

Looking out: the rise of the external workforce and its impact on internal functions

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Acknowledgements

This report is the culmination of surveying 430 C-level executives on the changing trends in procurement during January and February 2022 and the accompanying research and interview programme of practitioners and subject-matter experts, conducted by the Economist Impact research team.

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Economist Impact wishes to thank the following experts for their participation in the interview programme:

- *Andrew Brightmore*, executive director, Foodbuy Australia & Compass Group Australia
- *Chris Shanahan*, chief procurement officer, Thermo Fisher Scientific
- *Steven Carnovale*, assistant professor of supply chain management, Saunders College of Business at the Rochester Institute of Technology
- *Gary Graham*, associate professor in operations and supply chain management, University of Leeds
- *Pardeep Gill*, chief procurement officer and vice president of supply chain, Ameren

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A growing focus on the external workforce

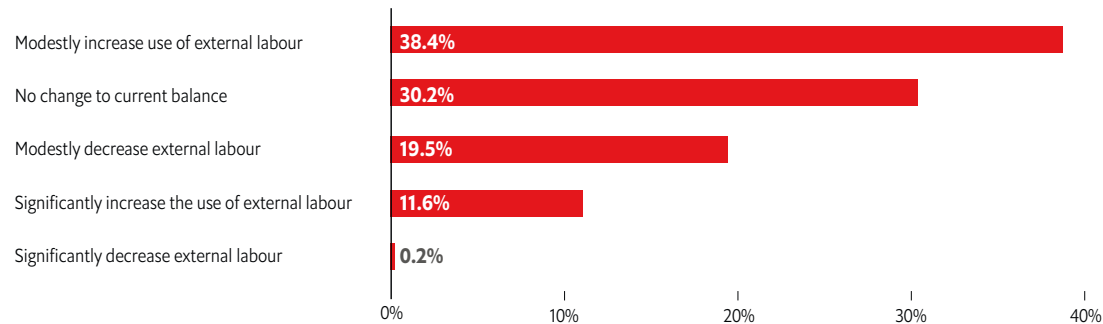
As organisations look to recover in the pandemic's aftermath, digital transformation is expanding opportunities for companies to make changes to their operating models. In turn, this process is allowing them to leverage the benefits of an external workforce through remote and hybrid work structures. Growing dependence on the external workforce is among the most important drivers for digital transformation in companies, according to an Economist Impact survey—picked as a top-three driver by 24.5% of respondents.

Organisational operating models are faced with a pivotal moment catalysed by the disruptions of the past two years, from covid-19 and supply chain upheavals to a range of geopolitical developments. Company leaders are no longer waiting for these problems to simply vanish; instead, they are proactively taking steps to mitigate risk and create value.

Many organisations are expanding their external workforce as a way of navigating this changing business environment. What does this mean for procurement strategically? And how do these changes shape the relationship between procurement and the rest of the organisation?

Exhibit 1a: Growing focus on external workers

By how much is your organisation seeking to change the balance of the total workforce between the use of external workers at the expense of full-time employees? Please select one.



Source: Economist Impact

These are some of the questions that an Economist Impact survey of 430 C-level executives¹ sought to address. It found that 50% of the surveyed organisations globally plan to increase their use of external workers.² In comparison, only a fifth (19.7%) of companies said

they planned a reduction, underscoring how rapidly organisational models and set-ups can be expected to change.

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¹ The Economist Impact survey of 430 C-level executives was conducted between January and February 2022

