





Driving growth through Business Process Outsourcing (BPO)

Financial institutions (FIs) have long considered Business Process Outsourcing (BPO) as an instrument for improved cost efficiency. The market has reached maturity and best practices established over time by vendors and advisors have increased the success rate of BPO relationships.

Some domains of the financial industry such as investment management and asset management have already opted for outsourcing certain processes and nowadays include it as part of their business models. However, other industries such as private banking and retail banking are not yet versed in outsourcing. It may be that outsourcing could provide the solution for banks' evolution in their highly competitive climate.

Moreover, BPO does not only offer a greater cost efficiency. As market conditions and technologies have evolved, outsourcing has followed suit to offer new adapted solutions, answering many challenges faced by banking industry actors. From increasing the level of digitalization to offering new value-adding services, how can your organization drive growth through outsourcing? ➤

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Banks are racing on a slippery track

Banks evolve in turbulent context and are facing several challenges that need to be addressed in order to ensure future profitability.

Bad weather on race day

In the wake of the financial crisis, the low interest rate environment has greatly narrowed the bank's margins. In the meantime, European financial institutions need to comply with an increasing number of regulations, many of which come at a cost. The increased governance and compliance expenditure is especially hard for small banking organizations to absorb, as they lack the economies of scale.

The public expects a great show

They are paying the price to attend the race and will back the winner. Banks' customers have rising expectations and higher customer experience standards. Banks are no longer solely compared to their industry peers, but also to GAFA (Google Apple Facebook Amazon), who offer best in class user experiences and customer centric services that can be accessed anytime and anywhere. Banks must get up to speed and meet these new standards of services.

New racers with improved engines

There are new competitors that take the form of FinTechs. They are built from the bottom up, using the latest technology, with customer care at their core. They are also able to leverage data analytics to bring additional value to the customer. These new entrants are agile because they are free from legacy technologies and can therefore offer highly competitive rates to the customer as they benefit from low operational costs.

This context creates lagging growth in the financial industry and builds up the need for strategic decisions to drive more cost efficiency and identify new streams of revenue.



52 percent of investors are willing to change their current wealth management provider if they continue to fail to meet their current expectations¹.

Focus on piloting: outsourcing the mechanical work to third parties and increasing cost efficiency

With margins being squeezed on all fronts, banks need to find ways to increase their cost efficiency. Outsourcing of back office and non-core functions permits significant reduction in operating costs. Outsourcing business processes to external partners helps to free up time, financial resources and managerial efforts. These can be reallocated to value-generating business processes.

Advantages of outsourcing

- **Reduced costs:** cost reduction is the main driver for BPO; it is achieved by leveraging the partner's economies of scale, whilst reducing the headcount
- **Increased flexibility:** outsourcing transforms many of the fixed costs into variable costs, thus providing more flexibility for the business. Likewise, whether your business is growing or decreasing in size, the BPO partner will scale accordingly in order to meet your business requirements

What is Outsourcing?

Outsourcing is the contracting out of the management and enhancement of business function to an external partner that can involve the transfer of people, processes, assets, and definitely responsibilities.

- **Refocus on core business activities:** BPO allows to refocus both efforts and financial resources on core business activities, and to deliver additional value to the customer
- **Enhanced service quality:** By leveraging the knowledge and the expertise of a partner, the quality of the outsourced process' output increase
- **Favorable regulatory framework:** The European financial industry regulators keep creating legal frameworks that ensure that the outsourcing providers are regulated to the same extent as financial institutions. Such a practice reduces the regulatory risk associated with outsourcing and prevents customers' data mishandling ➤

