DRIVERS AND CONSTRAINTS FOR BUSINESS PROCESS OUTSOURCING IN SOUTH AFRICAN CORPORATE AND INVESTMENT BANKING OPERATIONS

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A research report submitted to the Faculty of Commerce, Law and Management, University of the Witswatersrand, in partial fulfilment of the requirements for the degree of Master of Business Administration

Johannesburg
February 2013

ABSTRACT

The research sought to identify and analyse the business drivers and constraints that lead South African corporate and investment banks to either outsource operations processing to external service providers, or to conduct such operations processing internally.

The research took the form of a simple, interpretive study and followed a qualitative research approach, using in-depth, semi-structured interviews with executive management representatives in the wholesale banking operations industry in South Africa, including banks, outsourcing service providers and industry bodies.

The findings from the research identified the drivers for outsourcing as cost reduction, revenue growth, increased operating efficiency, organisational effectiveness and human resource development, improved strategic control, process control and operational risk management, external environmental factors and enhanced competitiveness. The constraints identified through the research were diminished strategic control, lessened ability to contend with competitive threats, cost escalations, insufficient management capability, human resources interests, diminished process control, increased operational risk, reduced organisational effectiveness, operating efficiency and external environment factors.

The drivers for outsourcing stem from the superior capability maturity levels of outsourcing service providers, the opportunity to free-up incumbent senior management and leadership to focus on core responsibility areas, the certainty and control inherent in formal partnerships, as well as the opportunity to leverage the capital resources of outsourcing vendors. Conversely, the constraints for outsourcing stem from inability to implement processing changes, operating model complexity, misaligned management cultures, lingering concerns about reputational risk, as well as lagging capability maturity levels in specialist processing areas.

DECLARATION

I, Sarel Jacobus van der Westhuizen, declare that this project report is my own, unaided work. It is submitted in partial fulfilment of the requirements for the degree of Master of Business Administration at the University of the Witwatersrand, Johannesburg. It has not been submitted before for any degree or examination in this or any other university.

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_______ day of _________________ _______

DEDICATION

Dedicated to my wife Suzette and my daughter Lara.

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1 INTRODUCTION

1.1 Purpose of the study

The purpose of this research is to analyse the drivers and constraints for business process outsourcing in the South African corporate and investment banking operations.

1.2 Context of the study

In their on-going quest to maximise shareholder wealth, executives must seek the optimal functional and global configuration of the activities of their organisations. They need to continually question which activities in the organisational value chain are best performed internally, and which activities could be performed more effectively by external service providers. Concurrently, they need to determine which of these activities could be better performed abroad (Contractor, Kumar, Kundu and Pedersen, 2009). Gospel and Sako (2010) distinguish between outsourcing, essentially a decision to either “build or buy”, and off-shoring, a decision about the best location for production of goods and services.

The traditional view is business strategies must accentuate the core competencies of organisations that add the most value in the value chain. Accordingly, it is argued those functions that add little value and can’t be performed cost effectively, should be performed outside the organisation - thereby making it possible for organisations to improve their business focus and to reap cost and quality benefits on the back of the outsourcers’ specialist resources, processes and infrastructure (Pearce and Robinson, 2000). However, a trend is emerging where the responsibility for portions of the value chain, traditionally deemed to be more strategic or core, are being allocated to external service providers (Contractor et al., 2009).

A further trend is that these constructs, which have been characteristic of the manufacturing industry, are increasingly being extended to service industries (Hill, 2011). Outsourcing is prevalent in the global banking industry and some stakeholders believe that increased regulation following from the global financial crisis of 2008, will lead to more outsourcing of processes such as treasury, cash management and custody services (Goolsby, 2011).

Although there are numerous factors within the South African economy in general, and within the corporate and investment banking industry in particular, which may be conducive to the proliferation of outsourcing and off-shoring of operations services, the industry is comparatively small and trails other emerging markets in terms of scale and maturity (Karthik and Rajpal, 2010).