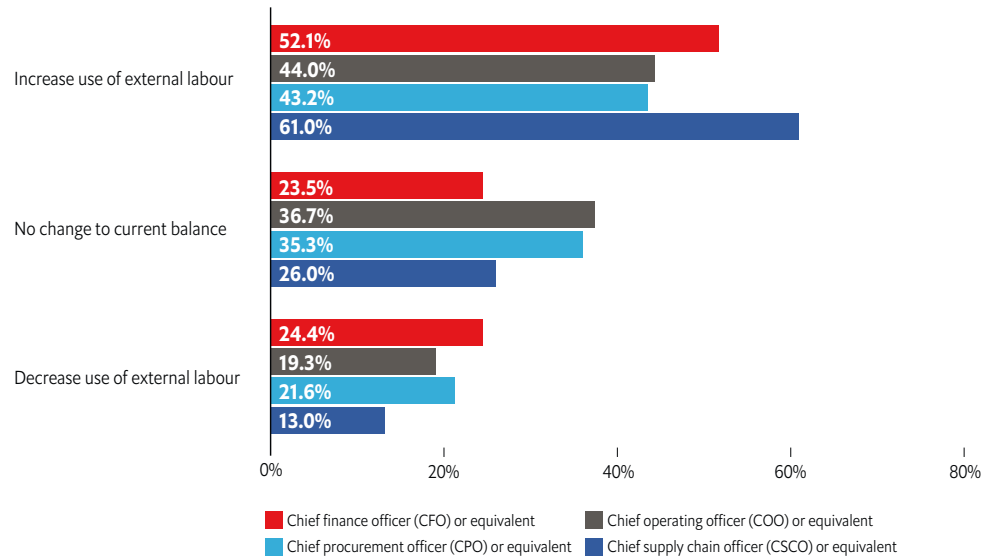
² This briefing paper complements a main research paper on how procurement teams are adapting in a covid-19 and post-covid-19 context and looking to meet new challenges by digitally transforming their operations. To access the main paper, visit [<https://www.ariba.com/resources/library/library-pages-hd/chain-reactions>].

The 2022 Economist Impact survey on procurement perspectives highlighted the emphasis placed by C-suite executives on hiring external workers, signalling that the external workforce is a centrepiece of strategic discussions within organisations. Roughly, half of all survey respondents, regardless of function, say that their organisations will rebalance their workforce in favour of more external hires. This sentiment was strongest among chief supply chain officers (CSCOs) (61%) and chief financial officers (CFOs) (52.1%).

However, not all businesses will hire more externally. Most organisations (58%) with revenue of more than US\$1bn are looking to expand their external workforce, while only a third of smaller firms (32.1%)—with revenue of US\$300m-500m—are looking to do the same. This is not surprising, given that larger companies may require more workers during peak business periods, for example, or simply have different work or skill requirements that are harder to fill in what is a tight labour market.³

Exhibit 1b: A clear focus on hiring external workers across functions

By how much is your organisation seeking to change the balance of the total workforce between the use of external workers at the expense of full-time employees? Please select one.



Source: Economist Impact

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3 IMF Blog, March 31, 2022. "Tight Jobs Market Is a Boon for Workers But Could Add To Inflation Risks". [https://blogs.imf.org/2022/03/31/tight-jobs-market-is-a-boon-for-workers-but-could-add-to-inflation-risks/] Accessed June 8, 2022.

What is driving the growth of the external workforce?

Reducing risks, saving costs

Several factors drive the increased use of an external workforce, but risk reduction emerges as the top factor among 53% of organisations. These workforce-related risks comprise a combination of issues, ranging from rising labour costs because of talent shortages to heightened turnover rates.

Steven Carnovale, assistant professor of supply chain management at the Saunders College of Business at the Rochester Institute of Technology, agrees with risk mitigation, but points to two more drivers underpinning this shift. “Second, it’s the changing nature of the way in which people are working [more people working remotely, more hybrid work models and greater flexibility in work hours]. And third, the most recent thing is the impact covid-19 has had and probably will continue to have on labour, requiring companies to be more flexible with their labour force.”

Chris Shanahan, chief procurement officer of Thermo Fisher Scientific, points to inflation risk as an underappreciated issue affecting the workforce, especially in light of the current economic environment—one

characterised by high inflation. “I think we’re in one of the worst environments to attract talent right now because expected salaries are a reflection of inflation,” he says. “If expectations go up, then so do the costs to retain people. Today is pretty competitive.”

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In this context, not having employees with the right skills—or even enough people—remains a key risk for companies. Many are using external workers to tide over this challenge.

According to Gary Graham, associate professor in operations and supply chain management at the University of Leeds, an external workforce helps create a buffer and reduce risk.

By increasing their dependence on the external workforce, organisations can more effectively build flexibility in their budgets and capacity, and plan for contingencies. A logistics company, for example, might face unexpected surges in pressure to deliver and ensure outcomes, leading them to outsource certain processes such as data analysis.

