

White Paper

BPO is an effective answer to the financial crisis

INTRODUCTION

The ongoing global financial crisis is a concern for everyone in almost all industries - fears of job loss, foreclosed homes, and bankrupt businesses. About **20% to 40% of the revenues** of offshore outsourcing companies are tied to the financial services industry. With its collapse, companies have been forced to look to other vertical markets.

Who wins and who loses from the crisis? In addition, in what ways can a company use BPO services to consolidate its position in this crisis-affected market? This white paper will provide you with answers to these questions, together with some updates on the evolutions of the BPO industry since the beginning of the financial crisis.

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Current economical situation

In order to better understand the effects that the crisis will have on the BPO industry, we must first have a look at the phenomena that generated the crisis.

For years, banks in the US have been lending out large amounts of money in the form of sub-prime mortgages. These are housing loans given to people who, by definition, are unlikely, relatively speaking, to repay them. However, since housing prices were consistently rising, the banks faced little risk: if the debtor defaulted on the loan, the bank could simply seize and sell the house. Then, housing prices started falling, so that soon the banks could not recover the loans and started losing big amounts of money. In a world where commerce is delicately interlinked, these losses had a domino effect, with many important financial institutions collapsing. The US government recently spent **\$700 billion** bailing banks out, but, despite the government's intervention, the damage is likely to be immense.

According to NASSCOM (The National Association of Software and Services Companies – an Indian entity connecting Indian software industry to the BPO sector), the United States is one of the largest contributors to the revenues of BPO companies, with around **60% of all the revenues**. The US financial sector, in turn, is one of the largest customers and the liquidity crunch that has hit these companies will directly cause them to start cutting costs - with customer care and backroom operations being the first they will give up.

Employment is one of the BPO aspects that will significantly be affected by the crisis. According to NASSCOM, the BPO industry offers employment to **700,000 people** in India alone. As of this moment, companies are not expecting to fire their employees any time soon. However, the explosive growth of the BPO industry is pretty much over. Although companies still expect to hire more people, they will not need nearly as many employees as in the last couple of years.

The financial crisis causes companies to look for even more effective BPO solutions

In the medium-to-long term, the sub-prime crisis will accelerate global outsourcing adoption as financial institutions look for new methods to cut costs, according to the Dallas-based Everest Research Institute. The Institute predicts business process outsourcing (**BPO**) **from the financial services sector will increase 40 to 45 times the current market size** over the next five years, with key drivers of growth coming from cost pressures and from **more vertical-specific offerings by offshore suppliers**, according to Everest Research's study, "Global Sourcing in Banking, Capital Markets and Insurance."

Within five years, the firm projects spending for global BPO by the financial services sector will reach US\$145-\$165 billion only for India-based services, the hub of global sourcing for financial services. The report also projects offshore **BPO adoption in the insurance sector will grow 12 to 15 times** during the same period.

Everest Research expects the increase to continue, and points to the financial crisis as the reason. Research made earlier this year by the London-based independent market analyst Datamonitor foresees the same increase in outsourcing. Datamonitor's report, "Trends and Strategies in Policy Administration BPO," notes that both large and small insurers will adopt BPO. Currently, insurers with fewer than 5,000 employees have the lowest policy administration BPO adoption rate; however, this is likely to change in the near future.

The survey also found that large insurers (those with more than 20,000 employees) are increasingly likely to outsource policy administration. Typically, these players were engaged in offshoring via captives, or company-owned facilities. However, since the captive route has not been as effective as expected, their interest in outsourcing to a third party is growing larger.

"The current financial crisis in the U.S. markets is accelerating interest across stakeholders to understand adoption trends and opportunity areas in outsourcing, among other cost containment measures. Banks and other financial services firms are under significant cost-reduction pressure, which is why a large number of firms plan to reduce headcount in Western geographies and move jobs offshore." (Nikhil Rajpal, VP, Global Services of Everest Research Institute).

Crisis effect on BPO

In the medium-to-long term, the sub-prime crisis will accelerate global outsourcing adoption as financial institutions are **counting on outsourcing to cut costs**, according to the Everest Research Institute in Dallas. According to Everest Research's study, the financial downturn could mean **increased numbers of clients** for outbound and inbound call centers, which might even receive new clients who are looking for more cost effective ways of running their business. Similar evolutions might occur in the fields of customer service, sales, and technical support.

No matter what the crisis brings, IT service spending might not feel drastic cuts since high-tech leaders look for ways to protect their budgets; moreover, outsourcers and service providers could help them contain costs and streamline operations. According to Forrester Research, the majority of IT executives report they are re-assessing how to invest what is left of their 2008 IT budgets. Many have decided to cut overall IT spending, but relatively fewer are reducing the amount they put toward outsourcing IT services. The survey shows that while 46% of 258 Global 2000 enterprises have already cut back their IT budgets, **only 21% of these companies**

have cut back on their IT services expenses. That means **IT executives that currently invest in outsourcing will continue that trend during cost-cutting times**, and companies that might not have previously considered sending IT services to an external provider might turn to the delivery model to avoid adding head count or investing in new technology.

