



## The Reality of Global In House Centres (GICs) - Formerly Offshore Captives

### Introduction:

There is an emerging trend where organisations are setting up Global In House Centres (GICs) to meet their needs for higher quality IT, BPO, Engineering and R&D facilities at a much lower cost. Whilst this is not a new delivery model (Offshore Captives were at the forefront of the outsourcing industry), there is a growing realisation that offshore outsourcing is not delivering the economic value that it originally offered during the growth years of the 90's and 00's. This is forcing organisations to re-evaluate the benefits of setting up and owning their own offshore capability and make it a key part of their global delivery model.

It should be noted that the original offshore model was pioneered by global corporations such as GE, British Airways and Texas Instruments who established their operations in India as early as 1986 – 1990.

### Outsource or Insource:

The emergence and success of offshore outsourcing was primarily driven by the benefits of labour arbitrage with a simple lift and shift of the clients' services using their tools and processes but employing low cost staff to deliver in a client dedicated environment. The amount of the employment differential was attractive enough for clients to be satisfied with the savings generated and also for the outsource suppliers to enjoy healthy margins.

Since the global recession many companies are again evaluating the cost of their IT and BPO services and there is a growing realisation that the Outsourcing Model may not be the key to cost efficiency that it once was. Rather than re-tender their contracts and try to obtain a better deal, many forward thinking organisations are carrying out bottom-up benchmarks and reaching the conclusion that it would be cheaper and more effective to 'do it for themselves' with the added advantage of regaining control of their IT and BPO capabilities. Companies including AstraZeneca, Daimler, Equiniti and Morgan Stanley have already declared their intent to build their own captives with reported expected savings of 40% plus, coupled with improved service levels, increased flexibility and better control.

### The Analysts' View:

The analysts that have commented on GICs have been very positive with AT Kearney describing them as 'The Business Model of Choice' and McKinsey expecting a further \$50Bn worth of value to be delivered over the next 5 years.

Everest puts typical savings in the order of 40% - 70% and believes that, provided you choose the correct location to base your GIC, the competitive advantage will be retained for the foreseeable future.

### India as a Location for GICs:

GIC activity is now predicted to be a major growth area in India, which is already home to 825 GICs, over 50% of the world population, and accounting for 21% of the Indian IT & BPO sector exports. NASSCOM is focussed on enhancing the presence of GICs in India with Bangalore expected to lead the charge as the 'GIC Capital of the World' with an additional 30 GICs being established in the city over the next three years bringing the total



number in India to around 900 employing circa 600,000 staff. NASSCOM is the catalysing agency responsible for the growth of the IT segment in India and has created a separate GIC Council holding a seat on its Executive Board that is intent upon building sustainable value for global enterprises wishing to set up GICs in India.

India has become the natural choice for many companies as it now has a matured, scalable and diverse workforce and has developed a management capability to deliver the class of service demanded by the Global Corporations. The original 20 year old IT professionals are now in their 40s and have matured as the industry has grown, progressing from technical engineers to senior delivery managers and ultimately facility directors.

Whilst wage inflation is often cited as a reason not to use India, a closer examination recently published by Everest, shows the cost of employment in India is still 80% below the UK on a like for like basis and is likely to remain so for circa 20 years. However, the gross margins enjoyed by the outsourcing companies of 50% plus has contributed to the perceived closing of the wage gap. These outsourcing companies have protected their profits by including contract clauses to pass on wage inflation and the client sees their cost benefits eroding with wage inflation given as the main cause. Simply by adopting a GIC model it is clear to see why a 40% cost saving can be easily achieved.

As offshore outsourcing was a major success for India, the GIC can be seen as the next natural wave, complementing the outsourcing industry. Setting up a GIC, recruiting staff and transitioning work can all be achieved in less than 12 months and the ROI case will be compelling. The transition from an Indian Outsource service to an Indian in house GIC is a low risk activity if you take experienced advice, particularly if the service is still running as a ring fenced operation using the client's own tools and processes

### Setting up a GIC in India:

To many organisations setting up a new facility in a foreign country could seem very complex, full of risk and potentially expensive as they may have no experience or internal capability to call upon; and indeed this can be the case without experienced help. However, all these concerns can be systematically addressed and de-risked by working through them with seasoned professionals who have trodden this path many times before. Experienced guidance can significantly shorten the timescales required to set up a GIC resulting in vastly reduced costs and a better quality facility.