Much like a relief valve, external workers help companies manage their workforce at an optimal level. “It’s common sense and sound business logic to do that capacity planning,” Mr Graham says. However, he adds that whether this approach is sustainable is questionable, “in terms of what effects it has on organisations and the way organisations are evolving.”

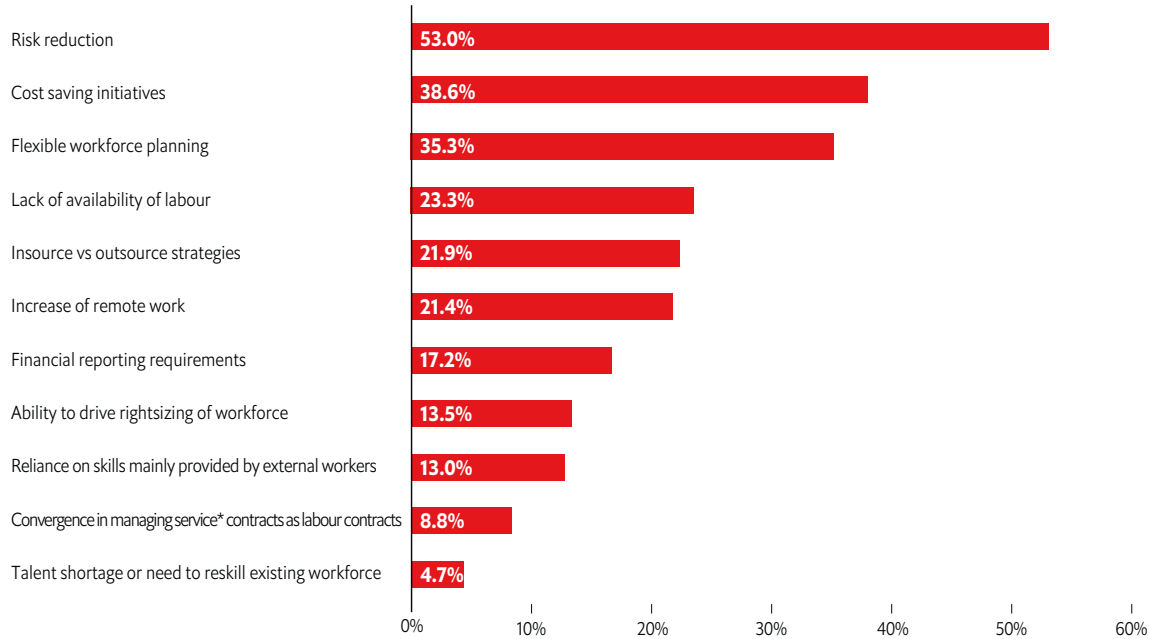
Cross-functionally, organisations seek to increase their use of the external workforce as a risk reduction tactic, with more than half of all respondents selecting this as their top priority. This reflects an organisation-wide shift towards a risk-forward approach, although the strongest sentiments were exhibited by COOs (54.2%) and CSCOs (54.1%). This makes sense for COOs—whose main responsibilities include managing human resources to ensure that the company’s day-to-day operations are not affected—as well as the CSCOs, 30% of whom pick labour shortages as

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Exhibits 2a: Reducing risk and saving costs drive the use of an external workforce

What are the top reasons your organisation is increasing the use of an external workforce? Please select up to three.



Source: Economist Impact

one of the three top priority areas for organisational risk in the next 12-18 months. One in five (20.2%) CFOs also pick external labour contracts as one of the three top areas to focus on to deliver increased value in procurement.

By reducing their risk exposure, organisations also have the added benefit of introducing cost savings (38.6%), the second-biggest factor driving the increase of an external workforce according to the survey.

Compared with full-time employees, external workers incur fewer obligations and costs, allowing employers to scale their workforce as needed, or scout for specific expertise, while avoiding the high costs of retrenching or firing in-house employees. Companies can also recruit experts, who they may not wish to hire full-time, for specific jobs.

Talk of these factors—along with others discussed subsequently—cast light on the re-emerging discussions on insourcing versus outsourcing. The difference now, however, is in the reasons companies are looking to outsource. While much outsourcing in the past was dictated by the need to save costs and centred on business process outsourcing, that is not the sole factor driving conversations today.⁴

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4 Ning Su, Natalia Levina and Jeanne W Ross. MIT Sloan Management Review. November 17, 2015. "The Long-Tail Strategy for IT Outsourcing". [https://sloanreview.mit.edu/article/the-long-tail-strategy-for-it-outsourcing/] Accessed June 8, 2022.

