

Making the Case: The Value of BPO in a Tough Economy

In a deep economic downturn, the instinct at most companies is to slash costs. Some have no choice. Their revenues have dropped so severely that overheads, especially labor, must be reduced immediately.

But for companies with some financial latitude, there is a better way: apply tighter scrutiny, investing only in initiatives that generate immediate cash, or those that position you to leap ahead of competitors when the upturn comes.

It's ideal to do both, and business process outsourcing (BPO) could be the answer. It's a way to generate immediate cash while improving business flexibility and scalability for the future.

Re-Setting Expectations

We have come through a period of strong and sustained economic growth, but not sustainable growth. As we know, much recent growth was propelled by speculation and lax credit terms.

The Business Process Outsourcing industry continues to grow during the downturn because it offers a route to flexibility and scalability.

Our reality today is much different. True growth will be harder to achieve even after faith returns to markets. In many industries, expectations are being re-set quite dramatically.

The businesses with the gravest challenges are those with inflexible operational models, such as manufacturers. In retailing, the field is split. Leading companies -- Wal-Mart is the best example -- have invested in their ability to respond efficiently to demand-to-supply signals. Others, with inflexible processes, are struggling.

The Business Process Outsourcing industry continues to grow during the downturn because it offers a route to flexibility and scalability. And the benefits are many, particularly with the outsourcing of business processes.

BPO: Spending Less To Gain More

"BPO involves handing over a segment of your business processes that you don't do any better than anybody else," explains Kaushik Bhaumik, VP and Global Head of Cognizant's BPO practice. "You have the opportunity to partner with a service provider that has access to greater scale, greater cost efficiencies, and greater technological capabilities. The goal is to gain an advantage in the marketplace while turning your internal resources to core capabilities that will further differentiate and build your business."

Technology outsourcing has been on a steady growth trajectory since the early 1980s because successful outsourcing relationships confer numerous benefits. In addition to significant savings, outsourcers enable companies to focus on their core business while providing access to talent and knowledge, operational expertise, scalable cost structures, and quality and performance improvements.

BPO has been called "back-office outsourcing" because it often involves processes related to traditional back office functions such as finance, accounting, payroll, and HR. Growth in BPO has come with more functions being outsourced, including such things as claims processing and fraud detection for insurance companies and research data processing work for healthcare companies.

According to McKinsey, the global "addressable" BPO market in 2009 is projected to be between



\$122 billion to- \$154 billion. The largest segments are retail banking (\$35 billion to \$40 billion), insurance (\$25 billion to \$35 billion), travel and hospitality (\$10 billion to \$12 billion), automotive (\$10 billion to \$12 billion), telecoms (\$8 billion to \$10 billion), pharmaceuticals (\$8 billion), and others (\$10 billion to \$12 billion) with finance, accounting, and HR accounting for \$20 billion to - \$25 billion.

BPO has also been called “business-enabling outsourcing” because its key advantages are flexibility and speed of business processes.

How can a company tell if its business processes should be outsourced or not? “Aggressive benchmarking and comparison will show whether you are the same, better, or worse than others at a particular function,” says Bhaumik. “Because of the economic downturn, that process is right now underway at many companies that have to do something to rationalize their operations costs.”

Generating Immediate Cash

Immediate cash. Longer-term advantage. On those two critical levels a BPO strategy is likely to pass scrutiny for many companies today.

Cash flow is badly needed. For so many companies, decreased demand has hurt revenues and their ability to repay debt and support overheads. BPO is a mechanism for immediately increasing cash flow. In years past, the return on outsourcing was often measured in years. Today, because of greater efficiencies and global sourcing available from all the largest providers, cash flow improvements routinely happen within months.

“It’s not your father’s outsourcing,” says Bhaumik. “Our experience at Cognizant is that clients can now save in the range of 30% to 60% off their baseline costs within the first year. That can be a tremendous stimulus to cash flow.”

Cognizant’s recent work with a leading video and gaming rental organization is a case in point. The video company is going through significant restructuring in response to fundamental changes such as the rise of video-on-demand in PCs and cable TV. Consumer traffic is declining at retail locations, so overheads had to come down quickly. The mandate for the project was a major reduction of retail store support costs (for several hundred stores) within six months.

The company worked with Cognizant to outsource systems for live 24x7 store support around staff issues and queries associated with the merchandising and point-of-sale systems. On

those costs, immediate savings were more than 40%. Cognizant has also been able to introduce productivity gains through centralization, better workflow, and call queuing that have provided an additional 10% savings. The company has re-directed some of the savings to fund its own direct-to-consumer video and game initiatives, to better position itself in the rapidly changing consumer entertainment space.

Built-In Financing

The obvious question is: What about the upfront investment in BPO? The transition of knowledge associated with any BPO initiative involves execution costs for both the client and the outsourcing partner.

