InformationWeek
BUSINESS INNOVATION POWERED BY TECHNOLOGY

Financial-Services Firms To Double Offshoring In Three Years: Survey

Low-value IT activities such as infrastructure management already are being sent offshore by 42% of those surveyed, with another 17% to do so during the next three years.

By Steven Marlin, [InformationWeek](http://www.informationweek.com)
Sept. 16, 2005
URL: http://www.informationweek.com/story/showArticle.jhtml?articleID=170703764

Financial-services firms are expected to double the number of jobs located offshore within the next three years as they attempt to reap cost savings, according to a survey released Thursday By PricewaterhouseCoopers.

The survey of 156 senior executives in the financial-services industry shows that a quarter of the survey participants now offshore between 10% and 20% of their employee workforce; that's expected to rise to nearly half in three years.

Cost savings was cited by 79% of participants as the most important benefit of offshore outsourcing, followed by strategic flexibility (33%) and greater focus on core competencies (28%).

Lower-value IT activities such as infrastructure management are being sent offshore by 42% of the survey participants, and another 17% plan to offshore such activities within the next three years. Higher-value activities such as applications and services are being sent offshore by 34%, with another 23% planning to send those tasks offshore in the next three years.

The trend is toward transferring more higher-value operations offshore, especially to countries such as India and China. ABN Amro earlier this month tapped five vendors for its most strategic IT work -- application development. ABN Amro will contract with Accenture, IBM, and Indian firms Infosys Technologies, Patni Computer Systems, and Tata Consultancy Services as preferred vendors for app-development services.

The offshore operating model of choice is the captive venture -- an operation that's majority-owned by the offshoring institution. This preference is most marked for activities such as financial research and modeling that require a degree of specialist knowledge, involve confidential information, or relate to core activities. Such activities are more than four times as likely to be outsourced to a captive operation than to an independent vendor.

PricewaterhouseCoopers

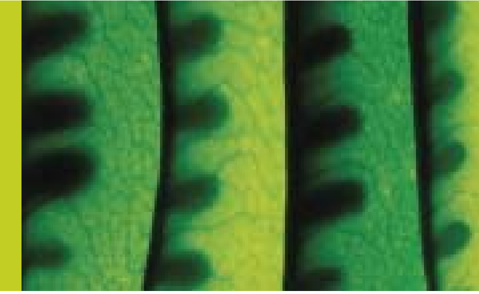
Offshoring in the financial services industry: Risk and rewards*

Contents

- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

*connectedthinking

A joint project with the Economist Intelligence Unit



Executive summary

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

PricewaterhouseCoopers Global Financial Services Briefing Programme

Welcome to the 12th report in our global financial services briefing programme, entitled **Offshoring in the financial services industry: Risks and rewards.** This briefing, written in association with the Economist Intelligence Unit, examines experiences and best practice in offshoring by financial institutions, aiming to identify the risks and rewards of offshoring functions, gauging the secrets of successful offshoring in the FS industry, and identifying the emergent models for future offshoring activity, from outsourcing to captives.

The research effort for this briefing comprised two global initiatives:

- The Economist Intelligence Unit held over 20 one-on-one interviews with senior executives at financial institutions in Asia, Europe and North America.
- The Economist Intelligence Unit and PricewaterhouseCoopers conducted a special online survey of senior executives in financial institutions on the subject of offshoring. Executives from 156 institutions in Asia, Europe and North America participated in the survey, which was conducted during June and July 2005.

The interviews and survey findings were further supplemented by significant desk research.

I am confident that you will find this briefing thought-provoking and insightful. Soft copies of this, along with our previous briefings on **Wealth Management, Economic Capital, Risk Management, The Trust Challenge, IFRS, Compliance, Restructuring, Governance, Performance Improvement** and **Growth,** are all available free of charge from our web site www.pwc.com/financialservices

If you would like to discuss any of the issues addressed in this briefing in more detail in relation to your organisation please speak to your usual contact at PricewaterhouseCoopers or one of the editorial board members listed at the end of this briefing. We would also appreciate your feedback on the briefing as it helps us to ensure that we are addressing the issues that you are focusing on.

J L Scott

Jeremy Scott
Chairman, Global Financial Services Leadership Team

Executive summary continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

The offshoring of activities in financial services – either to captives or by outsourcing them to third parties – is at a crossroads. More and more firms are seeking to take advantage of offshoring, yet the challenges they face are becoming increasingly visible.

In a new survey of 156 senior executives of financial services firms worldwide, conducted especially for this briefing, we found that offshoring activity is expected to rise significantly: whereas almost a fifth of respondents do not currently offshore any headcount, only 6% expect this to be the case in three years' time. Even in the US, where opposition from employees and unions has been growing, many companies that haven't already taken the plunge are under pressure from shareholders to consider offshoring. Similarly, institutions that already offshore anticipate substantial rises in their offshore headcount and in the number of overseas centres that they run.

Yet satisfaction levels with offshoring often leave much to be desired: only half the survey respondents pronounced themselves satisfied with its overall impact. Among the key sources of dissatisfaction are cost overruns, difficulties in recruiting and retaining staff and cultural differences between offshore employees and customers. Time will certainly help firms to offshore more successfully, as service providers and institutions themselves gain in sophistication and experience. But as offshoring activity reaches a critical mass, the problems will also increase.

Regulators are watching to ensure that standards of compliance and governance are maintained, particularly as offshoring pushes into higher value-added areas which are more critical to business continuity and where concerns over client confidentiality and data protection loom larger. Rising turnover of staff is a growing headache in the most popular offshore destinations. Some of the initial savings in wages are being eroded as competition for employees increases.

Lower cost is still seen to be the main benefit of offshoring, and the source of greatest satisfaction for those to have actually offshored. Companies will continue to focus on exporting lower value-added, transactional activities in order to reduce their overheads, and although offshoring to captives remains the preferred option, outsourcing some of these activities to third parties is set to gain ground.

Saving cost is not everything, however, Niall Mowlds, director in performance improvement consulting at PricewaterhouseCoopers in London, cautions companies to take a long-term view of their plans, which usually means between seven and ten years. And survey respondents count strategic flexibility and improved quality of service among the greatest benefits of offshoring.

Many in the industry believe that the distinction between offshoring and the sourcing of expertise and talent internationally will become increasingly blurred. As firms consider shifting higher value-added activities that require specific knowledge or head offshore to address skills shortages in home markets, those that place greater emphasis on people and expertise will do better than those that are simply out to cut their costs. 'The further you go into high-value work, the more it is going to become a team effort between people in high-cost countries and those in lower-cost ones,' says Rob Muth, HSBC's head of global resourcing.

Executive summary continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

As firms move towards building a global footprint in which processes are disaggregated and shared between multiple locations, so offshore destinations will need to differentiate themselves more smartly. Simply being cheapest is unlikely on its own to win business. As examples from India to Ireland show, a critical mass of offshore centres and providers, active government support and the quality of the local skills base will count for more over the long term.