Tight labour market woes

The move towards the external workforce is also being driven by a lack of available labour and talent. In the survey, labour shortages emerged as one of the top three organisational risks that organisations will focus on over the next 12-18 months (25.6%). This is particularly true of CPOs, with 35.3% exhibiting the most concern about the impact of labour shortages on organisations over the next 12-18 months.

Companies globally are having to contend with a particularly tight labour market.⁵ There is a critical talent shortage across sectors, and companies are finding it difficult to find the right people for the right roles. That is not all—employee expectations have also changed significantly in the past few years, particularly as the pandemic, along with remote work, has strengthened the focus on employee wellbeing and benefits, flexible work arrangements, and the desire to work for socially responsible and diverse companies, among others.

Smaller companies—with revenue of US\$300m-500m—have it worse than their counterparts with bigger budgets, with 30.2% placing labour shortages as their top priority given the intense competition for talent. In addition to employee wellbeing and flexible work arrangements, salaries remain a key motivator for professionals to change jobs, putting smaller firms at a disadvantage when it comes to attracting and retaining talent.⁶

Exhibits 2b: Strong cross-functional consensus that the external workforce reduces risk

What are the top reasons your organisation is increasing the use of an external workforce? Please select up to three.



Source: Economist Impact

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⁵ The Economist. April 5, 2022. "Are labour markets in the rich world too tight?". [https://www.economist.com/finance-and-economics/are-labour-markets-in-the-rich-world-too-tight/21808579] Accessed June 8, 2022.
⁶ HR Dive. March 16, 2022. "Talent wars push employers to focus on faster, more frequent financial rewards". [https://www.hrdiver.com/news/talent-wars-push-employers-focus-on-faster-more-frequent-financial-rewards/620472/] Accessed June 8, 2022.

Insourcing versus outsourcing

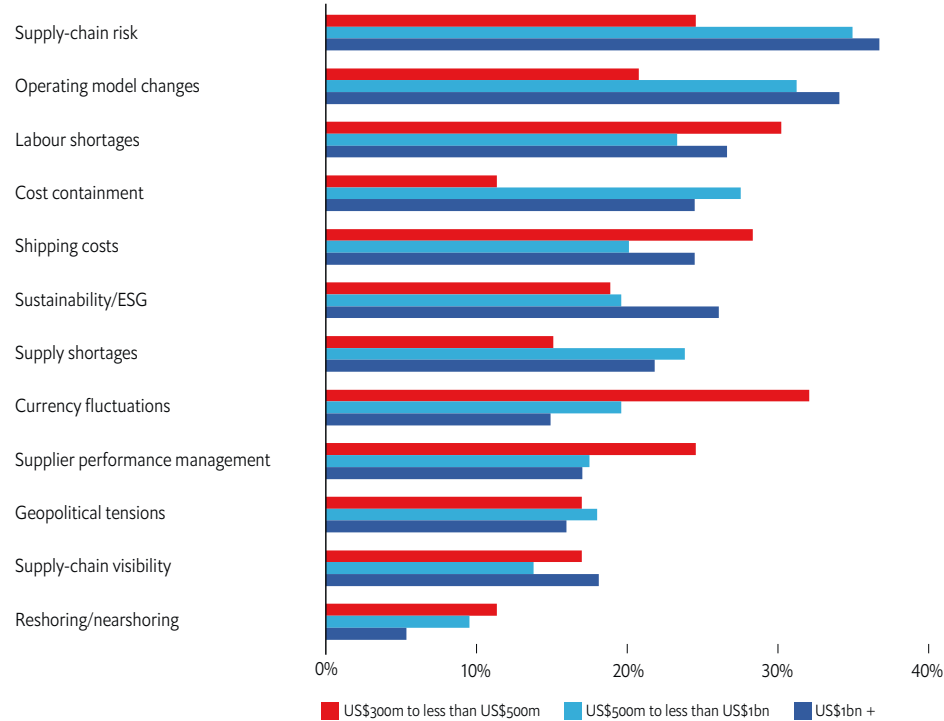
Firms may be able to outsource certain peripheral business activities to external workers in the interests of focusing their internal workforce on core value-creating activities.⁷ For example, a firm looking to create training material on a tight deadline might engage a freelance designer to get the job done faster and without overworking existing employees. Additionally, hiring external workers often means there is no need for training or “onboarding”, saving resources and time.