Bhaumik says programs can be financed so the cash flow benefits flow immediately without an undue capital burden. “With larger BPO programs,” he says, “it is often possible to amortize these costs over the life of an outsourcing contract, providing more cash flexibility to the restructuring organization. Furthermore, an outsourcing partner will sometimes be willing to re-coup its transition costs by bundling it into the price of services rendered, which are often hourly resource-based or transaction based.”

Immediate cash. Longer-term advantage. On those two critical levels a BPO strategy is likely to pass scrutiny for many companies today.

Scaling To Demand

Transaction-based pricing is a way to manage the “demand signal.” The video company faces gradual and predictable erosion. For other companies affected more dramatically by recession, the need is to respond to unpredictable conditions, without knowing when demand will return and by how much. Fixed overheads hurt during idle times. Service suffers during swells of activity.

Programs can be financed so the cash flow benefits flow immediately without an undue capital burden.

Claims processing is an example. In-house claims processing can be costly. Outsourced processing, with a fixed fee per claim, means that ebbs and flows, even large ones, are absorbed by the outsourcer. The demand signals are managed within vast offshore operations by moving work from many customers across many employees, so a relatively steady demand profile is maintained.

Two industries that thrive on outsourced transaction processing are airlines and healthcare. Dynamic pricing has revolutionized the way airlines price seats. Part of that revolution is price-per-transaction outsourcing of bookings and payments. Likewise, in healthcare, providers have been able to take significant cost out of claims processing, which tends to experience seasonal spikes. What was once a fixed cost is “variablized.”

Where BPO gets truly exciting for clients is when it not only pays for itself but uncovers a new profit center.

“Even though BPO is well entrenched, there is still a tremendous amount of potential in the back office realm,” says Bhaumik. “In the back offices of banking, insurance, and health-care companies there are still many fixed processing costs. They’re paying regardless of volume. Those costs can be ‘variablized’ by a trusted BPO partner. It’s a powerful competitive lever at a time when most need to offload their liabilities.”

New Levels of Value

Companies evaluating the business case for BPO have ample evidence strictly on the basis of cost savings and cost “variablization.” But there are a number of other major advantages that make BPO even more valuable during recessionary times.

BPO is an obvious way to improve business performance. And given the sophistication of today’s BPO vendor organizations, even more value is being uncovered each year as discipline, quality, and speed continue to be pushed upward by competition in the marketplace.

Service-level agreements have improved over the years between vendors and their clients. In the early years of outsourcing, SLAs were normally stick-driven agreements which penalized performance that fell below the agreed-upon level. Today, they resemble stick-and-carrot agreements that offer financial incentives when vendors exceed expected performance.

“Even though BPO is well entrenched, there is still a tremendous amount of potential in the back office realm.”

“Today, we are more commonly an extension of the client-partner’s own workforce,” explains Bhaumik. “We work together to achieve beyond the agreed level, and both parties benefit when that happens.”

Speed to market has also increased dramatically in BPO because providers are now able to move work around the world to different time zones.

Routinely, the same work is now done in India, Eastern Europe, Mexico, and China. Companies doing their own in-house work have a window of eight hours during the work day. Outsourced to a global organization, the same work can be done around the clock by as many trained people as are needed. That’s at least a 300% advantage in processing speed.

Data Management Costs Cut in Half

In the pharmaceutical industry, outsourced global services are having a very definite business impact. “Cognizant has been working with one of the world’s leading pharmaceutical companies to dramatically improve its product time-to-market and pipeline,” says Bhaumik. “One of the major strategic challenges facing all pharmaceutical companies is the cost and time associated with bringing a new drug to market, which averages nearly \$900 million and 10 years of research and development. One of the key activities in the clinical-research value chain is clinical data management (CDM), a very intense, complex, and laborious task of managing all data that comes out of clinical trials.

The data must be statistically analyzed for relevant efficacy trends and then submitted to regulatory authorities such as the U.S. Food and Drug Administration (FDA).

“This particular CDM engagement began in 2007 and has fundamentally transformed the client’s clinical operations. Data management has been centralized and streamlined, process standardization has been improved, delivery is more consistent, and there are significant economies of scale. Operating costs have been reduced by at least 50%. R&D cycle times are down 20%. The client has re-invested the savings to support accelerated development of its R&D programs.”

Untapped Profits

Where BPO gets truly exciting for clients is when it not only pays for itself but uncovers a new profit center.

A startling example: Claims payment and management in the healthcare insurance business is time consuming and expensive. There is a threshold -- based on existing in-house processing -- that is unprofitable. It made no financial sense, for example, for one Cognizant client to investigate claims under \$500 for possible fraud. The claim was simply paid.

But a fair amount of fraud occurs, both with patients and physicians, driving up healthcare

premiums for all plan members. Cognizant BPO worked with the payor to identify aberrant billing patterns (ABPs). Twenty-five new fraud patterns were discovered at the below-\$500 level. Under the more cost-efficient BPO model, those claims were worth chasing. The ongoing annual savings: more than \$20 million.