It is in this context that the drivers and constraints for business process outsourcing as a management strategy in the wholesale banking operations industry was researched.

1.3 Problem statement

1.3.1 *Main problem*

To analyse business process outsourcing in the South African corporate and investment banking operations industry.

1.3.2 *Sub-problems*

- To identify and analyse the business drivers that lead corporate and investment banks to consider outsourcing operations processing, to external service providers.
- To identify and analyse the business constraints and risks that lead South African corporate and investment banks to prefer conducting operations processing internally.

1.4 Significance of the study

The 2008/9 recession resulted in reduced volumes and margins in the banking industry globally. Business Day (Kamhunga, 2011) recently reported on a survey conducted by tax and advisory services firm PWC in March 2011: the survey found that lower revenues have resulted in South African banks, as they strive to bring cost-to-income ratios back to pre-2009 levels, treating cost control and efficiency as top priorities.

Research conducted by McKinsey & Company (Bremner and Simone, 2006) found that the high margins banks for many years enjoyed allowed them to operate in product-aligned silos. Whilst it permitted customised support services, it resulted in the formation of duplicated processing and support functions. Their recommendation from the research was that banks should fundamentally reconfigure their operations by creating shared services, utilising lower cost locations and outsourcing selected functions. They argued that such initiatives could bring about cost savings of 10% to 20%, improved service, increased innovation and could generate new revenues.

But while pundits of business process outsourcing suggest it could be used as an effective management strategy; concerns about loss of control, confidentiality and expertise cast a shadow over the proposed benefits (Contractor et al., 2009).

This study endeavours to fill a gap in the knowledge of drivers and constraints of outsourcing corporate and investment banking operations to business process outsourcing service providers. The research outcomes will presumably assist executives within the South African corporate and investment banking operations industry to make more informed decisions about, and minimise risks associated with, outsourcing as a management strategy.

1.5 Delimitations of the study

Study areas to be included:

- The study will focus on business process outsourcing of operations functions and activities, within corporate and investment banking.
- The focus will be on operations services, i.e. those functions associated with administration of client and transaction records, payment or receipt of funds or financial instruments, as well as related validation, accounting, reconciliation and service fulfilment processes.
- The study will cover the distinct, but interrelated constructs of business process outsourcing and off-shoring.
- The study will focus on the provision of business process outsourcing services within South Africa. Services offered by South African service providers would be relevant to global corporate and investment banks (with customers in foreign countries), but the study will only engage with stakeholders in corporate and investment banking with business interests in South Africa.

Study areas to be excluded:

- Whilst formation of shared services offerings often coincide with or precede outsourcing or off-shoring strategies, it will not be expressly covered in the study.
- Although the boundary between retail and corporate and investment banking operations is arbitrary in certain respects, this study will exclude retail banking, which typically entails the lower value, higher volume banking services offered to individuals and small businesses.
- The study will exclude various group enabling functions such as risk management, facilities management, information technology (IT), finance and human resources processing, which are sometimes associated with operations.

1.6 Definition of terms

Business process outsourcing (BPO):

> The long-term contracting of an organisation’s non-core business processing to an external service provider, which may be based in

the same or an offshore location, using defined and measurable performance metrics, such as productivity, customer satisfaction and costs. These are often IT intensive business processes, but are not IT processes per se (Halvey and Melby, 2007; Kshetri and Dholakia, 2011). Click and Duening (2005) define it as a socio-technical phenomenon, which impact on technical and social systems in organisations.

Capability:

Capabilities are descriptive of essential areas of work an organisation can deliver at a defined standard, based on combinations of people, systems and processes, within a defined location (The-Open-Group, 2011).

Corporate and investment banking:

Corporate and investment banking refers to the relatively lower volume, higher value banking services offered to customers within the larger corporate and financial institutions market segments.

