2001) increase the level of perceived risk, adversely affecting the intention to use.

RESEARCH MODEL

The aim of this research is to investigate the relationship of risk and usefulness of BPO as perceived by senior managers and the influence of these constructs on decision makers' attitude towards BPO. PRT has been chosen as a theoretical basis to conceptualize the influence of risk. The conceptualization of perceived usefulness of outsourcing has been derived by an analysis of empirical studies.

The proposed model does not address the intention to adopt BPO (as the TAM would do), it is focused on the attitude towards BPO. This decision has been taken due to the large number of factors that influence the intention to adopt. Despite risk and usefulness there may be factors like the external environment (such as competition, regulation etc.), internal pressures etc. This research is solely devoted to investigate the influence of risk and usefulness on the attitude towards BPO.

Applying Perceived Risk Theory to BPO

Perceived risk is a construct that builds on the beliefs of uncertainty regarding possible negative consequences. It has been described as comprising the subjective perception of two components: the amount at stake and the degree of certainty about possible negative consequences (Cox 1967; Cunningham 1967). It is formally defined as "a combination of uncertainty plus seriousness of outcome involved" (Bauer 1967, p.25). Cunningham distinguishes between six dimensions of perceived risk: Performance, financial, opportunity/time, safety, social, and psychological risk (Cunningham 1967).

For IS research, Featherman and Pavlou introduced a facet called privacy risk, the risk of loss or misuse of private information (Featherman and Pavlou 2003). The risk facets "psychological risk" and "social risk" have been combined to form a single facet called "psychosocial risk", which for the case of outsourcing was conceptualized to reflect the personal reputation of the manager. The facet "safety risk" has been renamed "strategic risk" to reflect the fact that a negative outcome does not directly harm the individual (as safety risk would imply) but could jeopardize the organization. The risk facet time/opportunity has been excluded from this research, as the original theoretical intention (the risk of losing time when searching unsuccessfully for a product) does not apply to the outsourcing context (Gewald and Franke 2005). The following table describes the risk facets in their application to a BPO context.

Applicability of PRT to the Outsourcing Decision

The work of Benatami and Rajkumar found evidence that the TAM can not only be applied to explain intentions of individuals, but also to organizational-level decisions (Benatami and Rajkumar 2003). It is also acknowledged that many organizational-level decisions are ultimately made or strongly influenced by single individuals (Barthelemy and Geyer 2001;

Kakabadse and Kakabadse 2002). Additionally, Dibbern showed that outsourcing - as a major management decision - is decided by individuals rather than organizations (Dibbern 2003).

No	Risk Facet	Description
1	Performance risk	The risk of the BPO engagement not to deliver the expected quality of service. This may be the vendor and/or the banks fault.
2	Financial risk	The risk to pay more money to reach the expected level of service than initially anticipated.
3	Privacy risk	The risk that sensitive client/internal data will be misused by the service provider or that third parties gain unauthorized access.
4	Psychosocial risk	The risk that the reputation of the decision maker is harmed due to the decision to outsource business processes.
5	Strategic risk	The risk to damage the corporation's long term survival chances.

Table 2: Description of Risk Facets

RESEARCH PATH

Following the incorporation of the discussed research strands, a causal model has been developed conceptualizing the hypothesized influences of PR and PU on senior manager's attitude towards BPO. The model developed to test the proposition of this research is depicted in Figure 2 (the graphic depicts only constructs, the formative and reflective indicators are not shown). The basic assumption that PR has a negative influence on the attitude towards BPO while PU has a positive influence is indicated by the "-" and "+" symbols, all other paths are assumed to be positive.

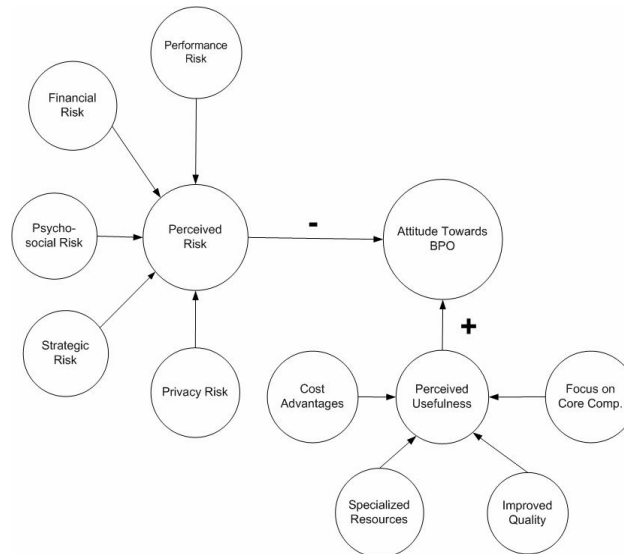


Figure 2: PR / PU Model

A questionnaire has been developed to empirically test the hypotheses. The development of the indicating questions was guided by intensive literature review to enhance construct validity. Three pre-tests with major banks have been conducted to refine the questionnaire.

The survey has been sent to business managers responsible for selected banking processes within the 200 largest banks in Germany. Data collection (including follow-up actions) will be finished by end of June. The analysis will be conducted using PLS and first results are expected to be available in July 2005.

The anticipated outcome of this research is a thorough understanding of how PR and PU influence the attitude towards BPO. Utilizing this knowledge, risk reducing measures can be taken by vendors, leading to a greater adoption rate and a (possibly) less risky BPO future.

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