BPO market still growing

The research company TPI estimates that the **global outsourcing market** will reach \$88 billion in 2008, **up 10%** from the previous year. Specifically business process outsourcing is expected to increase a total of 14% up to \$22 billion, and information technology outsourcing is forecast to be up about 9%, bringing revenue to \$66 billion. TPI representatives claim that infrastructure-oriented management of servers, desktops, and other IT components is expected to go unchanged, but application development work could be potentially impacted. There will be a downturn in discretionary projects in the short term, they say, but application maintenance will not be affected.

How to survive the crisis by using BPO smartly

So, what should companies do in times of financial crisis? First, they should realize that they need to have strategic thinking, and secondly, they should look more closely at their core-business components. This way, the risks they are taking with outsourcers will be smaller and companies can be more focused on what can really bring gains to the business. For example, during a crisis, companies can successfully outsource HR or Customer Support operations to professional providers of BPO in these fields, thus gaining both from the reduction in costs, and from the competitive advantages these providers bring. **Even in the middle of a financial crisis, those companies using outsourcing can still help the total spending go down.** However, by focusing only on cost reduction, companies might be missing benefits that can be created from global outsourcing partnerships.

In the end, how can companies still manage to go mostly unaffected through this crisis, and benefit from BPO services? It is easy for companies to panic because of the financial crisis and jump at outsourcing opportunities, simply with the goal of cutting some cost. In many situations, they have jumped at the lowest cost option, which has done them more harm than good.

Outsourcing clients have to **think more smartly and strategically**: they need to find solutions for new growth, **concentrate on their core-business and not just on reducing short-term costs.** If companies use outsourcing to become more competitive, it is more than just "shipping jobs offshore": it is an effective means of facing the crisis.

Many of the smart businesses that survive this economic crisis will come out of it more competitive and more globally integrated. Outsourcing alone is not the answer to overcome the crisis, but those companies that sign an outsourcing engagement with the right objectives in mind will gain:

- **Access to new talent**
- **Better process planning**
- **New technology**
- **Global markets**

There is a proliferation of service providers eager for business, and most of them will offer attractive short-term cost savings. However, clients must focus on forging a partnership with a provider that will work with them to add an approach that is a lot more competitive to their business over a multi-year contract.

Key points companies must consider when taking up outsourcing contracts

- **Global approach.** One of the significant differences between the current economic recession and those of the past is the fact that all of today's financial markets and economies across the globe are much more integrated than they used to be. The Internet and global communications revolutions have created unprecedented access to global talent. The need to enter new global markets quickly has never been as pressing as it is in today markets, and the right service partners can help you grow your business globally. Having an infrastructure that can support foreign payrolls, accounting procedures, local regulations, etc. can save your company months of painful work to expand in new markets.
- **Focus on common standards and bundling applications.** Engaging an outsourcing provider that can provide common processes around a solid ERP backbone is critical. Smart companies are moving closer to developing common standards to support processes that can enable them to operate and compete as global entities, and this current economic pattern is accelerating this dynamic. When you have rapid access to your global financial, HR, supply chain, customer, and product information, you are in a position where you can make informed decisions more rapidly to enter new markets and mobilize your resources and partners accordingly to respond to your existing and future customers.
- **Discipline for the revenue cycle.** A good BPO provider can add discipline to your collections and speed up your cash flow, eliminate bad debt, and come up with a more time-friendly cash supply. On the other side, quality procurement processes help you keep the cash you currently have. This is critical in today's tougher environment.

- **Cost-containment as an ongoing objective.** A good outsourcing partner should be able to help you sustain cost savings over a long period, not simply at the onset of an engagement, through ongoing quality and process improvements. For example, you may save \$10 million in the first year of your engagement, but how about the subsequent years? Those initial costs you saved will come back multiplied in the future if you do not constantly refine your processes across your global supply chain.
- **Vertical and horizontal insight.** Setting up strategic outsourcing arrangements should be made with providers who can understand your organization both vertically and horizontally. Vertically they should be able to view and understand the service relationship from strategic level up to the actual day-to-day operations and tasks that they perform. Horizontally, they should be able to increase your cross-functional integration.

Conclusion

Crisis or no crisis, there will always be plenty of companies in need of **good quality BPO services** that will help them get a competitive edge over the rest of the market in which they operate. The current predictions about the BPO industry show that in the future we will see a slowdown in the general growth of the market, but without any real signs of a consistent failure. While some traditional BPO providers are sinking – India being the most notable example - others are rising – as is the case of Romania, for example. In their efforts to reduce costs and cope with the crisis, companies will have to understand that they can turn the crisis to their advantage, and benefit from the decreased costs of BPO services. As to the BPO providers, their chance to survive is to diversify their service portfolio as much as they can, and to be able to offer assistance in more fields other than their traditional ones.