
The BPO Tipping Point: Pointing to the Long-Term Value

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If Malcolm Gladwell is right that almost everything has its tipping point, then we will probably look back on 2006-2007 as the tipping point for business process offshoring (BPO).

From our perspective, what had been a slow, sometimes tentative unfolding seems to have morphed quickly into a fast-spreading trend. We believe we are seeing what Gladwell calls, "the moment on the graph when the line starts to shoot straight upwards."

For BPO, that line will entail both a precedent and the unprecedented.

The precedent is ITO — information technology offshoring, the massive shift of software development jobs to other countries that paved the way for BPO. ITO, too, began as a lightly discernible trend that gathered strength as it delivered benefits and then spiked upwards as processes were perfected.

The unprecedented is more complicated and deserves the closest attention of all those involved in driving today's BPO trend upwards. *Despite the momentous gains in BPO, we believe that many of today's successful BPO operations could contain within themselves the seeds for their eventual obsolescence.* Unless offshorers fully recognize that the keys to a successful long-term offshore operation differ greatly from the keys to short-term gains, they risk the failure of their offshoring strategies.

As head of a BPO company for banks, it has been my job to talk to bank executives about their offshoring strategies.

Recently I have encountered a definite change in market attitude. Before, when I would meet with bankers, my topic was not the most desirable or highest priority topic for them. Offshoring was a highly charged subject politically and socially. Some felt threatened career-wise. Others were simply skeptical.

In her *BPO in Banking* report of May 2005, Celent senior analyst Madhavi Mantha wrote, "Most banks remain unwilling to discuss their BPO strategies publicly and are averse to being named as references by their BPO providers, largely due to public sensitivity about outsourcing in general, and offshore outsourcing in particular."

Then the sea-change happened. If I had to specify a timeframe, I would say early third quarter 2005 — right about the time big banks gear up their serious budgeting cycles. Not only did I find my calls being taken enthusiastically, but I myself started fielding calls from bankers asking to talk about offshoring.

Mantha observed the same, writing in early 2006, "The earlier reticence still holds true in many cases. However, we have definitely seen increased interest and activity levels in offshoring as evidenced by recent announcements by leading US banks who are either implementing or expanding their offshore operations. This is consistent with a global banking trend to use offshore providers to improve the economic efficiency of back-office processes."

Despite the momentous gains in BPO, we believe that many of today's successful BPO operations could contain the seeds for their eventual obsolescence. Offshorers are recognizing that the keys to long-term success differ greatly from the keys to short-term gains.



What happened to shift market attitude? To fuel a race to offshore among organizations that only recently were racing away from the subject? To infuse organizational energy into pursuing strategies that once were anathema?

We think three things changed over the past year to push offshoring to the tipping point. Combined they are making it not only vital but feasible — and not only feasible but desirable — for banks to pursue nuanced, tailored offshoring strategies.

Expense Pressures

Despite years of belt-tightening at most banks, there is no relief on the expense front. Any hard-won savings are quickly consumed by fierce competition for costlier deposits. Compliance outlays are growing faster than new fee opportunities are emerging. Technology innovations take more investment dollars. And for the back office in particular, the shift from paper to electronic payments is raising the per-unit cost of paper payments to untenable levels.

Last year's savings are long absorbed. Management is looking for more of the same, and they are especially looking in areas with high headcounts, especially when it means leveraging investments already made in technology like image intended in part to deliver better productivity.

Early in 2005, Wachovia announced an efficiency drive designed to reduce annual expense by a smooth \$1 billion by 2007. A few months later, ABN AMRO followed with its own plan to eliminate \$930 million in annual expense beginning in 2007. When they review quarterly performance, bank analysts rarely fail to single out expense efforts and results.

Offshoring Results

Financial institutions are notoriously secretive about the results of their offshoring strategies efforts, but evidence of positive results can be inferred from a number of situations and proven from others.

Business Week reported on January 30, 2006, "Bank (of America) execs estimate that they've saved roughly \$100 million since 2001 by offshoring some work that was previously performed in the U.S. and Britain. But just as important was the dramatic savings in time that BofA realized when it developed new products and services."

