
Offshore Business Process Outsourcing

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Abstract

This paper focuses on the relatively new growing industry of offshore business process outsourcing, which has provided developing countries with literate language and information technology skilled workforce with an excellent global business opportunity. The main advantages to business process outsourcing, cost versus quality and other reasons for choosing offshore outsourcer and the challenge of high industry attrition rates are briefly analysed here.

Key words

Business process outsourcing (BPO), offshore outsourcing, information and communication technologies (ICT), globalization, e-work

JEL Classification: E01, Q51

Introduction

The process of globalization and the influence of new technologies on globalization attract interest of many professionals and lead to research and prognosis in this area. While a hundred years ago the consumption of goods and services was still tightly connected to local production, during the last century the developments in transportation means, communication tools and growing globalization have totally changed the geographical relationships between demand and offer. Nowadays, it is quite usual to buy the products of daily use which were produced on the other side of the world and it is also considered efficient to buy certain kind of services from producer based in other part of world. The work can be relocated too, which all together brings us to e-work on a global scale and work outsourcing. The goal of this paper is to provide an overview of the current global business process outsourcing market.

Business process outsourcing basics

Business process outsourcing (BPO) is based on contracting of the operations and responsibilities for specific business functions or processes to a third-party service provider, replacing in-house services with labour from an outside firm.

We focus here on BPO that is contracted outside a company's country and often called offshore outsourcing. Another type of BPO is the one contracted to a company's

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neighbouring country and called nearshore outsourcing. With special attention paid to information technology industry, BPO is also categorized as an information technology enabled service or ITES.

The main categories of BPO are: 1) back office outsourcing, which includes internal business functions such as human resources, finance or accounting, and 2) front office outsourcing, which includes customer-related services such as contact center services (Wikimedia Foundation, 2011).

Main advantages of BPO

The main advantage of BPO is probably its influence on company flexibility. There are a few different ways how it works. Firstly, most services provided by BPO vendors are offered on a fee-for-service basis, which can help a company to transform fixed costs into variable costs and consequently to become more flexible. A variable cost structure helps a company to quickly respond to changes in required production/service capacity without necessity to invest in its assets (Willcocks, et al. 2004).

Secondly, BPO allows a company to focus on its core business and core competencies, without being burdened by the demands of its administration. Less staff is required and company specialists are released from performing non-core or administrative processes and can invest more time and energy in building the company's core business (Kakabadse, 2002).

Thirdly, BPO can increase the speed of some business processes and allow higher flexibility too.

Finally, even later in the life of a company when becoming efficient is necessary and risk of a growth slow down therefore arises, a company can maintain its growth goals while using BPO to ensure the required service levels. A company may be able to grow at a faster speed as it will be less limited by large capital expenditures for people or equipment that may take years to amortize, may become outdated, or in case of changes in company orientation may become useless (Fischer, 2001).

To sum the advantages up in other words – BPO is seen as a tool to improve performance and profitability, and to gain competitive advantage in the global marketplace. The profitability issues versus other reasons for choosing offshore outsourcing are the topic of the following chapter.

Cost versus quality

The first idea that usually comes to people's minds when thinking about reasons for choosing offshore BPO is the low cost of service. The wages in the same field are undoubtedly lower in Asia or Africa than in America and Europe (see Table 1).

