

Better, Cheaper, Faster. Now Repeat.

The Transformational Offshore Imperative in the Age of Payment Electronification

A Bank Offshoring Case History by Bob Olson

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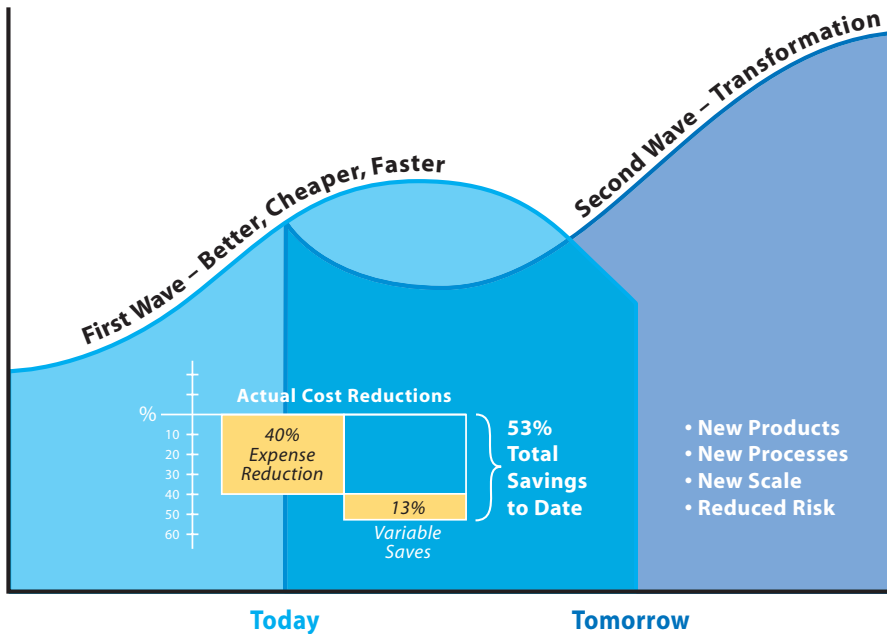
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The World Is Flat, Thomas Friedman's lively exploration of the "flattening" of global barriers, puts to rest forever any lingering view of globalized work forces as a purely expedient search for the cheapest labor. The best of today's offshorers, well aware that pure labor arbitrage is hard to sustain, are laser-focused on quality and transformation.

For the past year, our company has been successfully offshoring check processing back office functions for a large US-based financial institution that prefers to remain anonymous for now.

Transformation

The Offshoring Imperative in the Age of Payment Electronification



Our client's case history to date, detailed here, is powerful testimony to the first-wave achievements of offshoring: advances in telecom and digital imaging bringing global resources to bear on what has long been a costly, geography-bound operation. That is the first imperative in the business process outsourcing (BPO) business: tapping pools of qualified but less costly resources.

But technology advances are imitable, and labor arbitrage diminishes with competition, education, and other inevitable trends. It is the *next* wave of transformation, and the next, that will separate the value-adding offshorers from those with just one trick — low-wage workers — to offer.

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To satisfy the second imperative, financial institutions and their offshorers need to constantly ratchet up their performance by relying on deep domain expertise and steady innovation that meets the changing demands of financial institution customers. Sometimes they will be rewarded with major advances, but more often they must extract incremental advantage from small but steady improvements in process and performance.

This article describes how financial institutions and Carretek are producing both waves.

The Carretek Case History – The First-Wave

The functions we offshored from our client are performed at our facilities in Mumbai and Pune, India. These functions represent approximately 100 FTE saves for our client. We started with Proof of Deposit, then we added Exceptions, and we are preparing to add Adjustments. In the coming months, we expect to add other deposit operations functions for another 25-35 FTE saves. For other financial institutions, we are currently performing due diligence to offshore their lockbox operations.

Our clients are beginning to realize substantial gains:

Better

For Proof of Deposit, where our case history represents the longest experience, we quickly met our client's quality goals. This success was founded on three important foundations.

- The first is deep domain expertise. Payments are an exacting business, requiring extensive knowledge and freighted with regulatory, customer, and security issues. Between our client's experts and our own in banking, payments and back office processing, we applied a level of expertise unavailable to more generalized out-sourcers, whose lack of domain expertise can lead to oversimplification of offshoring processes and costly mistakes.
- The second driver of quality was preparation of our offshore employees. The extensive training they had already undergone as part of our operation was heavily supplemented by our client's training them on their specific processes. Before any of our client's work was performed overseas, our employees were rigorously tested on the client's detailed policies and procedures.
- The third driver of quality is our ongoing performance tracking. We monitor the quality of our performance on many key factors, and we routinely review that performance to find any and all opportunities for continual improvement.

Cheaper

We quickly exceeded our cost goals for POD. We had promised our client a 40% direct expense reduction. We delivered 53%, even after the initial start-up and transition costs; the variable expense saves linked to headcount amounted to an additional 13% cost reduction.