In the same issue, Deutsche Bank voiced a similar commitment to offshoring: "As far as Daniel Marovitz is concerned, offshore outsourcing is no longer a cost-cutting option for the world's biggest financial institutions. Nor is it even a source of competitive advantage. 'The issue is that if you don't do it, you won't survive,' says Marovitz, chief operating officer for technology at Deutsche Bank's global banking unit."

A PricewaterhouseCoopers survey in 2005 found that although only 2.6 percent of retail bankers polled said their banks had offshored 11 percent to 20 percent of their jobs, 12.5 percent of them said they expect to do so in three years.

Our own case history for offshoring back office functions for a leading US financial services provider delivered savings of greater than 50 percent, with no diminution of quality or speed, while we continue building scale in bank back-office offshoring.

What has happened to shift market attitude? To fuel a race to offshore among organizations that only recently were racing away from the subject?



Globalism Embraced

The third change is less calculable but no less apparent to those of us in the middle of offshoring conversations. I would put it this way: Where offshoring once signified in some circles "taking decent peoples' jobs and sending them around the world to exploit others' poverty," now it signifies "aligning the right jobs with the right resources for the overall value of the company and its stakeholders."

It would be easy to overstate the universality of that shift, and the domestic impact on individuals should not be minimized. But thanks to Thomas Friedman's [The World Is Flat](#), generous coverage of Asian politics and commerce, and all the ways that globalization has touched many people with innocuous or agreeable results, the subject of offshoring has become infinitely less polarizing.

The Economist (December 14, 2005) took issue with a rosy forecast by NASSCOM and McKinsey that India's ITO and BPO services combined are on a track to reach \$60 billion by 2010, not to minimize it, but to suggest that they might understate the case. Acknowledging a shift in western attitude toward offshoring, the article noted that India's share of the offshoring market "is expected to rise as demography — a western labour shortage — becomes more pressing than protectionism."

Indeed President Bush's affirmative remarks about outsourcing and his landmark visit to India represent an official U.S. warming to offshoring.

So today, offshoring can be discussed openly as a legitimate strategy that prudent managers are obliged to understand.

But just as those early gains are being consolidated, a new concern for BPO enthusiasts appears on the horizon. It is the age-old tension between short-term gratification and long-term sustainable gains.

Building for Your Future

It starts with a reasonable enough objective embraced by many companies. They wish to fuel their company's appetite for offshoring by first harvesting the low-hanging fruit. "Let's start with what's easy, uncomplicated, and low-exposure. We will choose two or three functions that are not core to our competitive positioning or key to our customer relationships. They won't entail major risk or compliance challenges. We will ship them overseas and enjoy the savings. Then we will do it again, and again, function after function."

Do that often enough and you will indeed succeed in building an offshore operation that lowers your costs, at least for a time. But it will be capable of performing and delivering only what it was designed for: uncomplicated processes and pure labor arbitrage — "Doing your mess for less."

It will not be capable of delivering what Gartner, Inc. calls Stage 2 and Stage 3 in *The Journey of Globalization* in a September 2005 report.

Gartner reports, "Many organizations that aspire to Stage 2 (Process Effectiveness) and Stage 3 (Ability to Respond to Business) falter after Stage 1 (Operational Efficiency). They are unable to achieve the next plateau of business benefits and savings unless they send more labor offshore.... During the next three years, organizations will no longer be able to justify the undertaking of sourcing globally for the sole benefit of labor arbitrage.... *They will have to find other business values in it* (our emphasis)."

Between Thomas Friedman's [The World Is Flat](#), waves of positive media coverage of emerging Asian politics and commerce, and all the ways that globalization has touched many people with innocuous or agreeable results, the subject of offshoring has become a great deal less polarized.



Is your organization building its offshoring strategy with the full, three-stage journey in mind, or are short-term exigencies skewing your Stage 1 structure with little horizon beyond?