It includes banking services such as underwriting and facilitating investment deals, assisting in mergers and acquisitions, brokering, merchant banking activities, trading of foreign exchange and financial instruments in global financial markets and wholesale transactional services (Loader, 2006).

Corporate and investment banking operations:

Operations services pertaining to functions and activities to process payment or receipt of funds or financial instruments, as well as related validation, accounting and reconciliation processes (Loader, 2006).

Off-shoring:

The business practice of sourcing goods and services from various geographical locations, so as to reap benefits from national differences in the cost and quality of factors of production. Goods and services might be sourced from an organisation's foreign subsidiary or an external foreign service provider (Contractor et al., 2009; Gospel and Sako, 2010; Hill, 2011).

Outsourcing:

The fragmentation of the production chain into discrete activities, which are allocated to distinct firms, who might be located in the same or different countries (Contractor et al., 2009; Gospel and Sako, 2010; Hill, 2011). The value proposition of outsourcing stems from Adam Smith's tenet of the division of labour, which proposes that increased functional specialisation leads to increased productivity and reduced costs (Chase, Jacobs and Aquilano, 2006).

Retail banking:

Retail banking typically refers to services offered to individual customers through local bank branches and related electronic platforms. Services typically include transactional and savings accounts, credit cards, personal loans and mortgages (Farlex Financial Dictionary, 2009).

Shared services:

The concentration of company resources responsible for performing similar functions and activities that are spread across an organisation, in order to serve multiple internal partners at lower cost and with higher service levels (Schulman, Harmer, Dunleavy and Lusk, 1999).

Strategic sourcing:

The organisational process that aims to continuously review and improve the procurement activities of an organisation. Often seen to form part of supply chain management, strategic sourcing covers identification and on-going management of suppliers (build or buy), with the emphasis on achieving continuity of supply (Pycraft, Singh, Phihlela, Slack, Chambers, Harland et al., 2000; Bakker, 2008).

1.7 Assumptions

- Representatives of corporate and investment banks, consultants, industry bodies and outsourcing service providers was willing and entitled to share their views of management strategies related to cost containment, operational efficiency and sources of revenue.
- Research participants may have been concerned about the research outcomes being publicly available. However, permitting the banks to also benefit from it, should have allayed such concerns.
- It was possible to draw parallels from literature about research conducted in other industries and geographies. Whilst different industries and geographies include very context specific content, it was expected the broader principles were relevant to this research.
- It was possible to obtain input from a sufficient number of respondents to gain adequate data.

2 LITERATURE REVIEW

2.1 Introduction

The literature review starts off by defining BPO as a management strategy for maximising business returns; it then assesses recent trends associated with the practice. It proceeds to explore factors in the international business environment that enable the proliferation thereof, and provides an overview of the prevalence of BPO within the wholesale banking operations industry. The literature review concludes with an assessment of the drivers and constraints that influence the decisions of business leaders in pursuing BPO as a management strategy.

2.2 An overview of outsourcing

2.2.1 *Outsourcing as a management strategy*

Executive leaders, in their on-going quest to maximise shareholder wealth, must seek the optimal functional and regional configuration of the activities of their organisations. They need to continually question which activities in the organisational value chain are best performed internally, which activities could be outsourced to more efficient external service providers and which activities could be better performed abroad. The global trends are towards finer decomposition of the value chain, relocation of different parts of the value chain to different regions, and towards international division of labour. In a sense, this is a logical outcome of lean manufacturing programs conducted at a global level (Contractor et al., 2009).

BPO refers to the outsourcing of an entire, end-to-end business line or process to an external service provider deemed to be a strategic partner, rather than a traditional supplier (2005). Like many modern business innovations, BPO is an inter-disciplinary construct that comprises both technical and social components, and is defined as an emergent (rather than evolutionary) change phenomenon (Click and Duening, 2005).