The offshore agenda

Levels of satisfaction with offshoring among survey respondents could certainly be higher: only half pronounced themselves satisfied with its overall impact. To give themselves the best chance of succeeding, firms must:

- **Plan ahead exhaustively.** There are hidden traps for the unwary, not least the prospect of having to pay more tax if firms fail to do their homework, paying inflated salaries in locations with a small pool of talent or exacerbating cultural differences by parachuting expatriate managers into offshore locations. When asked what they would do differently in retrospect, survey respondents with offshoring experience repeatedly replied that they would have benefited from investing more in planning and shaping the deal.
- **Be realistic when drawing up targets.** Too many companies fall victim to over-enthusiasm and end up disappointed by their experience of offshoring. Nearly a third of survey respondents actually experienced an increase in costs in the first year after starting to offshore. Executives identified performance-based compensation for offshore staff and managers as the most effective strategy for delivering ongoing value from offshore operations.
- **Assess the risks properly.** Those who offshore too quickly will live to regret their decision. True, there are solid and immediate gains to be had from ‘value arbitrage’ but there are hazards too, not least to a company’s reputation, if there are offshore security breaches or perceived failures of social responsibility in lower-cost locations. Its ability to stay close to its customers may also be compromised. When choosing outsourcing service providers, survey respondents put experience and expertise far above cost in the list of critical attributes.
- **Think ahead.** The real gains are made by companies that continue to make efficiency improvements even after

Continued overleaf

Executive summary continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

The offshore agenda continued

they have captured the initial employee cost savings from offshoring. Many respondents anticipate moving from a captive model to an outsourced one for lower value-added activities, for example, as well as starting to push higher value-added activities offshore. Fully one-third of respondents say that they either already generate revenue or that they intend to through selling the use of their offshore capabilities to other firms.

- **Stay close to the regulators.** Regulatory scrutiny of offshore activity, whether in captive centres or outsourced to third parties, will only rise as the practice becomes more widespread. While different regulators may have different standards and approaches, what is certain is that they will expect firms to be transparent and to demonstrate active management of risk, both operationally and contractually. Over half the survey respondents have on-the-ground managers at their offshore centres with designated responsibility for risk management.

- **Reward outstanding staff.** Finding and retaining people of the right quality count among the most prominent risks facing offshore managers. The best way to tackle rising rates of attrition, to deliver sustainable improvements to performance and to ensure that the firm's brand and reputation are consistently maintained around the world is to treat offshore staff as you would people in your home market. Four out of five respondents point to training and career development as the most effective way of keeping best performers.

At the crossroads

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

Offshoring – the relocation of business processes and infrastructure overseas – is at a crossroads. A decade or so after American Express and General Electric took their first steps into India in search of lower costs and economies of scale, offshoring's growth prospects and operational challenges have both greatly expanded.

At first glance, the prospect is one of uninterrupted growth. In its most recent World Investment Report, the United Nations Conference on Trade and Development said that offshoring of corporate service functions of all forms could become 'the next global shift'. The Organisation of Economic Co-operation and Development estimates that 20% of all employment in the US, Australia and Canada, as well as the 15 member states of the EU prior to the 2004 enlargement, could 'potentially be affected' by the international sourcing of service activities[1].

Gartner, a research group, estimates that the international market for offshore business process outsourcing (BPO) could reach US$130bn this year, and reckons that India's share of the services offshored by US financial institutions alone was worth about US$1.4bn in 2004. Even in countries with less developed offshoring traditions, such as Japan, financial institutions are also starting to consider shifting processes such as data entry and processing.

In a survey of more than 150 senior executives of financial services firms worldwide conducted for this briefing, the percentage of respondents who expect their firms to offshore up to 10% and 20% of their workforces respectively is set to virtually double by 2008. Similarly, the number of companies in the survey group that do not currently offshore at all is expected to more than halve over the same period.

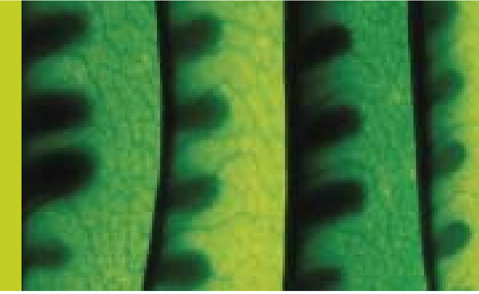
More than 50% of the survey group are either already engaged in IT offshoring or expect to offshore IT activities within three years. Nearly a third of those questioned said that lower value-added human resources activities (such as payroll) which are now being carried out in their home country were likely to be moved offshore within the next three years or so. A further 25% reckoned that lower value-added contact with customers (such as scripted outbound sales calls) was also likely to be shifted.

Nor is it just lower value-added jobs that are expected to move. Although there is greater reluctance to shift higher value-added activities overseas, particularly when customer contact is involved, many institutions are open to the possibility. More than 20% of respondents think that a proportion of knowledge-based tasks such as financial research and modelling is likely to be transferred offshore over the next three years.

'For all operationally-driven activities, we have to ask ourselves 'Why are we doing it here and could we get more value for money doing it in an offshore location?',' says Andrew Robinson, Offshoring Centre of Expertise head for ABN Amro, a leading international bank.

John Worth is chief information officer for Prudential, a UK life assurer and international financial services group that employs a thousand people in Mumbai. The centre is very much part of the UK business which employs around 7,000 in total and Mr Worth sees little practical difference between the two: training, for instance, is homogeneous and, from a regulatory point of view, all processes are transparent, wherever they are.

1 Potential offshoring of ICT-intensive using occupations, April 2005, OECD Working Party on the Information Economy.



At the crossroads continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

Yet the expansion ahead will not be easy or free from growing pains. As offshoring enters the industry mainstream, the challenges it entails are becoming ever plainer:

- Demand for educated staff is already pushing up labour costs significantly in the most popular destinations, particularly in key cities in India. As more firms decide to offshore more activities, the pressures can only intensify, even though new destinations are beginning to open up.
- As the total number of companies taking the plunge offshore increases, regulators may become more intrusive as the risks of disruption to services and of fraud rise. Regulators are likely to respond strongly to high-profile breaches of security in offshore locations, even if the risk of failure is no greater than at home.
- Opposition to offshoring is growing in some developed countries where jobs are seen to be under threat. In 2004 two US states – Illinois and Tennessee – passed new laws aimed at limiting the volume of offshoring; more are considering legislation that would limit state aid and tax breaks to firms that offshore. Chief financial officers are also worried, particularly in the US, that news of their plans to offshore or outsource part of their processes will prompt local staff to defect before the job is done. Since it can take up to three years to complete a move offshore, this can leave a firm badly exposed in the meantime.
- Shifting higher value-added tasks offshore is the logical next step in offshoring but will present particular challenges for managers, at home as well as in the country to which they are shifted.

Faced with these challenges, the companies that will benefit most from offshoring are likely to be those that seek to do more than just emulate their predecessors. ‘Companies are finding that there are no golden rules any more,’ observes Mark Stephen, a partner in performance improvement consulting with PricewaterhouseCoopers.

The costs of offshoring

Contents
Executive summary
At the crossroads
The costs of offshoring
Regulators ahoy
In-house or outsourced?
Where? The offshore locations of tomorrow
Conclusion
Appendix: Survey results
Contacts
PricewaterhouseCoopers Global Financial Services Briefing Programme

Cost savings will continue to be the principal driver of offshoring, but moving functions overseas does not guarantee improvements to the bottom line. When asked to identify the top three benefits they expected to reap when they set out to offshore, more than 75% of those questioned in our survey pointed, unsurprisingly, to cost savings. A third pointed to greater focus on their core competences and to an improved quality of service and around 25% to strategic flexibility.

When we asked respondents what benefits they had actually gained from offshoring, costs savings remained by far the most significant benefit, although the proportions citing this, a focus on core competencies and improved quality of service had all declined (the last most steeply of all). Interestingly, the biggest gainer after the event was strategic flexibility.

But cost overruns compared with original planned savings are common. Nearly a third of survey respondents actually experienced an increase in costs in the first year after starting to offshore, and 15% of respondents reported no change in cost base even after five years of offshoring. For many respondents, costs were higher than expected in areas such as quality control, the transition from old to new facilities offshore, the demands of retraining people and compliance.

