Taking captive offshoring to the next level

Captive offshore operations centers could create vast value beyond traditional efficiencies. To do so, they must change their operating model.

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Captive offshoring is coming of age. Our research[1] shows that operation centers that are located in low-cost countries and are owned and managed by the corporations they serve are not only pushing the boundaries on cost, productivity, and quality. They are also beginning to drive superior customer experience and provide consumer insights that aid product managers in making better decisions.

Business leaders now expect managers of their offshore centers to build the next generation of high-performing captive operations. When doing so, they must find ways to deliver further efficiencies as well as added value to the business while navigating growing operational complexity and reforming a traditional back-office culture.

Evolving sophistication

Over the last decade, head count in captive centers has grown at a compound annual growth rate of 13 percent. These centers now employ almost half a million people across shared business services, IT, and engineering and R&D. Our survey of nearly 1,200 business leaders and managers using the services indicates high satisfaction with their captive offshore operations centers—83 percent are either satisfied or highly satisfied with performance. What's more, nearly 65 percent of respondents said they were likely to increase staff at their offshore operations by at least 15 percent in the next two to three years. Perhaps more important, almost 70 percent were likely to increase the role of advanced skills in the work done offshore.

[1] Over the last six years, we benchmarked the operating performance (for example, productivity and cost of delivery) of more than 250 captive offshore centers in low-cost locations like India and the Philippines. In parallel, we surveyed nearly 1,200 business leaders and managers about their level of satisfaction with their center's services and the maturity of its operating practices. We also interviewed about a third of the survey respondents and conducted deep dives on the processes in the centers.

Takeaways

Captive offshore centers have grown steadily over the last decade: they now employ almost half a million people. They have also expanded the scope of their services, requiring staff with a high level of business understanding and analytical skills.

While their owners' top priority is still productivity and cost, increasingly, they also want their operations centers to help improve business outcomes. This new complexity calls for less focus on incremental improvement and more on entrepreneurial leadership.

To capture the full opportunity, managers must rethink their operating models so that they promote not only sustained value through efficiencies but also improve the customer experience and increase revenue.

Offshore centers have rapidly expanded the scope of their services. Nearly a quarter of the work delivered requires a high level of business understanding and analytical skills, for example, in modeling natural calamities and their impact on the pricing of insurance products, remote relationship management with affluent banking customers, and financial planning and budgeting for the enterprise. Four years ago, less than 10 percent of the work offshored required such complex skills and deep business-domain knowledge. Multiple forces are contributing to this shift: the growing experience of middle management in the centers, frontline teams' deeper understanding of the business, and a trend of greater collaboration—across operations and technology—with teams housed in the offshore center, to convert data into insights and insights into actions. For example, an HR shared-services center accepted the help of an offshore technology team to create standardized forms for each type of employee query coming into the center. The standardized forms helped ensure that all requests were completed, leading to a 30 percent productivity increase for the request-fulfillment team and a 90 percent reduction in backlog.

Challenges to achieving the full potential

Business stakeholders' top priority is still cost and productivity, but they are now almost equally set on their offshore operations owning and driving business outcomes, such as increased revenue and an improved end-customer experience. This dual priority is challenging because it requires managers in offshore centers to influence stakeholders and processes beyond the four walls of the centers, as opposed to simply delivering according to specified standard operating procedures. To meet these expectations, captive centers must address two major constraints.

First, shared-services networks are becoming more complex. Only four years ago in India, which hosts more than two-thirds of captive offshore centers globally, 70 percent of the offshore centers were located in one or two cities. Now nearly half of the centers have a presence in three or more cities within India. Additionally, more than half of the enterprises that have a significant offshore presence in India have a two-country offshore location strategy. What's more, the number of enterprises that use a combined captive and third-party sourcing model—in order to have greater flexibility, scalability, and focus—has doubled from 20 percent in 2008 to 40 percent in 2012 (Exhibit 1).