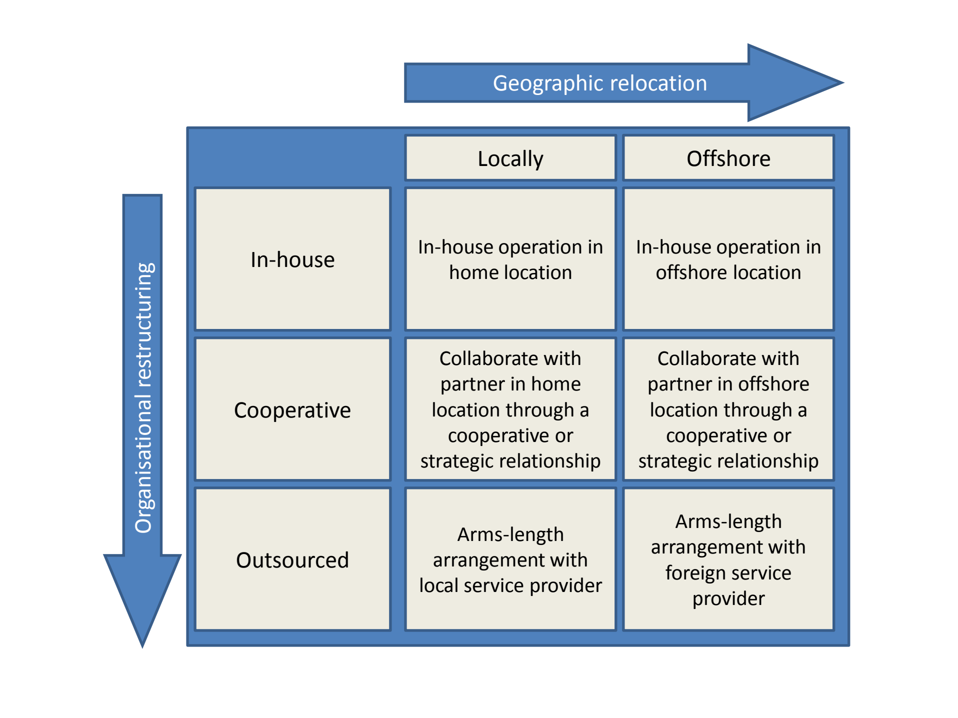


Figure 1: Location and Organisation Form Choices for Parts of the Value Chain (adapted from (Contractor et al., 2009))

Prahalad and Hamel's proposition, that organisations need to develop a portfolio of core competencies specific to the customers they serve, and that they should operate as few non-revenue producing units as possible, is representative of the traditional view of outsourcing (Click and Duening, 2005). Core competencies typically provide organisations with potential access to various markets, increase perceived customer benefit and are hard for competitors to imitate (Chase, Jacobs and Aquilano, 2006). They are central to the organisation's strategy and basis of competitiveness, are often the most profitable portions in the value chain and present the greatest risk if leaked to competitors.

Such competencies are usually difficult to separate from the rest of the value chain, are hard to quantify, measure and monitor and tend to be difficult to transfer to external parties, due to being complex, embedded, or based on tacit knowledge (Contractor et al., 2009). According to the traditional view, business strategies must accentuate the core competencies of organisations that add the most value in the value chain. Functions that add little value and cannot be performed cost effectively should be performed outside the organisation, thus making it possible for organisations to improve their business focus and to reap cost and quality benefits on the back of outsourcers' specialist resources, processes and infrastructure (Pearce and Robinson, 2000).

Contractor et al (2009) argue that fewer competencies are being defined as "core", due to continued dissection and standardisation of organisational competencies, leading to more activities becoming eligible for outsourcing. The notion of outsourcing more strategic portions of the organisation's value chain seems to contradict with the argument that firms must distinguish themselves by these inimitable capabilities. Those sceptical of outsourcing core portions of the value chain believe it will expose organisations to leakage or loss of technology and intellectual property, and risks of supply chain disruptions.