The only areas where more respondents said costs were lower than expected rather than the reverse were tax and labour. Even here, things can go wrong. Take tax. Outsourcing to an offshore service provider can result in an organisation having to pay sales tax, something that some overlook when weighing up the pros and cons of such a deal. Frans Oomen, a partner in PricewaterhouseCoopers Amsterdam office, says he has come across several companies that received a nasty shock when they realised that value-added tax or the equivalent would be levied by the provider of the service that is outsourced.

As for labour costs, wages in many offshoring locations are rising fast in the face of high demand. The wage differential between Western markets and offshore locations such as India and China isn't about to disappear, of course. Rising salaries are more important in highlighting the tight labour market conditions that often exist in major offshore centres, particularly for skilled functions. According to a recent report by PricewaterhouseCoopers[2], the turnover of staff in main centres in India can be between 40% and 60%.

The difficulty of finding and keeping the right calibre of people looms large in the minds of those institutions that offshore. Asked to identify the risks that concerned them both before and after they had shifted some of their activities, respondents betrayed much higher levels of concern about people issues once they had made the leap offshore.

Higher basic wages is one way to retain people, but it's a strategy that anyone can replicate. Long-time offshorers already complain about the impact on staff turnover of newcomers dangling fat salaries in front of local employees.

2 The Evolution of BPO in India, PricewaterhouseCoopers.

The costs of offshoring continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

The most effective retention strategy, in the minds of respondents, is to offer offshore employees genuine training and career development opportunities. Similarly, the two most effective strategies for ensuring ongoing value from offshoring activities, after initial efficiency gains have been realised, are implementing performance-based compensation and developing clear progression paths for outstanding offshore employees.

A focus on people-based strategies will become more important as firms offshore higher value-added activities, where concerns over employee skills, confidentiality of data and understanding of the core business are higher.

ANZ steps ahead

ANZ did more than acquire a bank when it bought Grindlays in 1984; thanks to the latter's presence in 40 countries, including India, ANZ also stole a march on many of its competitors. Since the bank first set up an IT operation in Bangalore in 1989, it has barely looked back.

Today, ANZ has 650 staff in Bangalore (some 25% of its entire IT team). The operation looks after the group's software systems and manages some of its technology infrastructure in conjunction with ANZ's other technology campuses in Australia and New Zealand. Not only is ANZ planning to expand that number to around 1,000 over the next 18 months, it is also considering using Bangalore for some back-office processing and is recruiting 50 new staff to pilot the concept.

'These will be new jobs,' says Mike Grime, ANZ's managing director for operations, technology and shared services, 'stuff that we either can't find skills for in Australia or that we couldn't afford to do with Australian labour.' The bank recently completed a study which concluded that a significant number of functions could economically be transferred to India, including back-office processing such as opening new accounts, processing payments and the like. However, ANZ intends to stop short at customer service roles.

'There is a great deal of anecdotal evidence that customers notice and react to the remoteness of service,' says Grime. 'At the same time anecdotal evidence suggests that customers don't care about those parts of the bank's operations they don't directly experience.'

Bangalore is four and a half or five and a half hours behind ANZ's head office in Melbourne, depending on the time of year. So work is easily passed on to Bangalore at the end of Melbourne's day to be continued overnight. 'We use the term 'three campuses' – Australia, New Zealand and India – for our virtual technology team. They are three interchangeable campuses that support each other,' says Grime.

As a centre of technology, Bangalore has distinct advantages. Many of the country's software vendors, such as Infosys and Wipro, are based there, making it handy if they are suppliers. The pool of labour in Bangalore is much larger than in Melbourne. ANZ recently moved 70 vacancies to Bangalore because the bank simply could not fill them at home. Bangalore has graduates galore, many of them trained in newer technologies such as Java and ERP. Yet salaries are around one-third of the level in Australia.

ANZ is using Bangalore increasingly as a strategic asset, a decision that seems to have put the bank a step ahead of its competitors. Only now is National Australia Bank undertaking a pilot project in Bangalore, while Commonwealth Bank is looking, among other places, at the Philippines.

Regulators ahoy

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

People risks are not the only dangers facing institutions that offshore. Fraud and loss of data are others. Recent media scare stories have impressed upon regulators and companies alike the need to ensure tight security and controls when offshoring.

Evidence suggests that the risks are greatest within call centres, which handle customers' identification, PIN codes and the like. Aware of the need to step up security, Nasscom, the lobby group for India's software industry, plans to introduce stricter rules to enhance the protection of privacy by the end of the year. These will raise standards, among other things, for encrypting sensitive data.

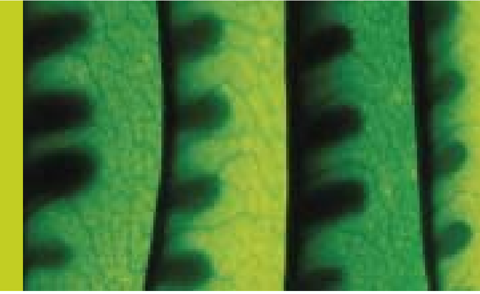
Regulators are monitoring these and other risks, such as business continuity in the event of a systems failure, closely. A recent survey of top firms by Britain's Financial Services Authority caused the agency to think aloud about the difficulties of overseeing activities sometimes thousands of miles from a company's head office. 'It is important that, even as this mode of operation becomes more common, the risks remain under scrutiny,' the FSA concluded.

John Tattersall, chairman of PricewaterhouseCoopers UK Financial Services Regulatory Practice, says it is important that firms demonstrate to regulators that they have as much, if not more, control over their activities as they did before they were offshored. While regulators have so far shown a willingness to give companies the benefit of the doubt, this could be tested if lapses escalate. A broader interpretation of the risks associated with offshoring could also encourage regulators to request that banks and other financial services companies dedicate more capital to certain areas of their business than has hitherto been the case.

The question of access is also near the top of the regulators' list of concerns. 'If, for example, a local regulator doesn't allow the home regulator the same degree of access as it would get at home, then there could be problems. The regulator needs to know that it can get access to data wherever it is,' says Mr Tattersall. Another concern is the transferability of data. Regulators in countries such as Switzerland, where laws about confidentiality are strict, are particularly worried about data security.

To be fair, most firms are aware of regulators' worries. When asked what risk management procedures they had in place, almost half the respondents to our survey said that they had oversight committees whose job it was to look after their offshore operations. Even more respondents said their firms had managers on the ground with responsibility for risk management at each offshore centre (although how effective this governance is in practice is of course a different question).

To counter threats to data security, most service providers have endorsed one or more of the international standards (such as BS 7799 or ISO 17799) which demonstrate that the company has taken steps to safeguard the property of its customers. However, these are weaker than external yardsticks such as SAS70 reports which document the steps taken by firms to ensure security as well as to test their adequacy. In addition, service providers screen potential employees and carry out periodic audits to ensure that their safety procedures are in place.



Regulators ahoy continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

More than half of those questioned in our survey recommended protecting offshore facilities through access controls (such as swipe cards). Many said that their firms stored the data on servers in their home country or recommended secure data transmission protocols. Yet, as experience shows, such measures are far from impregnable. Further well-publicised breaches, if nothing else, may encourage some financial services firms to stay with the security of captive operations instead of farming out their activities to outsiders.

In-house or outsourced?

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

The offshore operating model of choice among survey respondents remains captive ventures – operations that continue to be majority-owned by the offshoring institution. This preference was most marked for activities such as financial research and modelling that require a degree of specialist knowledge, involve confidential information or relate to core activities. Indeed, such activities were four times more likely to be captive than outsourced to an independent vendor.