In the early days of offshore services, it was the global companies who established their captives as they had experience of establishing research centres, manufacturing plants or regional head offices across the globe and would have in house functions to take care of it. The emerging outsourcing companies were able to offer established offshore capabilities and for many it was perceived to be a low risk, easy to establish way of exploiting offshore resources, although not recognised at the time, coming at a significant premium.

Finding office space in a tax efficient zone in India is relatively straight forward once you establish the right contacts as the choice is limited to a few major cities and they are all still continuing to construct new complexes. Once the office has been acquired fitting-out can be achieved at a relatively low cost much quicker than in the UK. Normally a 500-1,000 seat office can take between 3-6 months to fully complete.



Hiring Staff is another challenge that can deter a company that has no experience of India. However, one of the outcomes of the rapid growth of IT services in India has been the maturity of Indian HR functions and their ability to hire large numbers of the appropriate staff rapidly. In the UK it is not possible to find and hire on this scale and the task is further complicated by TUPE. The large population of educated and experienced staff, together with reduced government restrictions, ensure that these issues do not act as a barrier to building a GIC in India.

Staff attrition can be an issue if not handled properly, but this can be managed and even exploited. An approach to staff management has to be established from the outset and a combination of experienced staff supported by a graduate recruitment scheme lessens the rate of attrition. Graduates will be more inclined to stay if they are given the opportunity to learn and progress and this can compensate for the potentially higher attrition rates in the more experienced technical staff. On the positive side, staff attrition can be used in the GIC's favour. Once the service is established it will need to improve by increasing productivity through tools and automation, resulting in a requirement for fewer staff. Attrition managed correctly will result in early benefit realisation through these improvements, unlike the UK where shedding staff is a costly and lengthy process.

Transition from incumbent suppliers needs careful planning and execution with a well practised methodology. An assessment of the current delivery will determine the difficulty and the length of transition and it is crucial that this is undertaken at the business case stage and further followed up in the Due Diligence process. This is another area where access to experienced transition managers will prove critical to the project's success.

### **Are We Big Enough to Set Up a Captive?**

The question that is often asked is that it may be OK for the big boys, but is it OK for me and is my company too small to adopt this approach?

Circumstances will vary from case to case, but our general rule is that the critical mass to achieve a successful offshore presence lies in the range of 75 – 100 staff. Once IT and BPO have been considered most companies will find themselves potentially satisfying these requirements. The smallest successful installation that we know about contained 30 staff but operated in a very specialist area with a requirement for specific niche skills.

### **Why have some Companies Sold Off their Captives?**

Companies selling off their Indian Captives were largely attracted by the offer of an immediate and substantial cash injection from the Outsourcing companies to purchase their captives. In many cases this 'windfall' was used to prop up ailing balance sheets or was reinvested elsewhere. At the start of the recession it was clear to understand why corporations would take this approach. This was a great short term gain, but like most transactions of this nature they came with a cost and that was usually an extended lock in to the supplier, at pre-determined rates which rapidly become less attractive as the buyer recovered its investment and lost margins.



### The Facts and Figures:

Provided that a company takes advantage of expert advice, GICs can be set up relatively quickly in a low risk manner with typical timescales and savings for a 100 seat installation of:

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|----------------------|---------------|--------------------|-----------|
| ➤ Costs to Set-Up    | £2.0m - £2.5m | ➤ SLA Improvements | Circa 25% |
| ➤ Annual Run Savings | £2.5m - £5.0m | ➤ Project Duration | Sub 12m   |

So it can be seen that it is possible to invest in a project that will improve service levels, deliver savings of 40% - 70% and achieve a payback of less than 12 months. No wonder AT Kearney describe it as 'The Business Model of Choice'.

### Why CIO Plus:

CIO Plus provides independent impartial advice and our team has delivered over 40 successful projects based in India. We have a proven methodology and can provide full life-cycle coverage in India and the home country including:

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|--|---------------------------------------|
| ➤ Strategy, Business Case & Planning         | ➤ Recruit, Train & Knowledge Transfer |
| ➤ Site Location, Negotiation, Design & Build | ➤ Full Service Set-Up                 |
| ➤ Existing Contract Exit                     | ➤ Stabilisation & Optimisation        |

Using our experienced staff will ensure that your project is successfully delivered and value for money is maximised. If you are interested in discovering if this is the right direction for you or you require further information, please get in contact.