The increasing complexity of shared-services networks is leading to further fragmentation of processes, with multiple cross-border handoffs across the processing value chain. It is commonly observed that even a standard-

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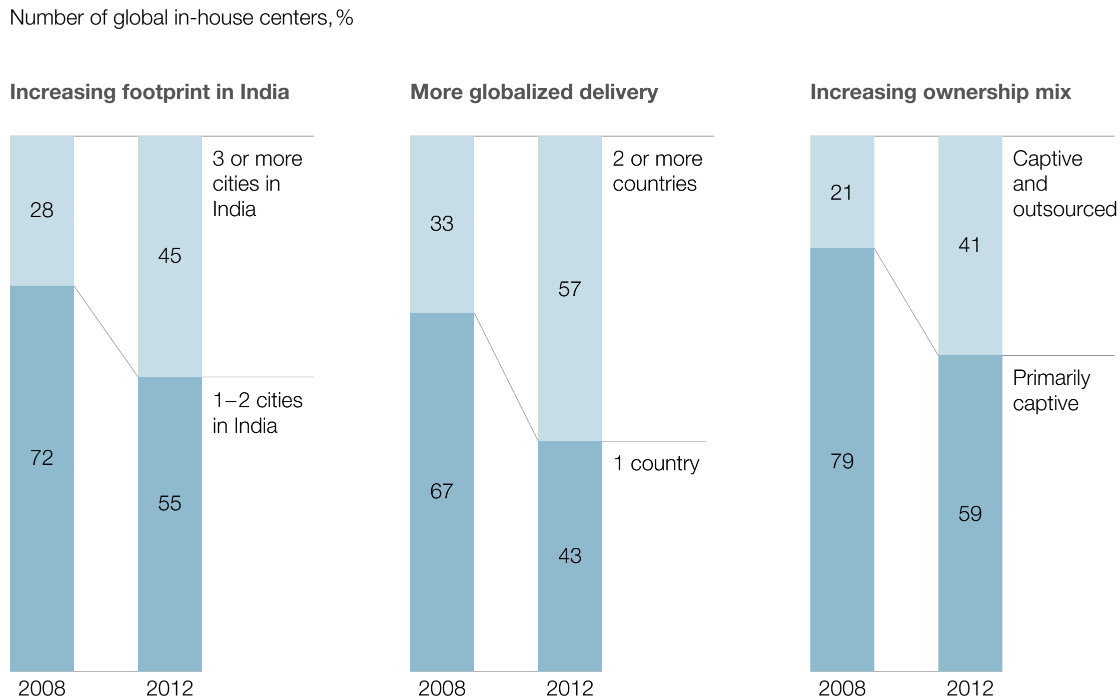
Exhibit 1
Network and operational complexity is rising rapidly.



ized transaction like issuing a credit card is processed in three countries before the card is delivered to the customer (Exhibit 2). Delivering value beyond labor-cost arbitrage in such a distributed footprint is challenging. Most offshore centers have a limited end-to-end view and limited control of the process. In such a setup, driving meaningful performance shifts requires greater coordination and management bandwidth. A leading insurance company addressed this issue by creating cross-border teams whose operations report to a manager located in its offshore center. And at a financial institution, the chief operating officer is also head of the company's offshore center. This has helped break cross-border silos and instill a customer focus in the teams involved.

The second constraint is that many captive centers continue to operate with a deeply rooted culture focused on incremental improvements. Centers reward meeting operational service-level agreements (SLAs) and offer limited incentives or encouragement for driving innovation and change. Some centers have also found it difficult to attract, retain, and develop entrepreneurial leaders who are focused on improving the business and not just meeting the SLAs. One onshore business executive that we interviewed said, "Leaders need to have an idea of what we need not only tomorrow but also three to four years in the future. I don't need to know what we can do to improve our SLAs—but rather what we can do to improve our business."

To address this problem, captive offshore centers need to develop entrepreneurial leaders who are encouraged to take initiative. One center has started a program to develop leaders who are accountable and given incentive to have an impact on business outcomes and to change the culture of the offshore center.