Many of these centres are on greenfield sites established by financial institutions themselves. But some banks that have inherited outsourced facilities after making acquisitions take them back in-house, either by shifting the operation or by buying out the current vendor.

HSBC is one such organisation. The group acquired outsourced facilities when it bought, among others, Household Corporation of the US. The reasons for switching are straightforward, says Rob Muth, the group's head of global resourcing. Bringing facilities back in-house not only gives HSBC more control over the way the operations are structured and run; it also helps to reassure other stakeholders, such as regulators, that the group is responsible for the way the facilities operate.

It can also be easier to get a bank's domestic workforce to buy into the idea of shipping some jobs offshore if the facility remains under the ownership and control of the institution. And it can be easier to recruit and retain staff if the bank is a well-known brand name in the country to which the functions are being offshored.

Other models have their champions, however. Barclays, for instance, is happy with a halfway house. In 2004, the bank bought a 50% stake in Intelenet Global Services, an established supplier of BPO services, from India's Housing Development Finance Corporation. Barclays reckons that this arrangement gives it sufficient control over pricing and the level of services it needs without having to tie up capital by owning the supplier outright.

And outsourcing remains an attractive model for many financial services organisations. After all, a host of well-known names – from UBS to Mellon Financial, Citigroup, Capital One Financial and American Express – have successfully outsourced some of their operations.

More institutions are likely to do so in the future. It is one thing to benefit from a substantial saving from offshoring at the outset; to continue generating value from the move over time, a transition to an outside service provider can make sense. When survey respondents were asked which operating model their companies are likely to favour in three years' time, the proportion opting for captives falls noticeably, particularly for firms offshoring back-office activities that are not regarded as core competencies or ones that directly impact upon the customer experience.

One reason for the preference for captives, says Andrew Tinney, Deutsche Bank's chief financial officer for Asia Pacific and head of the bank's 'Smartsourcing' programme for the Finance Function, is that many vendors are still relatively immature in the business process space, with little track record. This will change as time passes.

In-house or outsourced? continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

Indeed, some service providers are already becoming more advanced, helping to re-engineer processes as well as simply slice away cost. The change is partly because the pricing regimes with service providers have become more sophisticated of late, says Mr Stephen at PricewaterhouseCoopers. 'This means that the service provider can now share in the rewards of any efficiency savings and therefore has an incentive to do so.'

As a result, financial services organisations are more likely to form a partnership with their provider in order to improve processes and to generate further savings than they were even a few years ago. 'Outsourcing success is a combination of decision, approach, monitoring and managing,' says Crispin Henderson, chief operating officer at Threadneedle Investments, an asset manager now owned by American Express. 'In eight years' time, will it feel like the right deal with the right people?'

All of which will reinforce the industry preference to 'lift and shift' – to offshore first and then consider re-engineering processes later rather than vice versa. That way, they still get the benefit of the 'value arbitrage' – an immediate saving of between 30% and 40% in costs which then helps to pay for improvements down the line.

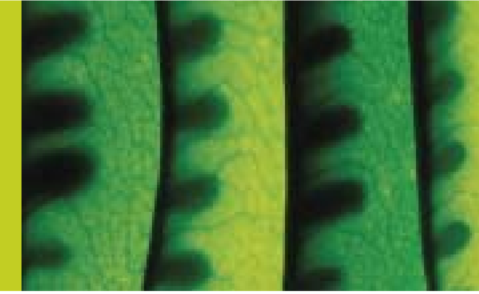
This is true even of those institutions, like HSBC, which offshore only to their own in-house facilities. 'We are going to re-engineer on a global basis some of our existing processes,' says Mr Muth. 'So it is much more than just a question of labour arbitrage.' It is striking that the risk of deteriorating quality of service looms much larger in survey respondents' minds before they outsourced than after they did so.

According to Mr Robinson at ABN Amro, offshoring has facilitated the creation of shared services by aggregating processes that may not have been previously consolidated. 'You can lift and drop similar processes from multiple units into one offshore centre, where the co-location gives visibility to processing differences. So why not take the best process and standardise to create high-quality, true shared services?'

That said, even the ability to 'lift and shift' successfully depends on the quality of the process being offshored and the robustness of documentation. Many firms have reported that they faced significant problems after offshoring because they had not documented their processes adequately or solved certain process problems prior to transition. Processes do not have to be completely re-engineered to be offshored but they do need to be stable enough to be transferred and replicated with relative ease.

For example, Friends Provident, a UK insurer, reaped real benefits from having standardised the systems it used at several centres in the UK. These were adopted more or less without change when the company outsourced parts of its back-office operations to a third party in India, says John Barry, the company's head of BPO. Friends Provident has since needed to make hardly any changes to its systems, even though its contract allows both the company and the vendor to benefit from subsequent improvements.

Prior to offshoring, ABN Amro had already consolidated some of its operational processes into regional hubs in London, Amsterdam and Chicago. Offshoring was then a natural progression, given people were already concentrated and processes standardised into these central hub locations.



In-house or outsourced? continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

Standardised or not, some activities remain much more sensitive than others, of course. Concerns over data confidentiality, cultural differences and quality of service are particularly acute in areas where offshore centres have direct contact with customers. According to Mr Tinney of Deutsche Bank, processes that are most ‘industrialised’ will continue to be outsourced first, while those that require most contact with customers are more likely to be held back.

In future, he says, companies may even choose to re-skill more expensive employees at home and use them as the main point of contact with higher-value customers. Even so, these people will probably be supported by offshore centres that would process data and pipe them back to customer-facing staff. ‘In the long run, it is more about ensuring that your organisation becomes, or remains, a centre of excellence and how to balance that against the cost base,’ says Mr Tinney.

This view is echoed by one of the survey respondents: ‘Our experience indicates that predictable transactions or services are best suited to offshoring. The emerging model is likely to be a hybrid where an unpredicted situation is handed back to the client-facing location for resolution.’

Where? The offshore locations of tomorrow

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

That companies are looking to offshoring to solve more of their problems is beyond dispute. But it is also clear that the reasons why firms offshore, and the types of activities that they will seek to move, will vary greatly between individual institutions. **For some, cost savings will continue to be the overriding objective.** For others, improved processes and the sourcing of skilled employees will be the primary goals. These differences will affect their choice of destinations.

According to a recent ranking of offshore destinations by the Economist Intelligence Unit (EIU)[3], India ranks top on the basis of nine attributes such as macroeconomic stability, regulations, and labour costs and skills. Thanks to its combination of an educated, English-speaking population, low costs and a highly-skilled workforce, India's BPO market has grown at an annual rate of between 40% and 50% over the past few years. Despite increasing competition for skilled labour, it still costs less than US$7,500 a year to hire a call centre agent in India, which is under half what an employer would have to pay in, say, the US or Australia.

So far, offshoring has been centred round a few key cities in India such as Bangalore, Delhi-NCR, Chennai, Hyderabad and Mumbai. As costs in these places rise, others are likely to come into the frame, so maintaining the country's overall competitiveness, says Joydeep Datta Gupta, a partner specialising in outsourcing advisory with PricewaterhouseCoopers in India (see box).

Blazing a fresh trail

When call centres and other business process outsourcing (BPO) work began in India, companies went first to Gurgaon, an expanding mini-city on the outskirts of Delhi, along with the commercial capital of Mumbai (Bombay) and the high-tech hub of Bangalore. Those three places still top most companies' lists, especially for financial services. But BPO is now spreading far wider to places like Kolkata (Calcutta) and, on a smaller scale, to the tourist city of Jaipur in Rajasthan and even the old French colonial outpost of Pondicherry near Chennai (Madras). This diversification is being driven partly by staff costs – Jaipur is 15% cheaper than Gurgaon and staff attrition 50% lower – but more often by the need to tap high-calibre university graduates.

