

An end to the Indian centre adventure

More and more stressed companies are selling their captive set-ups to cashed-up locals, writes **Paul Smith**.

When Western businesses first stumbled upon the idea of developing their own offshore centres, as opposed to outsourcing to India's rapidly growing technology giants, many thought they had solved the conundrum of cost arbitrage versus loss of control.

With financial markets crashing, the tide has turned, however, and the number of big name global institutions selling their captive centres to those same Indian firms has led many to write obituaries for the strategy.

Citigroup, Barclays, Philips, GE, Prudential, Ericsson and Aviva are among those that have sold their Indian centres to outsourcers, and others are seeking to join the list. Insurance firm Axa is looking to reduce its Indian footprint, AIG's Indian software unit is up for grabs, and UBS has its business process and knowledge process outsourcing centres in Hyderabad and Poland on the market.

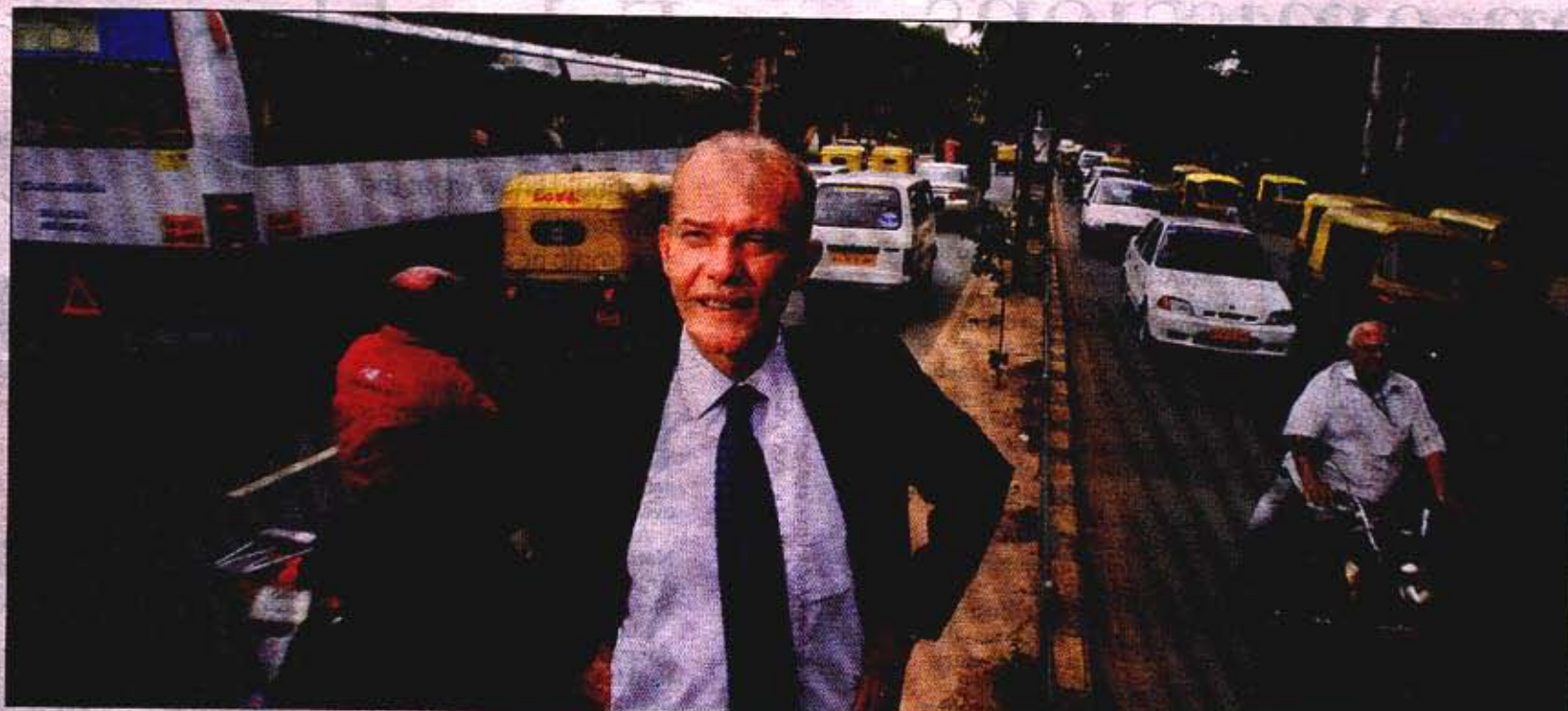
With Indian vendors willing buyers, it is looking to many analysts as if the benefits for those on both sides of a deal are helping to bring the subcontinental adventures of many corporations to an end.

The executive in charge of analysing potential captive centre acquisitions at Indian outsourcer Wipro, chief strategy and M&A officer K.R. Lakshminarayana, says there is a clear trend towards companies looking to sell their Indian centres. With more than \$US1 billion (\$1.2 billion) in the bank, he says Wipro and its cashed-up Indian peers have the whip hand and are keen to buy companies that will then guarantee them long-term outsourcing deals to continue to operate the centre.

"Companies want to sell, but they also want to guarantee that they have a continued reliable service from the centre, so it is a huge advantage for companies like us, as long as we have the appetite and resources for it," Lakshminarayana says.