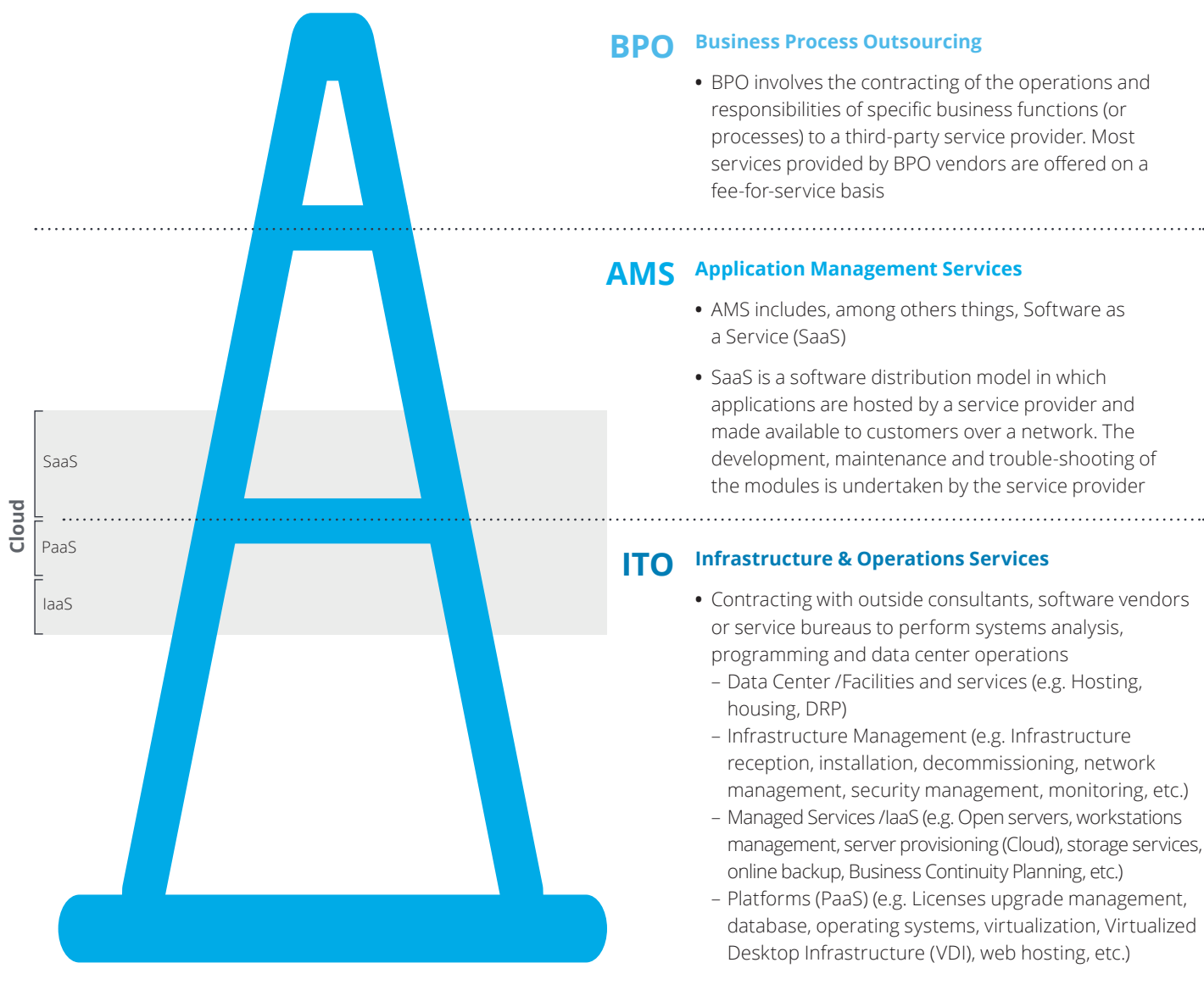
¹ Roubini, Wealth and AM 2021



Identify the parts to outsource

According to the individual situation of the bank and its goals, improvements can be targeted through various types of outsourcing, such as the IT Outsourcing (ITO), Application Management Services (AMS), and Business Process Outsourcing (BPO).

Figure 1: Types of outsourcing



There are multiple examples of banks looking for a BPO provider that is also able to offer ITO and AMS. We can see some factors steering towards this type of global outsourcing, such as the continuous regulatory changes that require sophisticated IT process remodeling on the one hand and the maintenance of applications and renewal of IT licenses on the other hand.