That's not all. BPO clients get the continually increasing benefit of technology and methods sharing. "Since we work with multiple clients," says Bhaumik, "we are able to develop systems and tools -- like the fraud-detection tools -- that we can leverage across multiple projects and engagements. There is a constant 'cycle of innovation' that gets distributed among our clients. That level of innovation almost never occurs with in-house organizations."

Positioning To Win

Many of the benefits of BPO that confer immediate advantage also help position companies for the future. Low-cost operations. Greater flexibility and scalability. Faster time to market. More discipline. Round-the-clock processing. Continuous technology and application development. New profit centers. These are ongoing. To be able to take advantage of this basket of business-enabling possibilities in the midst of an economic downturn can be an extraordinary advantage once the inevitable upturn comes.



Leaders don't stop investing in their future. According to BusinessWeek magazine's 2009 Innovation Survey, many top companies, including Microsoft and GE, continued to maintain aggressive R&D spending through the down side of business cycles. "BPO can yield both the cash and human resources needed for future-looking initiatives," says Bhaumik.

"Reallocating your best people to revenue-generating projects makes a lot of sense."

"Reallocating your best people to revenue-generating projects or projects that will help drive market-share gains when the upturn comes makes a lot of sense, especially if you are saving money in the meantime."

As one of the fastest-growing global services companies in the world, Cognizant will also work deals with companies that own captive processing centers or shared centers. Says Bhaumik: "If, in this downturn, it's clear that such a center is costing more than it's worth, we can take it over, pay the client some cash, and sign on to run it more efficiently as part of our global network. The net effect, again, is immediate relief from overheads, greater business efficiency, and a fixed transactional cost that can flex with business volume."

Retaining Staff

In recessionary times, layoffs are a sensitive issue for companies faced with cutting overheads. Cognizant is one of the few global services companies that commonly retains and re-badges internal staff. In a recent contract with a global pharmaceutical company, near 50 of the staff were retained to support clinical data management and handle the interface with the research organization.

"Outsourced to a global organization, the same work can be done around the clock by as many trained people as are needed. That's at least a 300% advantage in processing speed."

"More and more companies want a role for a retained organization," says Bhaumik. "We've re-badged hundreds of people over the past few years at onsite or near-shore delivery centers. We can often offer them a better career as part of a services organization than they might have had in an insurance company or healthcare company. In some cases, it's a step toward greater opportunity."

BPO Partner Selection Begins With Asking the Right Questions

Understanding the dual short-term/long-term benefits of a BPO program in tough times is one thing. Choosing the best vendor is another.

The key considerations are capabilities, track record, approach, price, value, and the quality of the client experience. Make sure consulting is part of the package not an expensive add-on, and that it is pragmatically suited to these recessionary times. It also pays to work with a outsourcer who can blend BPO with IT Infrastructure Management Services in a single coordinated approach. The fewer hand-offs the better. Then ask these questions:

- 1 How can you help my business grow?
- 2 How can I get business advantage by outsourcing this process to you?
- 3 What do you bring in terms of capabilities and technologies that are truly a competitive advantage to me, so I'm not just replicating what I have?
- 4 Are you just cost-focused or can you help me make money with services I haven't considered?
- 5 What is your track record in helping others innovate and deliver value beyond pure outsourcing arbitrage?
- 6 When there are issues, are you organized to resolve problems fast? What is your track record for doing that?
- 7 What can you offer me in terms of geographic expansion, innovative deal structuring, etc.
- 8 Can you take over my captive center, or buy it from me?
- 9 Are you willing to commit to a price that's locked in?
- 10 Since I'm outsourcing critical processes, will you be around in five to ten years?

The right answers will get you closer to the right choice.

About Cognizant

Cognizant (NASDAQ: CTSH) is a leading provider of information technology, consulting and business process outsourcing services. Cognizant's single-minded passion is to dedicate our global technology and innovation know-how, our industry expertise and worldwide resources to working together with clients to make their businesses stronger. With over 50 global delivery centers and 63,700 employees as of March 31, 2009, we combine a unique onsite/offshore delivery model infused by a distinct culture of customer satisfaction. A member of the NASDAQ-100 Index and S&P 500 Index, Cognizant is a Forbes Global 2000 company and a member of the Fortune 1000 and is ranked among the top information technology companies in BusinessWeek's Hot Growth and Top 50 Performers listings.



Cognizant | Business Process Outsourcing
Passion for building stronger businesses

World Headquarters

500 Frank W. Burr Blvd.
Teaneck, NJ 07666 USA
Phone: +1 201 801 0233
Fax: +1 201 801 0243
Toll Free: +1 888 937 3277
Email: inquiry@cognizant.com

European Headquarters

Haymarket House
28-29 Haymarket
London SW1Y 4SP UK
Phone: +44 (0) 20 7321 4888
Fax: +44 (0) 20 7321 4890
Email: infouk@cognizant.com

India Operations Headquarters

#5/535, Old Mahabalipuram Road
Okkiyam Pettai, Thoraipakkam
Chennai, 600 096 India
Phone: +91 (0) 44 4209 6000
Fax: +91 (0) 44 4209 6060
Email: inquiryindia@cognizant.com