We have accomplished these gains while protecting our client's data security and the privacy of the client's customer information, an increasingly important factor and one that requires extensive domain expertise.



As banks in general watch a steady decrease in check-based revenue due to payment electrification, cost reductions of this magnitude that come with no reduction in quality, are vital to a bank's payments business.

Faster

In the world of payments, time matters. Time IS money. In these early stages, we do continue to maintain, at our own cost, some redundant resources at our facilities in India to cover almost any contingency that could impact rapid turnaround. This redundancy offers a pay-off to future clients: already-trained staff for their volumes. However, we are well positioned to meet SLAs and exceed our client's expectations for rapid turnaround.

Needless to say, we have accomplished these gains while protecting our client's data security and the privacy of the client's customer information, an increasingly important factor and one that requires extensive domain expertise.

Our client's satisfaction to date is expressed in a number of ways, perhaps most convincingly by their consideration of additional functions for us to offshore. As the client's Chief Information Officer affirmed, "Our shareholders are clear: They expect our bank to be a market leader in using technology and processes, not only for low-cost provider purposes but also for leadership in innovation and customer service. Carretek is a key player in helping us earn that leadership position."

All well and good. For many offshorers, this would be almost time to declare mission accomplished and move on to the next client in search of scale to shore up the flattening advantage curve.

But in the financial institutions world, that would be shortsighted, given the changing nature of the payments business. Banks' payment revenues are under pressure as check volumes decrease. Banks find themselves competing against less-regulated technology providers who cherry pick the payments electrification evolution for product advantage, leaving banks holding the infrastructure costs. Banks must aggressively seek changes in all aspects of their business that can deliver cost, revenue, and/or process improvements.

The CIO of a fairly large U.S. bank who expects to offshore his back office functions, echoed the quote that opened this article. He told us, "Even if I deliver a 50% cost reduction this year, I don't foresee a year when my goals include anything less than a 3-5% improvement in productivity. My management may not care how I get there — process, products, prices — whatever. But they know that labor costs are not a bottomless source. Bring me new ideas, big ideas, small ideas — or old ideas for a new environment. That's what offshoring needs to do for me."

Transformation — The Second-Wave

What are some of those ideas? At Carretek, in our formative period, we tended to spend half of our time, resources, and energy making good on the first wave. Now, as we see our concept, process, and training benefiting our client in function after function, we are increasingly dedicating ourselves to the second wave, proactively seeking out innovations that will deliver the next set of benefits to our customers.

In our formative period, we tended to spend half of our time, resources, and energy making good on the first wave. Now we are increasingly dedicating ourselves to the second wave, proactively seeking out innovations that will deliver the next set of benefits to our customers.

Second-wave transformation opportunities appear to revolve around four categories:

1. **New Product Opportunity for Banks** Every new product entails a new set of back office functions, and every back office function offers, at least implicitly, a cost-reduction opportunity via offshoring.

One of the most attractive “new” products to emerge in the bank payments world is distributed capture — capturing images of checks at locations remote from the banks operations center, including customer sites. Almost overnight, as this product takes hold, banks will be confronted with massive amounts of payment data to be aggregated, managed, distributed, reported, archived, and retrieved. We expect many banks to resist the traditional urge to set up the supporting back office functions “in house” and instead design the product with certain functions offshored from the start.

2. **New Processes** In India, we can process 24-hours a day, using highly skilled resources around the clock. That advantage has scarcely been tapped so far, with most banks still processing in batch mode and foregoing the ability to deliver same-day turnaround on customer issues where an hour here or there can make the difference in customer retention or transaction value.
3. **New Scale** For years, banks have been forced to ratchet up their “worth processing” threshold — the dollar size of transactions worth addressing in their back office. Ten years ago, a \$50 transaction was worth working. Today, many banks simply write off anything under \$150, and that number would probably keep climbing, given current operations. However, offshoring upends the numbers. Maybe the right cut-off is \$5. If your operators cost you one-third as much, and if they can solve it that night, the right threshold — the level at which solving it is more cost-effective than writing it off — is sure to be lower. We are applying our domain expertise to significant questions like these.
4. **Risk** Ask almost any banker for his or her list of five top concerns, and “payments risk” is bound to be among them. As risk and fraud concerns erupt on all fronts, and the cost of risk-related compliance reaches crippling proportions, few banks wish to hire all the staff it will take to “do it all.” Those risk-related decisions, data entry, and clerical functions that can be digitized are likely to join their check operations functions overseas. That is one of the reasons we have made security and customer privacy a priority concern from the start.

Offshoring as a game-changer is still in its infancy — still proving over and over, function by function, the value of accessing global resources for their lower labor costs. But building a business case purely on first-wave costs is an almost certain road to disappointment in future years. Transformational offshorers should be able to help their clients envision, from the start of their relationship, how they should expect to see substantial improvement year after year. You never get a break from it...

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