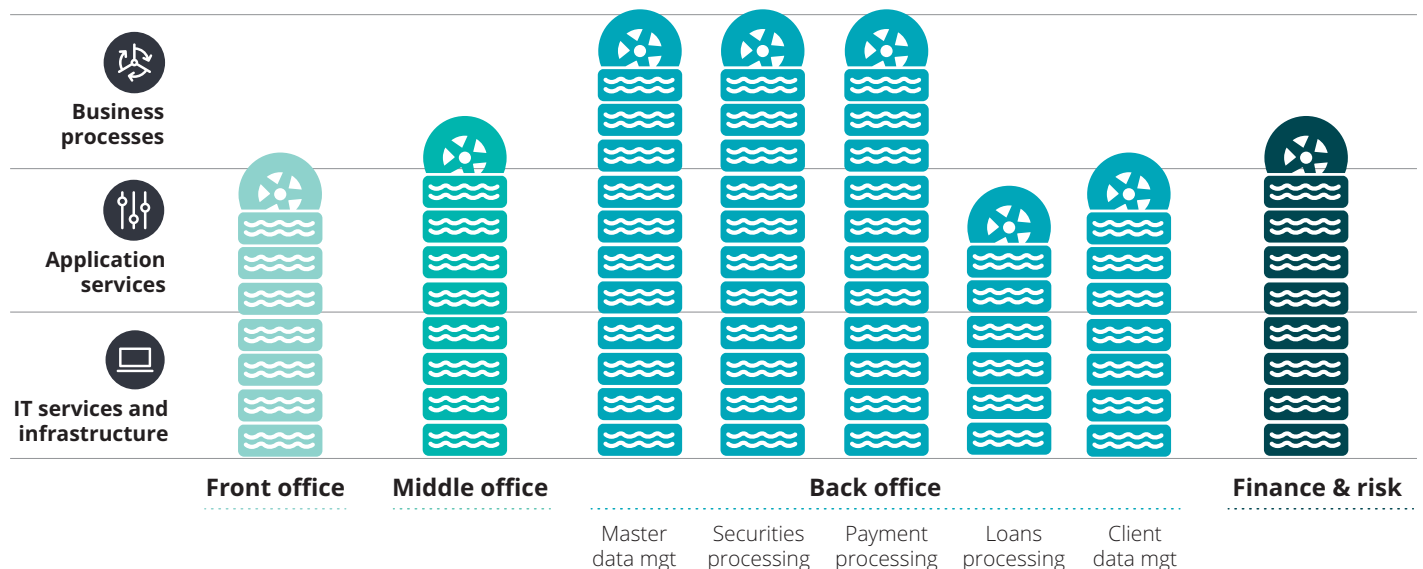
There are different levels of outsourcing as we can see in Figure 2 and the selection is among generic functions as opposed to strategic or knowledge based functions. The latter should be retained in-house in order to remain in control. Nevertheless, it is part of best practice to establish more centralized or mutualized service centers (Center of Competence, Center Of Excellence). ➔

Commonly outsourced functions:

In the financial industry, outsourcing has reached great maturity for all back office and IT processes. The decision makers that have not carried out, or at least considered, outsourcing some internal functions are rare. BPO is not limited only to back office perimeter anymore but outsourcing also reaches the front office.

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Figure 2: BPO/Outsourcing scope





Most commonly outsourced functions:



Private banking

Master data management, case processing, securities processing, loan processing, client data management, regulatory and client reporting, trading, dealing processing, credit scoring, AML/KYC and invoicing, tax reclaim.



Asset management

Valuation and accounting, custody and settlement, client servicing and reporting, treasury and cash management, compliance and regulatory reporting.



Retail Banking

Procurement, Payment, Mortgage, Accounting.

Activate your cruise control: let the robots do the work

Emerging technologies are expected to drive the cost of outsourcing down. Indeed, many of the outsourced processes are rule-based and highly repetitive. These tasks are costly because they have the tendency to be time-consuming. Moreover, they are tedious and provide low job satisfaction to the person executing them. The solution therefore lies in automation. BPO vendors that plan to automate their processes will gain competitive advantage, by offering more competitive prices, and reducing both error rates and time to deliver. Thus, your pit-stops will be faster, better, and cheaper.

What criteria to investigate when selecting a BPO partner

As BPO contracts typically span over five years, it is essential to choose the right partners. Depending on the business process to be outsourced, criteria may vary, but we have selected seven key areas to look into when selecting a BPO provider.



Level of expertise and service offering

One of the main advantages of setting up a BPO partnership is the value that will be derived from the BPO vendor's knowledge and expertise. Building on that knowledge will permit an increase in the quality of the outsourced functions' output and in the time to deliver the desired output. Therefore, when choosing a partner, it is important to assess their level of experience, inquire about their other clients, and the nature of their existing BPO partnerships



Flexibility

If your business expects a growth or a decline in the quantity of output required, it is important to ensure that your partner will be able to keep up with your requirements. Does the provider's pricing models allow for flexibility? Are they capable to support a rapid growth in demand?



Strategic development plan

Your partner's strategic development plan for the next five years should be assessed. Does it seem achievable? Is there any chance that the level of services provided will decrease over time because of the vendor's decision to free up resources to focus on other strategic projects?



Financial health

What is the potential partner's financial health? The risk of bankruptcy faced by the potential partners should be evaluated. Do they have important debt ratio, are they profitable, do they have liquidity problems? Is the partner part of/backed by a big group that could provide financial help if threatened by bankruptcy?