"Technology firms using captives to do core work and core R&D will continue to grow their centres. But there are others that moved to India solely with the purpose of leveraging the cost arbitrage and they are now seeing that, in the current climate, they can achieve that without the headache of owning the centre."

Asia-Pacific president of advisory firm TPI, Arno Franz, says that



Fred Bertram, now with ING Australia, photographed in Bangalore, India, a few years ago... 'rising salaries really won't be an issue in captive centres'.

Photo: NAMAS BHOJANI

depending on the individual circumstances, it can be cheaper to run a captive centre than to outsource. However, he says the financial climate means financial services firms are looking to free up capital and cash in on their centres, while Indian IT firms are looking to increase their capabilities.

The quickest way for an outsourcing company to develop new marketable skills is to buy them, so captive centres performing specialised business processes become prime targets.

Director of Sydney-based independent consultancy Mindfields, Mohit Sharma, says the Indian companies have evolved in the last five years to become gurus of driving out cost-centre efficiencies and leveraging economies of scale. He says the race is on among the Indian IT specialists to diversify their offerings and attract new customers to outsource commoditised business processes.

"The acquisition of Citigroup BPO in 2008 and Financial Network Solutions in Australia has transformed Tata Consultancy Services into essentially being a banking institution without a banking licence," Sharma says.

"These acquisitions have made it possible for TCS to offer end-to-end processes to the banking industry which would not have been possible through organic growth."

The Citigroup acquisition provided an example of how a deal

Selling up

Recent and ongoing captive centre deals

Captive owner	Acquired by	Employees	Deal value (\$USm)	Contract after acquisition
Philips	Infosys	1,500	28	\$US200m contract over 5yrs
Citigroup BPO	Tata Consultancy Services	12,000	505	\$US2.5bn business over 9.5yrs
Citigroup IT	Wipro	1,650	127	\$US500m business over 6yrs
Citigroup Warsaw	Bravura	n/a	31.5	3yr contract
AVIVA	WNS	5,000	228	\$US1bn 8.4yr contract
ON THE MARKET				
AIG	Patni, Polaris, Mindtree and Mphasis in the race	1,000	30 approx	n/a
UBS	TCS, Infosys, Genpact and Wipro in the race	1,500	200 approx	n/a

SOURCE: MINDFIELDS

can be made more manageable for an acquirer through the guarantee of long-term business. Tata's agreement bundled up a 9½-year agreement to provide the back office services back to Citigroup, which will be worth \$2.5 billion over the life of the contract.

Bucking this overarching trend, ANZ Banking Group says that, despite persistent rumours to the contrary, its Bangalore captive centre, with 3000 staff, is not on the market. The bank has owned the centre since 1989 when Index Computing was established to run technology for ANZ Grindlays in India.

The bank's group managing director, operations, technology and shared services, David Cartwright, says he prefers to run a captive centre rather than outsource because of the

better risk profile, greater flexibility and control. He says ANZ approaches the topic with an innate sense of conservatism, and the idea that it will be better able to respond to changing circumstances if it retains total control. "We have had the Bangalore

Indian players see it as an opportunity to buy an income stream.

DAVID CARTWRIGHT, ANZ

captive for over 20 years and it is part of our DNA. It has become more important over the last few years because the capability that you can acquire in Bangalore has increased," Cartwright says.

"Some firms are selling because they need to raise capital and the Indian players see the current crisis as an opportunity to buy a long-term income stream. We don't have the sort of problems other institutions are facing so we don't have to think about those issues."

However, rumours persist that ANZ is looking to sell its Bangalore facility. According to the Australia and New Zealand head of Indian firm Satyam, Venki Prathivadi, the array of companies seeking to sell off their Indian centres is indicative of an initial rush to get into India, without long-term strategic planning. He says some companies invested in India because they saw rivals doing so and had only flimsy business cases for following suit. "It almost seemed like a knee-jerk

being successful in providing services and thinking they could just do it themselves," Prathivadi says.

He says some companies were ill-prepared for cost blow-outs and the reduced benefits due to the significant appreciation of the Indian rupee against the US dollar and other currencies.

The rising cost of Indian labour has been blamed by some for problems faced by captive centre operators, but Fred Bertram, who ran ANZ's Bangalore operation for three years before becoming chief operating officer at ING Australia last year, says this is a furphy. While the growth in the Indian IT sector has seen a rise in wages, Bertram says Australian businesses can still save a premium in staff costs by sourcing talent there.

"Rising salaries really won't be an issue in captive centres; people who say it will be confusing the CPI [consumer price index] increase with wages," Bertram says.

"The differential for the bulk of an Indian workforce is so significant that the benefits don't dissipate. While some of the more senior people are paid significantly higher wages, the bulk of an Indian workforce has a substantial labour arbitrage, which is not going to be eroded by the increases for the foreseeable future."

Having been back from Bangalore for 18 months, Bertram says he doesn't feel like the captive centre model has run its course, rather that the global economic climate has caught up with some financial institutions and precipitated a strategy rethink.

He says as banks have moved their attentions to better positioning themselves within their home markets during the downturn, Indian IT vendors have simply taken the opportunity to move in and acquire.

"It really depends on where an individual company sits and what it sees as core to its business — you see other companies that have outsourced are now insourcing so I believe it is a fluid situation," Bertram says.

"Those looking to acquire will tell you it is a definite trend towards selling, but in my time out there, there were always approaches being made by Indian companies looking to expand their operations by acquiring a captive