Flexible workforce planning is picked as a top-three driver for using more external labour by a third (35.3%) of companies, showing that companies want to be able to address spikes in work. This is important given the global economic uncertainty and hard-to-predict troughs and surges in economic activity.

“I think we’re moving in the direction of more external workers for risk mitigation, but also really to remain flexible and agile, because of the simple onboarding process for a consultant or anyone who’s an external worker and not a full-time employee; and because it is super easy to bring them on,” Mr Carnovale says.

Exhibit 3: Concern about labour shortages highest among smaller firms

What are the top priorities for organisational risk that you will be focusing on within procurement over the next 12-18 months? Please select up to three.



Source: Economist Impact

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⁷ Supply and Demand Chain (SDC) Executive, May 11, 2022. “The secrets to surviving the supply chain resignation”. [https://www.sdccxec.com/warehousing/article/22223378/cin7-the-secrets-to-surviving-the-supply-chain-resignation] Accessed June 8, 2022.

Bridging the skills gap

The emergence of the external workforce is underlined by companies' search for the right talent for the job. External employees are enabling firms to rightsize their workforce by giving them access to sought-after skills and knowledge without the added complexities of formal employment. These are especially important when it comes to business needs for specialised skillsets in IT and digital technologies or industry-specific knowledge.⁸

In some cases, organisations using an external workforce may even be able to access “high-end niche experts” that would be otherwise challenging to source. Platforms such as Toptal, for example, claim to give users access to best-in-class freelancers from around the world.⁹ In some industries, especially highly regulated ones, outsourcing certain tasks to a third-party service provider enables organisations to pass risks on to an entity better equipped to handle them. More than one in five (21.9%) companies say their decision to hire external workers is being dictated by conversations around insource versus outsource strategies. A lot of this eventually comes down to the procurement function, which until now was largely focused on procuring products and supplies.

The four reasons cited by a bigger share of companies as a driver for increased hiring of external workers —risk reduction (53%), cost saving initiatives (38.6%), flexible workforce planning (35.3%) and the lack of availability of labour (23.3%)—effectively contribute to decisions around insourcing versus outsourcing. The survey results underline that the question of whether to outsource certain jobs is going to be a key conversation among company executives for the foreseeable future.

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The pandemic is another factor that has pushed the adoption of the external workforce. Covid-19 was a key catalyst of “The Great Realignment”, which is still being felt by companies across the world. This is also evidenced by the survey finding that the availability of skilled labour is the third-biggest impact of supply chain disruptions faced by organisations (13.7%).

For all its disruptions, the pandemic has helped push companies to experiment with hybrid working structures and reorganise work into components that can then be outsourced. These experiments are likely to become permanent thanks to digital communications tools that make collaboration seamless between in-person teams and remote workers.¹⁰

More broadly speaking, technology has also allowed access to a “pool of labour”, says Mr Carnovale. “People can access labour from across the world at the touch of a button. Owing to digitalisation, a lot of it can be done without really needing to be physically present. The flexibility that digitalisation has given employers is great.”

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⁸ SAP Fieldglass. February 2021. “Agility Isn’t Always On The Payroll”. [https://www.fieldglass.com/resources/research/agile-procurement-insights] Accessed June 8, 2022.

⁹ Harvard Business Review. December 2020. “Rethinking the On-Demand Workforce”. [https://hbr.org/2020/11/rethinking-the-on-demand-workforce] Accessed June 8, 2022.

¹⁰ Procurement. February 9, 2022. “CIPS: Hybrid working in procurement grows in popularity”. [https://procurementmag.com/sustainable-sourcing/cips-hybrid-working-in-procurement-grows-in-popularity] Accessed June 8, 2022.

What the greater use of the external workforce means for procurement

With greater flexibility comes responsibility

As a result of the operational model changes being witnessed in a majority of companies, the procurement function's gamut of responsibilities is increasing. This means that it cannot be 'business as usual' for procurement professionals, with the function itself also needing more specialists.