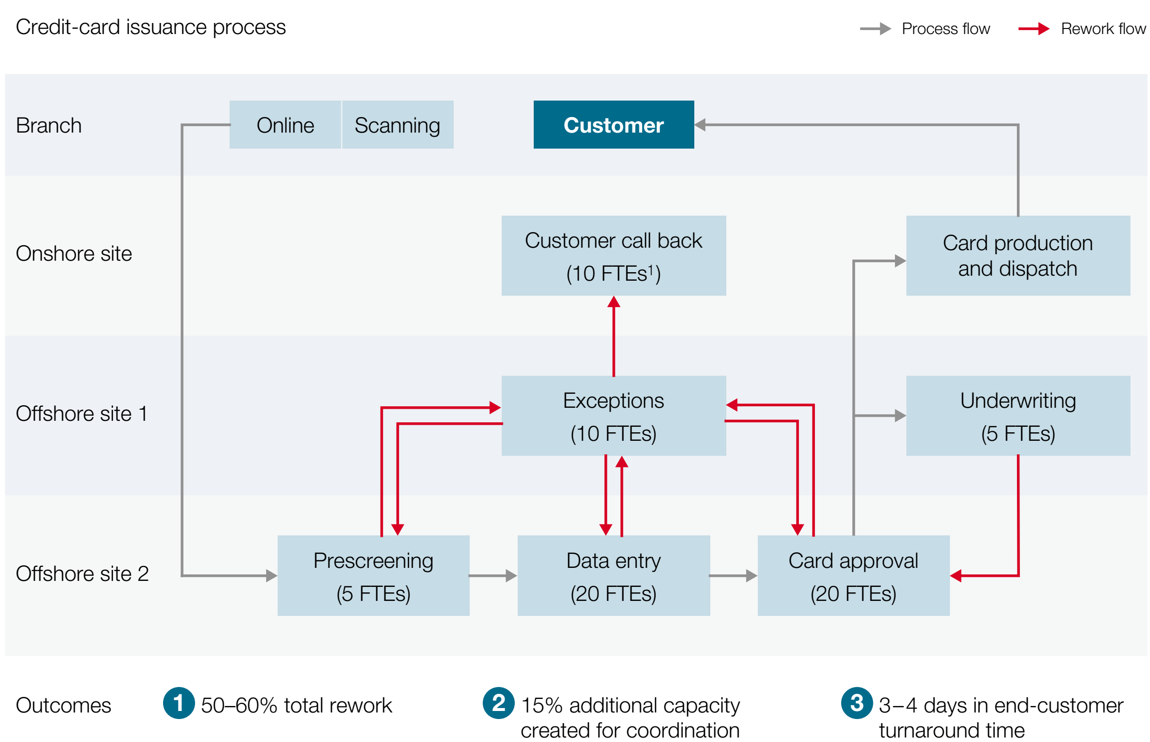
Capturing the opportunity

Despite the challenges, our analysis suggests that captive offshore centers will continue to grow in stature and strategic relevance.

To capture the full opportunity, managers must rethink the operating model so that it promotes higher and sustained value through efficiencies as well as improved business outcomes.

Offshore managers should continue to emphasize cost control and productivity to remain relevant to their enterprises. They should also move beyond traditional back-office responsibilities and offer services to front-end sales and product-development teams. This means improving capabilities such as pricing and consumer analytics that can support better decision making.

Exhibit 2
Fragmented end-to-end processes make improving efficiency and business outcomes challenging.



[1]Full-time equivalents.