The movement to new areas has coincided with a dramatic improvement in India's telecom infrastructure which, though still far from perfect, is manageable in most sizeable cities. Consequently, other factors now top the list of priorities. Pramod Bhasin, chief executive of GECIS, which is part-owned by America's General Electric, says: 'Managers need to be persuaded to go to live in developing cities which means having adequate schools and employment for spouses.'

India's recent boom in highway construction is also opening up possibilities near established centres. Pune, an industrial city which is now only three hours drive from Mumbai, is becoming popular with BPOs including Wipro BPO (until recently Wipro Spectramind) and EXLService, which is based on the outskirts of Delhi. Construction of

Continued overleaf

Where? The offshore locations of tomorrow continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

Blazing a fresh trail continued

satellite business areas on the edge of established centres is also opening up new locations, especially around Delhi and Mumbai. Further afield, ICICI One Source, which is majority owned by ICICI, one of India's largest private-sector banks, has set up small operations in Pondicherry and Trichy, which it regards as satellites to a larger one in nearby Chennai. The attraction is that education levels are high, there are no other big BPOs to compete with for staff, and it can tap talent in Chennai. Cochin and Trivandrum in Kerala, Nagpur in central India, Dehradun in the foothills of the Himalayas, and the tourist State of Goa are also vying for business.

BPOs also want more support from state governments. One of the most ardent is the government of West Bengal, of which Kolkata is the capital. So far, it has attracted operators such as IBM, Tata, HSBC, Wipro BPO and GECIS, and others are on the way. Another is Chandigarh, a modern city a few hours drive north of Delhi, which has attracted Dell Computers. In addition to giving firms tax breaks, regional governments also help by providing various other financial and non-financial incentives to BPOs, such as cash-back support for real estate used for BPO activities and special laws that give BPO activities the status of essential services.

However, recruits in developing cities usually require more training than those in the metropolitan areas; this, together with the cost of importing managers, often offsets any savings. Such cities can also often absorb only one or two operators. 'Once you've built up your staff, there must be capacity to backfill your employment churn,' warns Devashish Ghosh, chief operating officer of Wipro BPO, which is part of the broader-based Wipro IT group and has 15,400 employees in six centres.

Mr Ghosh believes that traditions are important. For example, Kolkata benefits from being India's former colonial capital and the headquarters of old financial institutions; Chennai and Pune also have strong financial roots along with Mumbai. 'You need to consider the DNA of a city because everything is dependent on a talent pool with good English,' he says.

Asian countries, including China, Hong Kong, the Philippines and Thailand, account for most of the EIU's top ten. China has a growing reputation as a centre for research and development, particularly with international companies like General Electric. But, thanks partly to its relative lack of English-language skills and patchy laws on intellectual property and data protection, it has yet to gain extensive ground within the financial services industry.

Vietnam is also touted as a future location for offshoring by respondents to our survey. But competition from other regions is growing. South Africa is mentioned as a possible contender by some. Thanks to the fact that they are among the states that have recently acceded to EU membership, the Czech Republic, Poland and Hungary also feature among the ten most popular destinations in the EIU's ranking. Slovakia, which is 12th in the EIU's rankings, is also mentioned as an up-and-coming destination by respondents to our survey.

Language skills also boost other states. For example, four million Romanians speak French and two million of them German. In time these skills could attract an increasing number of financial services groups from continental Europe seeking to reduce their costs.

Where? The offshore locations of tomorrow continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

Dubai is also cited as an attractive potential destination over the longer term, particularly since its telecommunications links and other such facilities are well developed. With the savings and financial markets in the Middle East becoming more and more active, banks and investment houses may in time be tempted to consolidate more of their regional operations there.

US firms in particular are looking anew at Latin America, especially Mexico, says Paul Horowitz, lead partner for the outsourcing group in PricewaterhouseCoopers New York office. Cultural affinities and Latin Americans' apparent willingness to work with their US counterparts in improving processes are also cited as advantages. The fact that some outsourcing centres are within driving distance of the US border may also be a factor.

Not all destinations are in emerging markets (see box). Singapore and Canada, a near-shore destination for many US companies, are fourth and sixth respectively in the Economist Intelligence Unit rankings. Thanks to their pro-business cultures, advanced telecoms and transport infrastructure and lack of red tape, even the US and the UK rank 20th and 29th respectively in the number of offshore projects across all industries, including call centres, shared service facilities, IT services and, importantly, regional headquarters.

Up, up and away

What to do if you already play host to 450 or so of the world's largest financial organisations, many of them American, but are so successful that you are no longer cheap? Answer, according to Ireland IDA, the country's development agency: go up market.

In a way, it is a nice problem to have. Since it was established during the late 1980s, Dublin's International Financial Services Centre has gone from strength to strength. Thanks to a well-educated and articulate workforce, the centre acted as a honey pot for banks, fund managers, insurers and the like seeking an offshore base in the European Union. It helps that Dublin is only a short hop from America's east coast and that corporation tax is a mere 12.5%. Indeed, most financial services organisations can expect to pay even less.

A slew of big international banks now treat Dublin as home from home. At the last count Citigroup's global processing centre there was handling transactions worth at least US$750bn a day. The group has more activities under one set of roofs in Ireland than anywhere else in Europe outside the UK. Its base in Dublin handles everything from risk management, billing and payment routeing to fund administration, global custody and settlement, and assurance.

Yet, with asset prices and wages rising, Dublin is no longer a cheap place to do business. Budding centres in the accession states of eastern Europe, many of them with well-educated workforces of their own, are better placed to handle the lower value-added tasks required by banks operating in the European Union.

Continued overleaf

Where? The offshore locations of tomorrow continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

Up, up and away continued

As a result, Ireland plans to capitalise on its other strengths. It wants to promote itself as a centre for securitisation and specialist debt products. International banks there have already started issuing covered bonds and certificates of deposit. Another idea is to broaden the country's appeal as a hub for global banking products.

'The next step may well involve Dublin acting as an international hub for financial services organisations,' says Pat Wall, a partner with PricewaterhouseCoopers. 'Some of the lower value-added work could be transferred to cheaper locations in eastern Europe but the products would still be domiciled in Ireland, particularly with the country's fiscal and regulatory advantages.' If successful, this could be a model for others to follow.

Conclusion

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

There is little doubt that offshoring presents financial services organisations with an important weapon to gain competitive advantage. Twenty years ago many scoffed at Nike's plans to revolutionise the sportswear industry by internationalising it; now it is difficult to imagine trainers being produced any other way.

Many believe that we have seen only the tip of the iceberg in the trend towards offshoring in financial services, not least because the working-age population in many developed markets is set to dwindle over the longer term. Indeed, skill shortages in certain areas are already having an impact on some institutions. Friends Provident found that competition for experienced insurance underwriters in the UK had reached a point where it made sense to outsource part of its new-business processes in order to secure the skills it required.

Almost one quarter of the survey respondents expect to be running five or more offshore centres in three years' time. The burgeoning expansion of Indian service providers into a number of overseas markets is one example of how vendors are offering institutions global support. HSBC's Mr Muth can foresee a time, for example, when specialist groups working on, say, credit analysis or economic modelling will combine the skills of people in three or four continents in order to solve problems and produce original work.