More important, however, are questions about how procurement can work with other partners in an organisation. A shift towards more external workers across an organisation means procurement needs to be in the discussion to understand the company's broader direction for its workforce strategy, and how that sits in its overall business strategy. This, in turn, means procurement needs to understand what it needs to do differently from a contract as well as a technology perspective.

Andrew Brightmore, executive director of Foodbuy Australia, says that for organisations to manage the increased hiring of external workers successfully, they must invest in their procurement capability. By that, he means that shifts in working models are impacting the kinds of skills that a procurement function needs to have. "If an organisation is changing the way it is going to do

business, expectations of what a function might look like will also change," he says.

For example, procurement has to balance the skills required in the organisation with the budget available to hire external workers. "What's affordable to do versus your aspiration of what you want this function to be?" Mr Brightmore asks. A starting point to these discussions is to understand the factors driving this need to look outwards.

In addition to weighing the costs of using more external workers versus the value they bring, procurement must also be mindful of the risks companies are exposed to with a greater number of external hires. For example, Mr Carnovale says it can bring the risk of "lack of continuity" and "the control that gets placed in the hands of the contractor in terms of where, when, how and to what degree they perform the work."

Pardeep Gill, chief procurement officer and vice president of supply chain at the American utility company, Ameren, agrees. In addition to saying that contracting external workers to supplement our staff or outsource a portion of our work is not always a cheaper option for companies (although it can be an easier one), he says there are risks associated with using external labour. Even with the best protections, external workers can still walk away with a

company's intellectual property, Mr Gill says, and in areas such as this, procurement needs to be central in any discussion around contracting external workers. "I don't think risks are reduced by using [an] external workforce in supply chain and procurement. No one buys for your company like employees of your company," he says.

Managing an external workforce can also be a daunting task, and ensuring critical visibility of their performance can often prove difficult due to the ad hoc nature of these working relationships.

The inadequate management of the external workforce can result in any number of issues, ranging from digital security breaches, overcharges and inaccurate invoicing to noncompliance with labour laws, missed milestones and others. Fortunately, digital technologies can offer a way forward by opening up better avenues for communication between in-house and outsourced workers and improving the visibility of the external workforce for maximised value. External labour management systems, for instance, help organisations find and manage external workers such as independent contractors, freelancers and service providers of different kinds, providing greater visibility into the external workforce.

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Increasing use of external workers within procurement

In addition to dealing with the greater use of an external workforce at an organisational level, the procurement function itself is having to deal with higher demand for such workers. Recruitment woes have plagued procurement leaders for years now, as evidenced by a 2018 survey that found that more than half of employers struggled to hire procurement talent despite surging demand and salaries.¹¹ Another report estimated that there was only one qualified candidate for every six procurement-related job vacancies.¹²

Part of the problem lies in the fact that procurement's evolving organisational roles are demanding more and more from its professionals, especially as procurement transitions from a transactional function to one of strategic value creation central to organisations' long-term strategies.¹³ Moreover, as the procurement function continues to digitalise, there are new kinds of roles that procurement teams need to fill. For example, 43.7% of CPOs say that the need for additional resources resulting from the adoption of new technologies is one of the three top reasons for the increase in the size of the procurement

function. They are also increasingly competing for people with technical skills that are in high demand across other functions and industries (picked by 29.2% of CPO respondents). The procurement function has also seen the scope of its activities increase with the increase in the number of categories managed (47.9%).

Most importantly, the increase in staff in the procurement function is being driven by operating model changes. The survey results bear this out. Two in three (66.7%) of CPOs highlight operating model changes as one of the top three reasons for the increase in staff.

Mr Gill says that in addition to the technology side of things, his company has used external workers for market intelligence, spend analytics, bid analysis, tail spend reduction and software renewals, among other things. However, doing so was at a premium compared to having an internal workforce. While the use of external workers brought transformation-related benefits, decisions around hiring more of them were nuanced.

"Initially, I went outside for that skill set. We contracted and relied on several companies, and then what I figured is how much all these subscriptions and services were costing my organisation, and you know, they're not sitting

next to my folks, they don't understand the nuances of my company quite as well as an employee, and so we then started to insource some of these functions."