Compliance/security

As the chosen partner will most likely gain access to protected data, it is vital to ensure that the partner is compliant in all aspects. A non-compliant partner will put your whole organization at risk. Is he well aware and prepared for incoming regulations? What is his timeline to implement them?



Digitalization/innovation and the inherent risk of disruption

Besides the need to investigate the vendor's current technologies, it is also crucial to investigate the vendor's future development plans in terms of technology and capability. This is especially important since BPO contracts span on several years. Thus, at a time of such rapid technological shift it is important to scrutinize the market, looking for potential disruptors.



Location

What are the partner's current location? Is he present in the country where you operate? The impact will be on his capability to understand and comply with your regulatory obligations. ➔



Outsourcing digital transformation is about adding digital capabilities, by implementing out-of-the-box solutions, developed by third parties.

BPO: helps you stay on the track

New technologies, evolving market conditions, and pressure from clients have paved the way for the development of a completely new branch in the outsourcing field. It now provides an answer to pressing strategical challenges faced by Banks. From the digitalization of services to the addition of new capabilities, outsourcing can help drive your company's growth.

Regardless of their size, financial institutions will have to embrace the digital turn in order to keep thriving. While the bigger incumbents may choose to develop digital capabilities internally, or even lead their transformation through acquisitions, it is not an option for the smaller players lacking the resources and expertise to lead such transformation strategies. Their best alternative is therefore to outsource their digital transformation. Indeed, new players have emerged, proposing agile modern and scalable solutions built with the customer's needs at their core. Successful

Fls are those that will team up with them to build the right network of partners. These partners will provide the technology, take care of the maintenance, and let the financial professionals focus on what they do best—providing the best services to the customer.

Outsourcing digital transformation is about adding digital capabilities, by implementing out-of-the-box solutions, developed by third parties. This permits great cost savings (R&D and hiring costs) and shorter time-to-market, which is mostly determined by the time of implementation. Consequently, it is a particularly good solution for companies that have made limited efforts to digitalize their offerings, as it permits them to catch up quickly on their delay. In fact, a global asset manager survey found that 40 percent of the digital laggard asset management companies plan to outsource their digital development work.

Due to the strategical considerations involved in outsourcing digital transformation, the decision to outsource should not be assessed through the sole lens of cost reduction; it should be considered as an investment, on which a return is expected. The real currency here is the amount of additional value brought to the customer, which through increased satisfaction and increased customer loyalty, leads to greater revenue.

Thus, outsourcing allows banks to lead their digital transformation with a very short time to market, while staying cost efficient.

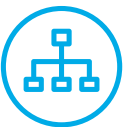
Understand the associated risks

Although the outsourced processes are usually non-core business activities, they are vital to the organization. Moreover, FIs must control and mitigate their reputational risks: delegating responsibilities to a third party does not free the FIs from their duties towards clients. Therefore, there are always risks involved in BPO, and they must be properly assessed and managed.



Control loss

Control loss is more of a consequence than a risk, but it becomes a risk when mismanaged. When outsourcing processes to a third party, you inevitably lose some control over the carrying out of the process. To mitigate this risk, the right Service Level Agreements and the right governance model must be established.



Dependency

Relying on a partner to carry out some of your business processes can make your organization dependent on the partner. Outsourcing may lead your organization to lose its knowledge and expertise regarding the outsourced processes. This creates a certain dependency, as your organization is no longer able to take over the process, or it lacks the expertise to assess the quality of the output provided.



People risk

During the transformation phase, in-house employees in charge of the processes to be outsourced are unsure what a BPO means for them and their jobs. This uncertainty can lead to demotivation and productivity losses. To mitigate this risk, it is important to ensure clear communication with the employees who will be affected by the BPO, to listen to them and to take their concerns into account.



Risks of disruption

In a BPO strategy, where contracts span over five years, the increasing speed of innovation and the growing role played by technology paves the way for the risk of disruption. It is costly and complicated to renegotiate a BPO contract in place. Therefore, there is a risk that a new player disrupts the way one of the processes is carried out by our BPO partner, offering to do it at a much lower price.



Unforeseen costs

When building the business case, two aspects must be taken into account. On the one side, there is the cost of transformation, and on the other side, the cost of operations. Discrepancy in either one of these cost forecasts often arises due to overly optimistic projections.

Conclusion

BPO can offer organizations a new-found flexibility, external insights, and not to mention the benefit of reduced costs. It is however important to remain informed and aware, with a view to mitigating any possible risks, as mentioned above. With this formula, collaboration between FIs and their outsourced counterparts will no doubt lead to a fruitful end result. ●