Our experience says there are three hallmarks of a Stage 1 BPO operation that can also progress to Stage 2 and 3.

1. Transformational Is the BPO equipped with transformational capabilities? Can it take tried and true processes and reinvent them for better results? Can it "see" a need for a process that has never existed and create it?

To the untransformed, that can sound discouragingly abstract. But as any transformed organization can aver, transformation is a thoroughly concrete and deliberate event. It rests on three core competencies.

- Deep domain expertise is the first. The bane of many BPOs has been the assumption that if you could offshore a function for one industry, then you could do the same for another industry. If you can field customer service for, say, an insurance company, how different could it be for a travel club? Maybe not very different in Stage 1, but worlds apart for Stages 2 and 3. Transformation requires intimacy with the most intricate and demanding issues of the business at hand.
- Technological superiority is the second. Not just better technology tools but a truly superior ability throughout the organization to bend technology to the best advantage of the operation. That kind of superiority thrives only in organizations that embrace transformation as their mission.
- Workflow management superiority is the third. Again, not just a focus on wringing efficiencies out of existing workflows, but an ingrained cultural predisposition for continual process improvements.

2. Collaborative Is the relationship between offshorer and the BPO highly collaborative? Post mortems on failed BPOs as often as not reveal an over-the-wall mentality, where the company decides what will be "shipped over," dictates the process, and then expects the proscribed results. "We will work out the changes and transformations — you just focus on your SLAs." That doesn't work on shore — why would it work offshore?

Successful BPOs actively seek out opportunities to collaborate as they plan. They see the offshore resources as experts with part of the answer, a different piece of the puzzle to be solved — as a partners, not another vendor. They seek advice and feedback from the BPO before finalizing decisions. They know that as often as not, the best answer comes from the shop floor, not the executive suite.

A key fact about collaboration: it is defined by culture, not organization structure. If it were structure driven, the captive offshore model would almost always be the most collaborative. But the facts show otherwise. Non-captives can deliberately cultivate a culture of collaboration, just as captives can undermine their advantage with a culture of silos. As C.K. Prahalad put it, "Many companies don't understand yet that outsourcing isn't about exporting jobs. It's about importing innovation."

Do that often enough and you will indeed succeed in building an offshore operation that lowers your costs. But it will be capable of performing and delivering only what it was designed for: uncomplicated processes and pure labor arbitrage — "Doing your mess for less."



3. Governance It is safe to say that one of the main reasons for failed offshoring is simply bad governance. Has the development and communication of the governance model received as much careful attention as the rest of value proposition? Take a look at the expectations. Now at the governance. Is there a full match? Are there governance provisions for all that must be accomplished today, tomorrow, and beyond?

We subscribe to four "pillars" of good governance (see Jagdish Dalal's "Governance — The Secret Sauce of Offshore Outsourcing Success" in *Offshore Business Sourcing*):

- Relationship Foundation
- Operational Delivery
- Commitment Compliance
- Risk Management

Is the BPO governed to deliver value to all parties in the relationship? To meet and beat the right service level agreements? To assure both sides of an ongoing, if flexible, contractual commitment? To assess and manage the ongoing risk profile of the operation?

For each pillar, the question must be asked at each stage whether the BPO governance is structured to facilitate matters for both parties.

Our own experience confirms that in the early stages clients focus their energy on getting specific results and trust the governance to emerge from that experience. Our method is to keep matters of governance close to the forefront — not only for governing Stage 1 but keeping in mind that as soon as the client sees early results, Stages 2 and 3, which typically require more astute and attentive governance, are not far behind.

Can you visualize your offshore operation performing not just the simple, labor-intensive functions of your initial business case, but also more complex, even mission-critical functions of your organization? If you cannot — if your vision is limited to Stage 1 operational efficiencies for today's processes in today's workflow — you may be prematurely sunsetting your offshoring opportunity. You may be trading today's gains for benefits that will be even more critical to your company's future.



Bob Olson, president of Carretek, provides Stage 1 and Stage 2 business process offshoring for financial institutions and can envision his Stage 3 offering.

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