That said, "people are hiring differently for sure, even in procurement," says Mr Gill. "You need people for forecasting and demand planning and market intelligence, and those groups didn't exist before. We are hiring data scientists, math majors, engineers, information sciences majors—so our mix of labour is absolutely changing". He adds that even some traditionally required skills in procurement are in short supply, such as category managers, project procurement and contract negotiations. In some cases, he says, external workforces can help deliver increased value in procurement for tail spend, where there is low risk in procurement and the ability to easily change vendors, or with software renewals where contracts don't have to be updated.

Mr Gill's views highlight a few of the dilemmas that companies face that tie back to the outsourcing versus insourcing debate, even as the digital transformation imperative continues to guide the overall direction of their business and operational strategy.

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¹¹ Supply Management. April 26, 2018. "More than half of employers struggling to find procurement talent". [https://www.cips.org/supply-management/news/2018/april/more-than-half-of-employers-struggling-to-find-procurement-talent/]

¹² Arkestro. November 30, 2021. "Procurement's Talent Shortage: How to Continuously Motivate High-Performing Teams". [https://arkestro.com/procurements-talent-shortage-how-to-continuously-motivate-high-performing-teams/] Accessed June 8, 2022.

¹³ Gartner. November 2, 2021. "The Great (Procurement) Resignation Didn't Have to Be This Great". [https://blogs.gartner.com/power-of-the-profession-blog/the-great-procurement-resignation-didnt-have-to-be-this-great/] Accessed June 8, 2022.

Conclusion

As the recovery from covid-19 continues, organisations will continue to rely on an external workforce as a way to navigate a risk-ridden landscape characterised by inflationary pressures, supply chain disruptions and growing global competition.

Mr Carnovale says the demand for an external workforce is “going to stick around.” He adds, “I think when companies see the flexibility it gives them and when workers see the flexibility it gives them, I think this is a trend that will stick around, and what rate it will grow at will vary from industry to industry.”

Talent and labour shortages continue to severely impact organisational capabilities and are unlikely to abate given the various macro factors at play. However, digitalisation-driven capabilities are offering relief for companies charting a future-forward path. These changes to operating models will not happen without significant efforts by companies to reimagine the possibilities for the future of procurement, but there are signs that the shift is well underway.

As the recovery from covid-19 continues, organisations will continue to rely on an external workforce as a way to navigate a risk-ridden landscape characterised by inflationary pressures, supply chain disruptions and growing global competition.

This means that procurement has to now think increasingly about the intangibility of service—how it buys these, determines their value, and manages and pays for them. Procurement also now needs to think of outcomes and not solely costs and, to do so, it must know what the rest of the business is thinking and what is driving company strategy, and engage with the business. Companies are changing, and procurement must too.



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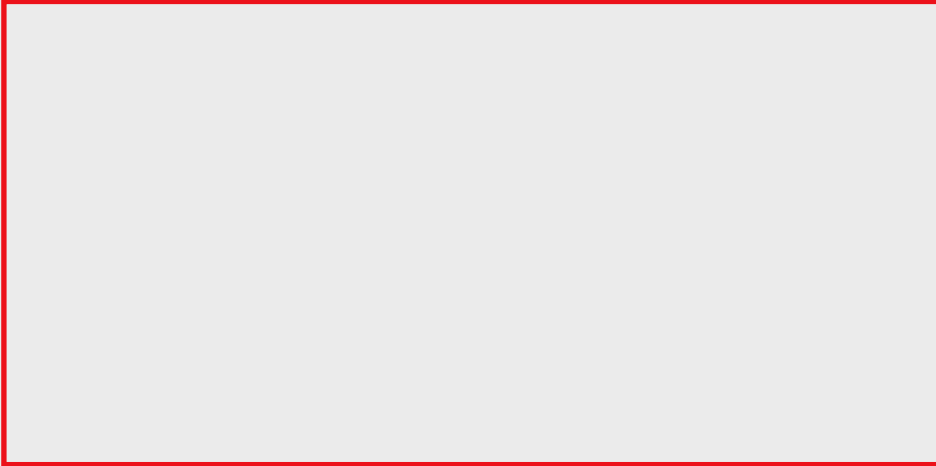
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