Labour arbitrage can deliver substantial savings, to be sure, but many of the long-term gains from offshoring come from smarter ways of doing things, from improved processes and from knitting together a number of offshore centres, some in low-cost countries and others in high-cost ones, into single, cohesive activities. Those who get most out of offshoring are likely to be those who put most into planning at the outset and who look beyond the initial cost savings and towards leveraging a global talent base. □

Appendix Survey results

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

The Economist Intelligence Unit and PricewaterhouseCoopers conducted a special online survey of senior executives in financial institutions on the subject of offshoring. Executives from 156 institutions in Asia, Europe and North America participated in the survey, which was conducted during June and July 2005.

Our thanks are due to all those who participated for sharing their insights with us.

Please note that totals do not always add up to 100 because of rounding, or because respondents could choose more than one answer.

Section 1: About you

1. In which region are you personally based?

Western Europe	32%
Asia-Pacific	24%
North America	22%
Latin America	8%
Eastern Europe	7%
Middle East & Africa	7%

2. What is your title and area of responsibility? Please check as many as apply.

Senior management	35%
Finance	22%
Strategy/planning	19%
Risk management	18%
Board member (executive director)	12%
Line manager	12%
Operations	12%
Other	8%
Marketing and communications	6%
Board member (non-executive director)	4%
Investor relations	4%
Legal	3%
Human resources	1%
Internal audit	0%

Appendix Survey results continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

3. What area of financial services do you personally work in? Please check as many areas as apply.

Investment banking	34%
Retail banking	27%
Corporate banking	26%
Capital markets	25%
Investment management/Real estate	15%
Private banking	14%
Life insurance	10%
Private equity	10%
Outsourcing services provision	10%
Non-life insurance	9%
Other	8%
Re-insurance	3%

4. What was your organisation's total global income, in US dollars, in 2004?

Over $10bn	27%
$5bn-$10bn	21%
$1bn-$5bn	14%
$500m-$1bn	15%
Less than $500m	23%

5. How long has your organisation been offshoring activities for?

More than 10 years	21%
6-10 years	17%
5 years	12%
4 years	10%
3 years	14%
2 years	8%
1 year or less	6%
We do not offshore	12%

Appendix Survey results continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

Section 2: Your organisation's offshoring plans and experience

6. What percentage of your organisation's headcount is currently offshored and how much do you expect to be offshored in three years' time?

	0%	1-5%	6-10%	11-20%	21-30%	31% plus
Now	18%	46%	16%	9%	4%	7%
Three years' time	6%	29%	29%	16%	8%	11%

7. Which of the following types of activity do you currently offshore and which do you intend to offshore over the next three years?

	Currently offshore and intend to keep offshore	Currently offshore and likely to bring back in-house	Do not currently offshore but likely to within three years	Do not currently and unlikely to offshore
Lower-value IT activities (e.g. infrastructure)	42%	3%	17%	38%
Higher-value IT activities (e.g. applications & services)	34%	3%	23%	39%
Lower-value customer contact activities (e.g. outbound, scripted sales calls)	25%	5%	25%	44%
Higher-value customer contact activities (e.g. inbound helpdesk calls)	17%	4%	17%	62%
Lower-value HR activities (e.g. payroll)	15%	3%	31%	51%
Higher-value HR activities (e.g. benefits management)	8%	4%	13%	75%
Lower-value finance activities (e.g. accounts payable)	17%	7%	27%	49%
Higher-value finance activities (e.g. financial statements and reporting)	11%	5%	19%	66%
Knowledge-based activities (e.g. financial research, modelling)	14%	7%	22%	58%

Appendix Survey results continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

8. Which operating model does your organisation currently favour for its various offshoring activities?

	Captive	Build-operate-transfer	Joint venture	Outsourcing to vendor	N/a
Lower-value IT activities (e.g. infrastructure)	32%	5%	7%	36%	20%
Higher-value IT activities (e.g. applications & services)	37%	11%	6%	25%	21%
Lower-value back-office processes (e.g. payroll, accounts payable)	36%	9%	7%	27%	21%
Higher-value back-office processes (e.g. benefits management, financial reporting)	41%	11%	8%	11%	30%
Lower-value front-office processes (e.g. routine outbound customer calls)	41%	4%	7%	17%	30%
Higher-value front-office processes (e.g. inbound helpdesk calls)	43%	7%	5%	12%	33%
Knowledge-based activities (e.g. financial research, modelling)	48%	5%	6%	10%	31%

9. How many offshore centres does your organisation run and how many do you expect it to run in three years' time?

	0	1	2	3	4	5	6-10	More than 10
Now	24%	27%	19%	10%	4%	4%	4%	8%
Three years' time	13%	21%	15%	16%	9%	6%	11%	10%

Appendix Survey results continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

10. What are/would be the most critical criteria for your organisation when choosing a specific offshore location? Please choose the top five criteria.

Political stability	64%
Low labour costs	58%
High level of education	48%
Quality of IT and communications infrastructure	47%
Language skills	43%
Availability of talent	41%
Macroeconomic stability	37%
Quality of intellectual property regime	27%
Tax/VAT/GST regime	22%
Quality of legal system	19%
Quality of third-party suppliers	18%
Quality of physical infrastructure (roads/airports/etc.)	13%
Liberal labour laws	10%
Transparency of tax regime	9%
Size and potential of home market	5%
Other (please specify)	4%

11. Which country currently accounts for the largest share of your organisation's offshore headcount? (Top five answers)

1. India
2. China
3. Ireland
4. Malaysia
5. Singapore

12. If your organisation intends to offshore to new countries over the next three years, which country is it most actively considering? (Top five answers)

1. China
2. India
3. Brazil
4. Philippines
5. Poland

Appendix Survey results continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

13. What are the top three benefits your organisation expects to reap from offshoring, if it is considering doing so? If it has already offshored, what were the top three your organisation expected at the point when it first chose to offshore?

Cost savings	79%
Improved quality of service	34%
Greater focus on core competence	34%
More efficient and transparent processes	28%
Strategic flexibility	27%
Access to better talent and technology	25%
Business continuity	21%
Increased revenue	13%
Risk reduction	12%
Launch pad into domestic markets of offshore locations	7%
Improved compliance	3%
Other (please specify)	2%

14. Now please choose the top three benefits your organisation has actually reaped from offshoring.

Cost savings	74%
Strategic flexibility	33%
Greater focus on core competence	28%
Business continuity	27%
Improved quality of service	25%
Access to better talent and technology	24%
More efficient and transparent processes	23%
Increased revenue	16%
Risk reduction	14%
Launchpad into domestic markets of offshore locations	6%
Improved compliance	5%
Other (please specify)	2%

Appendix Survey results continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

15. Please identify the top three risks you expect your organisation will have to manage if it is considering offshoring? If it has already offshored, please identify the risks you were most concerned by at the point when your organisation first chose to offshore.