Table 1 Call center employee cost

Country	Cost (USD/year)
USA	19
Australia	17
India	<7,500

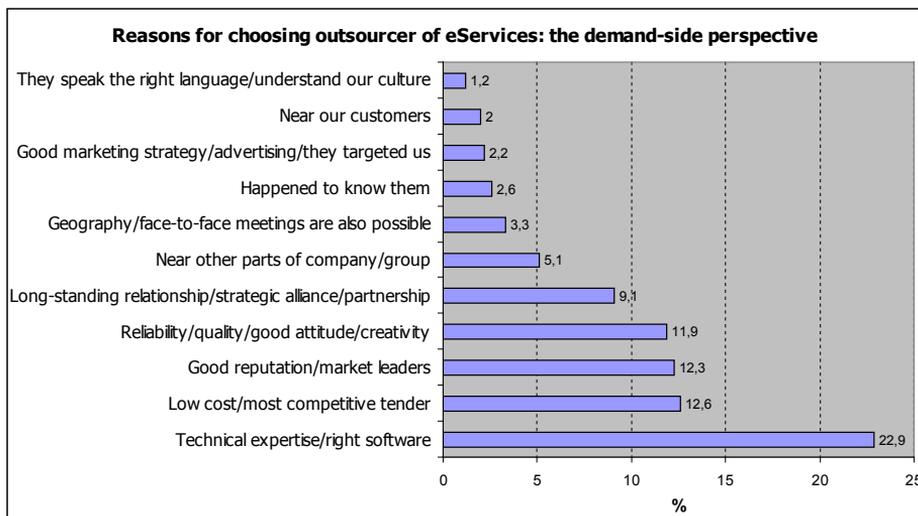
Source: PriceWaterHouseCoopers, 2005.

During 1995-2007 India became the number one in offshore business process outsourcing business with more than a 50 % share of this market and the demand for BPO services increasing at an annual growth rate of 25-50 %: 59 % in 2003, 45 % in 2004 and 43 % in 2005 - during this period (PriceWaterHouseCoopers, 2005).

Among many drivers of work being outsourced to India, the leading one was cost. According to US National Association of Software and Service Companies, American banking, financial services and insurance companies saved \$6 billion in the first four years of this century by outsourcing to India. This has resulted in quality and productivity gains of 15-20 % and in a customer satisfaction of almost 85 %. Similarly, the McKinsey Global Institute estimated its potential cost savings on factor costs up to 45-55 % and a 30-40 % savings on task and process level improvements in 2005 (Bandi & Srinivasan, 2005).

Though the low cost is undoubtedly the reason for choosing Asian, East European or African service outsourcer or location for remote work, it is by no means the only factor and may often take second place to other considerations including reliability, quality, specific rare skills, and the "right attitude" (see Chart 1.). If one of these factors is missing, a potential outsourcer may be rejected however low the price offered. It is probably one of the reasons why some country regions (e.g. Bangalore in India) still gain bigger importance in delivering certain service even though the wages are much over the countries average there.

Chart 1



Source: Huws & Flecker, 2004.

To mention some other important factors, among main facilitators of BPO industry in India are availability of skilled literate manpower, low cost of bandwidth and good telecom infrastructure, availability and applicability of net based tools, ability to standardize business applications, existence of a well established, relatively mature domestic IT sector, government policies (infrastructure, investment, taxes, training, creation of special zones), and IP legislation (Huws & Flecker, 2004).

BPO global market

The BPO global market has been growing steadily for some time and almost tripled in the 8 year period from 2000 to 2008 (see Table 2). The highest number of outsourcing companies comes from the USA – 59 % and from Europe – 27 % (see Table 3).

Table 2 Size of Global Outsourcing Market

Year	Size (USD Bn)
2000	119
2005	234
2008	310

Source: PriceWaterHouseCoopers, 2005.

Nearly 75 % of US and European multinational companies now use outsourcing or shared services to support their financial functions. 72 % of European multinational companies have outsourced financial functions over the past two years. Additionally, 71 % of European companies and 78 % US companies plan to use these services in the next 12–24 months. Overall, 29 % of US and European companies expect to increase their use of outsourcing of financial functions, with spending expected to be nearly 16 % higher than current levels (PriceWaterHouseCoopers, 2005).

Table 3 Global BPO Market by Geography in 2008

Country	Percentage (%)
USA	59
Europe	27
Asia-Pacific	9
Rest of the World	5

Source: PriceWaterHouseCoopers, 2005.