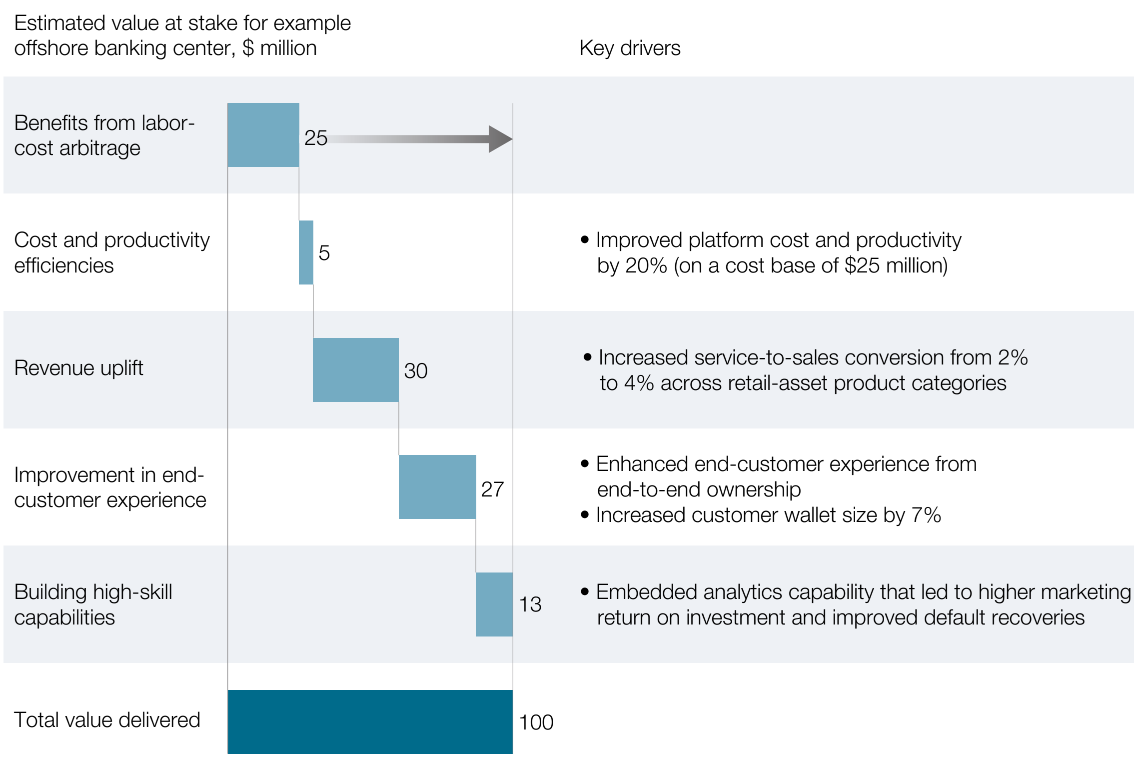
Leaders of captive offshore centers should also aim to own and help manage end-to-end processes in order to deliver a superior customer experience. This involves measuring and optimizing the time spent addressing customer-service requests as well as creating recovery desks empowered to help customers with service issues. Finally, they should focus on operations that can generate revenue, for example, by increasing product cross-selling through call centers.

Leading companies are already beginning to make steady shifts in these areas. For example, a high-tech enterprise has built a dedicated high-skill offshore center of more than 1,000 employees specializing in consumer and market intelligence and in developing proprietary models to improve sales-force effectiveness.

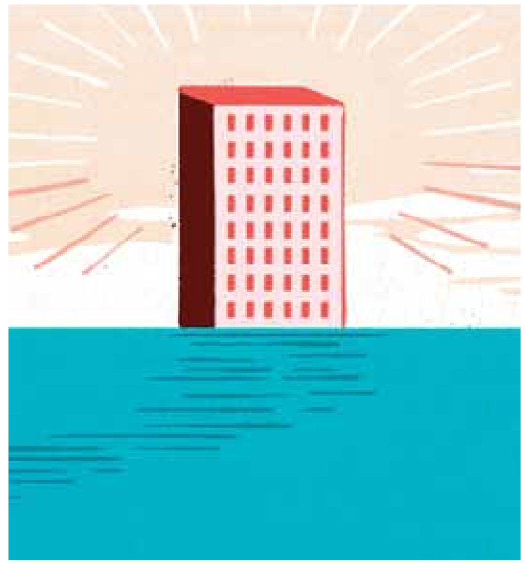
Similarly, a financial-services captive with more than 500 employees created on-demand and fee-based advisory and analytics services for internal and outsourced sales teams to help them offer more value-added products to customers. The analytics allowed the sales teams to minimize operational tasks and spend more time in front of the customer.

Exhibit 3

The potential value at stake is three to five times that of labor-cost arbitrage.



Another center, this one in the telecom and media industry, found that new customers have different needs than older ones in areas such as product use and fees. As a result, the center created a separate system to lead new customers through the process, resulting in a 70 percent reduction in complaints from new customers.



For enterprises and their captive offshore centers, the opportunity is too big to miss. Our analysis of a banking captive center with about 1,000 employees suggests that the potential value at stake could be three to five times that of labor-cost arbitrage (Exhibit 3).

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Captive offshore services centers have a tremendous opportunity to play a more strategic role for their enterprises. Making this shift calls for concerted efforts from both the enterprise and the leadership team in the captive organization to align the aspirations and operational priorities of the center and manage the constraints of growing complexity and a traditional back-office mind-set. o

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