Deteriorating quality of service	41%
Cultural differences between home and host markets	41%
Finding/attracting people of the right quality	27%
Cost overruns	26%
Political and regulatory risks in offshore location	23%
Inadequate levels of compliance and internal control	20%
Retention of top employees in offshore markets	19%
Rising wages	17%
Security of client data	17%
Inadequate communications and infrastructure	16%
Political and regulatory risks in home market	13%
Changes to taxation, VAT and transfer pricing regimes	12%
Security of intellectual property	11%
Impact on management time	9%
Other (please specify)	2%

16. Please identify the top three risks your organisation is most concerned by now that it actually is offshoring.

Finding/attracting people of the right quality	39%
Deteriorating quality of service	31%
Cultural differences between home and host markets	30%
Retention of top employees in offshore markets	29%
Rising wages	23%
Political and regulatory risks in offshore location	22%
Changes to taxation, VAT and transfer pricing regimes	21%
Cost overruns	17%
Inadequate levels of compliance and internal control	17%
Impact on management time	14%
Security of intellectual property	14%
Security of client data	13%
Political and regulatory risks in home market	11%
Inadequate communications and infrastructure	11%
Other (please specify)	2%

Appendix Survey results continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

17. Which operating model will your organisation favour for its offshoring activities in three years' time?

	Captive	Build-operate-transfer	Joint venture	Outsourcing to vendor	N/A
Lower-value IT activities (e.g. infrastructure)	26%	10%	7%	38%	19%
Higher-value IT activities (e.g. applications & services)	27%	12%	13%	25%	23%
Lower-value back-office processes (e.g. payroll, accounts payable)	28%	9%	9%	34%	20%
Higher-value back-office processes (e.g. benefits management, financial reporting)	38%	9%	10%	13%	31%
Lower-value front-office processes (e.g. routine outbound customer calls)	33%	9%	6%	23%	29%
Higher-value front-office processes (e.g. inbound helpdesk calls)	36%	6%	9%	14%	34%
Knowledge-based activities (e.g. financial research, modelling)	44%	4%	9%	12%	31%

18. Does your organisation currently – or does it intend to – use its offshore capabilities to generate revenue by offering services to other firms?

We will not become a profit centre	44%
We are already a profit centre	21%
We intend to become a profit centre	16%
We do not currently offshore	19%

Appendix Survey results continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

19. If your organisation has worked with outsourcing service providers in offshore locations – as opposed to offshoring within the organisation – what are the most important selection criteria when choosing a vendor? Please rate each attribute between 1 and 5, 1 being critical and 5 being unimportant.

	1	2	3	4	5	N/A
Competency/expertise	39%	19%	9%	6%	3%	25%
Reputation/experience/client base	34%	20%	11%	3%	5%	26%
Certifications (quality, security, compliance)	24%	27%	11%	6%	6%	27%
Infrastructure, including scalability and disaster recovery	22%	24%	16%	6%	4%	27%
Cost	18%	29%	18%	6%	5%	25%
Technological, including ease of integration	14%	24%	25%	6%	5%	26%
Cultural alignment	6%	15%	24%	21%	6%	27%
Geographic location	5%	12%	24%	17%	16%	27%

Section 3: Critical operational issues

20. How satisfied is your organisation with its experience of offshoring so far? Please rate each of the following areas between 1 and 5, 1 being very satisfied, 3 being neutral and 5 being very dissatisfied.

	1	2	3	4	5
Level of cost savings achieved	15%	45%	24%	14%	2%
Levels of compliance	14%	34%	41%	11%	0%
Quality of employees in offshore markets	13%	37%	31%	15%	4%
Levels of customer satisfaction	11%	40%	33%	15%	2%
Quality of management data	11%	41%	35%	12%	2%
Levels of performance improvement	10%	38%	38%	11%	4%
Morale of employees in home market	9%	28%	44%	17%	2%
Overall impact	9%	41%	35%	13%	2%

Appendix Survey results continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

21. What are the most effective ways to ensure the retention of offshore employees in an increasingly competitive market? Please choose no more than three answers.

Training and career development opportunities	84%
Performance-related compensation	70%
Higher basic wages	59%
Travel opportunities	19%
Improved medical benefits	16%
No poaching agreements with other firms	9%
Single-shift working patterns	8%
Other (please specify)	4%

22. How satisfied are you with the following elements of successful customer interaction at your organisation's offshore centres? Please rate each of the following between 1 and 5, 1 being very satisfied and 5 being very dissatisfied.

	1	2	3	4	5	N/A
A close working relationship between the business and CRM management teams	10%	29%	28%	9%	1%	23%
Thorough understanding of products and services	10%	27%	34%	10%	1%	18%
Real-time access to customer data and analytics	7%	34%	25%	9%	3%	22%
Data analysis skills within the customer-contact teams	5%	31%	32%	11%	0%	21%
Developed understanding of customers' cultural expectations	5%	20%	39%	15%	1%	20%

23. Which of the following risk management processes and controls does your organisation have in place at its offshore operations? Please select all that apply.

We have a designated on-the-ground manager with responsibility for risk management at each offshore centre	55%
We have an oversight committee charged with looking at all our offshore operations	49%
We have a local audit/risk management committee at captive operations	45%
We have change authorisation processes that require approval from the home market	44%
We are holding capital specifically against the operational risks associated with offshoring	22%
Other (please specify)	5%

Appendix Survey results continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

24. Which measures are most effective at ensuring the security of intellectual property and data privacy at offshore centres? Please choose no more than three answers.

Physical access-control measures (swipe cards, etc.)	61%
Secure data transmission protocols	51%
Data storage on servers in home market	49%
Non-disclosure agreements for all staff	42%
Background checks for all staff	30%
Close on-site supervision of employees	20%
Third-party security monitoring organisation	17%
Other (please specify)	4%

25. How quickly did your organisation realise cost savings as a result of offshoring? Please indicate the percentage change in its cost base, relative to its cost base when it first offshored.

	Increase in costs	No change	Up to 5% savings	5-10% savings	10-20% savings	20-30% savings	More than 30% savings
Year 1	32%	24%	17%	10%	6%	5%	7%
Year 2	6%	24%	24%	19%	11%	11%	5%
Year 3	2%	16%	18%	24%	24%	12%	5%
Year 4	3%	13%	13%	22%	27%	15%	7%
Year 5	2%	15%	9%	13%	32%	20%	9%

Appendix Survey results continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

26. In each of the following areas, please state whether your organisation incurred more costs than expected, fewer costs than expected or as much cost as expected, relative to the initial offshoring business plan.

	Greater cost	As planned	Less cost
Quality control	35%	58%	7%
Transitioning	32%	60%	8%
Project management	25%	63%	12%
Compliance	25%	62%	13%
Impact on upstream and downstream processes	22%	64%	15%
Retraining, outplacement and redundancy in home market	20%	62%	18%
Labour costs	15%	59%	26%
Taxation/VAT/GST	8%	73%	19%

27. Once initial efficiency gains have been realised, how can organisations best ensure the ongoing delivery of value from offshore operations? Please choose no more than three answers.

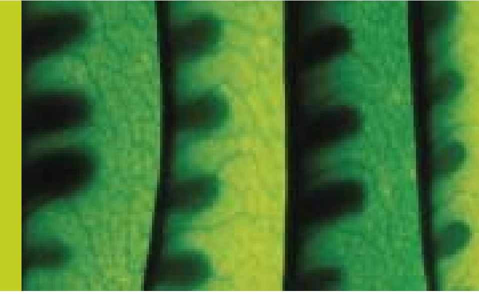
Performance-based compensation for offshore staff and managers	56%
Clear career progression within wider organisation for outstanding offshore staff	47%
Offshoring functions higher up the value chain	41%
Decentralisation of offshore operations, enabling local innovation	39%
Reducing cost by outsourcing offshore operations to third-party suppliers	34%
Insourcing the operations of other organisations	20%
Other (please specify)	3%

Appendix Survey results continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

28. What are the principal barriers to the offshoring of higher-value activities (research, analysis, client relations, higher-value finance roles)? Please choose no more than three answers.