The choice of an offshoring destination is often made according to cultural concerns. Japanese companies are starting to outsource to China, where large numbers of Japanese speakers can be found — particularly in the city of Dalian, which was Japanese-occupied Chinese territory for decades. German companies tend to outsource to Poland and Romania, where proficiency in German is common. French companies outsource to North Africa for similar reasons. For Australian IT companies,

Indonesia is one of the major choices of offshoring destination. Near shore location, common time zone and adequate IT work force are the reasons of offshoring IT services to Indonesia. (Wikimedia Foundation, 2011)

The BPO market growth has helped many developing countries to realize that there are important niches in global market for BPO which can be successfully exploited by developing economies with a literate workforce and a modern telecommunications system. (Huws & Flecker, 2004). One of them is Philippines where BPO industry has grown 46 % annually since 2006. This boom is led by demand for offshore call centers. The BPO output for 2008 was US\$ 6.1B (vs. US\$ 4.5B in 2007), putting the Philippines as the 3rd largest BPO destination (15 %) after India (37 %) and Canada (27 %). The call center industry comprises 80 % of the outsourcing industry in the country (Philippine Board of Investment, 2010). Countries like Australia, China, Mexico, Indonesia, Vietnam, Sri Lanka, Thailand, South Africa, and Ireland are also expanding outsourcing operations and sometimes providing cheaper services than India.

As Asian Emergence project (Huws & Flecker, 2004) explains, the outsourcing started in many cases just as an experiment or short time work relocation caused by some temporary reason, and only gradually evolved to real offshore outsourcing. The BPO market generally develops according to the demand of highly developed countries with high workforce cost and shortage of skilled specialists on one hand and offer of developing countries with reasonable workforce cost, growing numbers of educated people and expanding technology on the other hand.

Attrition rate

One of the challenges BPO industry is facing is to find quality human resources given the current attrition rate in India of around 35-40 %. Recently it was about 35 % in non-voice and 45 % in voice call centers (see Table 4). However the numbers don't show that more than 60 % of those who leave a particular BPO job do not leave for a competitor, but leave the industry as a whole. Here lies the danger for this sector and the challenge for HR consultants.

At an attrition rate of 40 %, the cost of attrition in the industry is 1.5 times the annual salary. If the current attrition rate continues, the outsourcing industry is likely to face a shortage of professionals soon.

Some reasons for high attrition could be that the work at a call center is considered to be a mechanical dull work, just a stop before one finds more attractive job because of restricted career options or growth opportunities for the youngsters, there is a stressful work schedule, particularly night shifts, which may create both physical and mental disorders, talent is overlooked there and the industry has concentrated on hiring young, dynamic people who are in fact looking for growth, career, opportunities and therefore do not stay long.

Table 4 Attrition rates across industries

Sector	0-3 years	4-7 years	8-12 years	13+ years
Pharma & Chemicals	25.00%	10.00%	5.00%	2.00%
Manufacturing	8.58%	2.46%	2.46%	3.00%
Financial Services	20.00%	20.00%	20.00%	20.00%
Hospitality	35.00%	25.00%	20.00%	7.50%
Ad & Media	40.00%	35.00%	20.00%	15.00%
BPO	40.00%	30.00%	20.00%	10.00%
Automobile	7.00%	3.00%	2.00%	2.00%
Auto Component	12.00%	15.00%	20.00%	12.00%
Banking	10.00%	5.00%	2.50%	2.50%
Infrastructure	16.00%	11.00%	7.00%	11.00%
IT & Telecom	32.00%	25.00%	10.00%	5.00%

Source: BPOIndia.org, 2008.

To fix this problem BPO companies try to hire mature talent of 35 years in age and more, create conditions that would increase the attractiveness of the job or offer benefits that are tailor-made for the group of employees like education opportunities or accommodation (BPOIndia.org, 2008).

Conclusion

The growing share of relocated work worldwide is currently an important issue to be analysed and taken in consideration in global business. Business process outsourcing as one of the ways work can be relocated or outsourced to foreign provider provides many companies with an option to increase their cost efficiency and flexibility. At the same time it provides countries with an abundance of literate skilled manpower and required level of technology to benefit from attracting foreign business partner. This seems mutually beneficial and we can therefore expect the BPO global market to continue to grow and develop. Though there are some risks and threats to outsourcing business functions, these are likely to be resolved and the cooperation optimized.

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