Confidentiality and privacy concerns are greater	46%
Insufficiently skilled offshore staff	39%
Insufficient understanding of the core business in offshore locations	37%
Cost savings are eroded because of higher wages of skilled staff	23%
Difficulties in communicating/liaising with colleagues in home market	22%
Language and cultural barriers have greater impact on higher-value activities	21%
Reputational risk concerns in home market	20%
Higher redundancy costs in home market	19%
Benefits of scale do not apply to higher-value activities	18%
Union opposition in home market	10%
Potential impact of having to exit is greater	9%
Heavier regulatory and compliance requirements in home market surrounding these roles	8%
Other (please specify)	4%



Contacts

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

If you would like to discuss any of the issues raised in this briefing in more detail please speak to your usual contact at PricewaterhouseCoopers or call one of the following:

Offshoring in the financial services industry: Risks and rewards

Editorial board

Enrique Babis
54 11 4850 6822
enrique.babis@ar.pwc.com

Thomas F Barrett*
1 617 530 7363
thomas.f.barrett@us.pwc.com

Uday Bhasin
971 4 304 3313
uday.bhasin@ae.pwc.com

Rahoul Chowdry*
61 2 8266 2741
rahoul.chowdry@au.pwc.com

Richard Collier*
44 20 7212 3395
richard.collier@uk.pwc.com

Ian Dilks*
44 20 7212 4658
ian.e.dilks@uk.pwc.com

Joe Duffy
1 267 330 2200
joe.duffy@us.pwc.com

Tony Elgood
44 117 930 7025
anthony.b.elgood@uk.pwc.com

Darryl Evans
44 20 7212 1656
darryl.f.evans@uk.landwellglobal.com

Joydeep Datta Gupta
91 33 2357 3417
joydeep.datta.gupta@in.pwc.com

Duncan Harwood
1 214 754 7244
duncan.harwood@us.pwc.com

Paul Horowitz
1 646 471 2401
paul.j.horowitz@us.pwc.com

Rossana S Javier
632 459 3016
rose.javier@ph.pwc.com

Jiri Klumpar
420 251 152 077
jiri.klumpar@cz.pwc.com

Niall Mowlds
44 20 7804 0866
niall.mowlds@uk.pwc.com

Dominic Nixon*
65 6236 3188
dominic.nixon@sg.pwc.com

Frans Oomen
31 20 568 4781
frans.oomen@nl.pwc.com

Jairaj Purandare
91 22 5669 1400
jairaj.purandare@in.pwc.com

* Member of the Global Financial Services Leadership Team

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

Offshoring in the financial services industry: Risks and rewards

Editorial board continued

Robert M Ross
852 2289 8499
robert.m.ross@hk.pwc.com

Marie-Hélène Sartorius
33 1 56 57 56 46
marie-helene.sartorius@fr.pwc.com

Robert Scott
1 416 815 5221
robert.w.scott@ca.pwc.com

Sanjoy Sen
44 121 265 6714
sanjoy.sen@uk.pwc.com

Mark Speller
44 20 7213 1154
mark.k.speller@uk.pwc.com

Mark Stephen
44 20 7804 3098
mark.stephen@uk.pwc.com

John Tattersall
44 20 7212 4689
john.h.tattersall@uk.pwc.com

Ronald van Remoortere
31 30 219 5360
ronald.van.remoortere@nl.pwc.com

Nigel J Vooght*
44 20 7213 3960
nigel.j.vooght@uk.pwc.com

Patrick M Wall
353 1 704 8602
pat.wall@ie.pwc.com

Hajime Yasui
81 3 5532 3041
hajime.yasui@jp.pwc.com

* Member of the Global Financial Services Leadership Team

Contacts continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

Global Financial Services Leadership Team

Jeremy Scott
Chairman, Global Financial Services Leadership Team
44 20 7804 2304
jeremy.scott@uk.pwc.com

Thomas F Barrett
1 617 530 7363
thomas.f.barrett@us.pwc.com

Etienne Boris
33 1 56 57 10 29
etienne.boris@fr.pwc.com

Javier Casas Rúa
54 11 4891 4550
javier.casas.rua@ar.pwc.com

Diana Chant
1 416 365 8207
diana.chant@ca.pwc.com

Rahoul Chowdry
61 2 8266 2741
rahoul.chowdry@au.pwc.com

Ron Collard
44 20 7212 6827
ron.p.collard@uk.pwc.com

Richard Collier
44 20 7212 3395
richard.collier@uk.pwc.com

Ian Dilks
44 20 7212 4658
ian.e.dilks@uk.pwc.com

Simon Jeffreys
44 20 7212 4786
simon.jeffreys@uk.pwc.com

Chris Lucas
44 20 7804 9652
christopher.g.lucas@uk.pwc.com

David Newton
44 20 7804 2039
david.newton@uk.pwc.com

Dominic Nixon
65 6236 3188
dominic.nixon@sg.pwc.com

Phil Rivett
44 20 7212 4686
phil.g.rivett@uk.pwc.com

Tim Ryan
1 646 471 2376
tim.ryan@us.pwc.com

John S Scheid
1 646 471 5350
john.scheid@us.pwc.com

Nigel J Vooght
44 20 7213 3960
nigel.j.vooght@uk.pwc.com

Akira Yamate
81 3 5532 2518
akira.yamate@jp.pwc.com

Contacts continued

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

Economist Intelligence Unit (EIU)

111 West 57th Street, New York, NY 10019

Andrew Palmer
44 20 7830 1149
andrewpalmer@eiu.com

Nigel Gibson
44 1825 791 474
nigel.gibson@btinternet.com

PricewaterhouseCoopers Global Financial Services Briefing Programme

- Contents
- Executive summary
- At the crossroads
- The costs of offshoring
- Regulators ahoy
- In-house or outsourced?
- Where? The offshore locations of tomorrow
- Conclusion
- Appendix: Survey results
- Contacts
- PricewaterhouseCoopers Global Financial Services Briefing Programme

- **Wealth management at a crossroads: Serving today's consumer –** November 2001
- **Economic Capital: At the heart of managing risk and value** – March 2002
- **Taming uncertainty: Risk management for the entire enterprise** – July 2002
- **Risk Management Survey – A follow up to Taming uncertainty: Risk management for the entire enterprise** – November 2002
- **The trust challenge: How the management of financial institutions can lead the rebuilding of public confidence** – December 2002
- **Illuminating value: The business impact of IFRS** – April 2003
- **Compliance: A gap at the heart of risk management** – July 2003
- **Focus on restructuring: The drivers shaping the financial services sector** – December 2003
- **Governance: From compliance to strategic advantage** – April 2004
- **Uncertainty tamed? The evolution of risk management in the financial services industry** – August 2004
- **From aspiration to achievement: Improving performance in the financial services industry** – December 2004
- **Focus on growth: Striking the right value balance within financial services** – May 2005
- **Offshoring in the financial services industry: Risks and rewards** – September 2005

PricewaterhouseCoopers (www.pwc.com) provides industry-focused assurance, tax and advisory services for public and private clients. More than 120,000 people in 144 countries connect their thinking, experience and solutions to build public trust and enhance value for clients and their stakeholders.

The Financial Services Briefing Programme is produced by experts in their particular field at PricewaterhouseCoopers, to address important issues affecting the financial services industry. It is not intended to provide specific advice on any matter, nor is it intended to be comprehensive. If specific advice is required, or if you wish to receive further information on any matters referred to in this briefing, please speak to your usual contact at PricewaterhouseCoopers or those listed in this publication.

For information on the PricewaterhouseCoopers Global Financial Services Briefing Programme please contact Áine O'Connor, Director, Head of Global Financial Services Marketing, on 44 20 7212 8839 or e-mail at aine.r.oconnor@uk.pwc.com

For hard copies please contact Alpa Patel at PricewaterhouseCoopers on 44 20 7212 5207 or e-mail at alpa.patel@uk.pwc.com