Berger and Gattorna (2001) argue that a critical mass of outsourcing has been achieved in the modern economy. They believe that horizontal and networked business models will be more competitive than vertical integration business models in future. This is in line with the view held by Perman and Scouller (1999), that organisations' ability to share activities could form a basis for competitive advantage, through associated cost reductions and increased differentiation.

Conroy (2008) describes a trend of 'transformational outsourcing': instead of outsourcing a distinct and single business process, organisations are starting to employ a holistic approach to outsourcing in order to achieve wider business benefits across the entire organisation.

2.2.2 *Factors that enable outsourcing*

Click and Duening (2005) describe BPO as the result of a series of parallel evolutionary changes in the business environment which, taken together, produced "surprising, unintended and unexpected" results. A number of factors that enabled the advent of outsourcing (Click and Duening, 2005; Contractor et al., 2009; Norman and Zaidi, 2011) are summarised below (see Appendix B for comprehensive list):

- Globalisation and intensified competition in the market place.
- Free markets and liberalisation of trade and investments.
- The advent of a well-established and reliable global communication and information infrastructure.
- National differences in costs.
- Growing education and skills in developing economies.
- Greater codification of corporate knowledge.
- Modularisation of business functions.
- Reductions in costs of transportation.
- A revolution in management strategy, in which managers seek to share control with various service providers for increased efficiency.

Reasons for the proliferation of outsourcing relate to necessity on the one hand, and the means to implement it on the other. Contractor et al (2009) identified a number of factors that enabled the outsourcing of high-value or strategic functions. These include the emergence of knowledge clusters or "centres of excellence" in specific product or technology areas, a shortage of internal resource skills, (in terms of quality and diversity) talent and the growing importance of foreign markets and related market feedback.

2.2.3 *The "outsourceability" of wholesale banking operations*

Wholesale banking organisations can typically be broken into distinct front, middle and back-office layers.

Front-office areas focus on revenue generation through designing and selling financial products and services that meet the needs of customers. Middle-office areas provide an independent support and control service, to ensure that transactions are validated and accurately captured into operational systems and records.

Operations areas provide the back-office services to bring about proper accounting, payment, settlement and reconciliation of transactions. One of the primary goals of the back-office is to standardise processes and reap benefits associated with achieving economies of scale. To this end, operations must be flexible and modular, allowing it to scale-up or down as the business changes and diversifies (Fung, Fung and Wind, 2008).

Loader (2006) argues that wholesale banking operations functions should be managed as mini-industries that turn trades into realised profits or losses. Operations functions are characterised by complex processes, involving many systems and counterparts, which often need to adhere to strict deadlines. A major part of operations constitute routine processes and procedures associated with processing payments and performing reconciliations. Other areas represent lines of business or products that could be sold, such as fund management and custody services, and thus earn revenue. It is usually a cost centre rather than a profit centre and not seen as part of the “sharp end of the business” (Loader, 2006).

Contractor et al (2009) propose that any business or technical operation that can be codified and digitised is eligible for outsourcing. This holds true for services, despite being traditionally defined as intangible, heterogeneous and inseparable. This view is supported by Norman and Zaidi (2011), who add that the advent of electronic service delivery, which negates the need for costly infrastructure setup and relocation of facilities, makes it possible to implement services outsourcing at a faster rate than in the case of manufacturing.

2.2.4 *BPO trends in wholesale banking operations*

Outsourcing has been prevalent in the global banking industry for many years. The French banking group Société Générale estimate in terms of total contract values, financial services accounted for 29 percent of global outsourcing deals between 2002 and 2007; compared to manufacturing (25 percent) and telecoms (14 percent). The maturation of the industry over the last few years has brought about multi-selective sourcing, consolidation and the expansion of BPO in numerous markets (Conroy, 2008). Norman and Zaidi (2011) determined that in the United States, offshoring of tasks in the financial services industry to developing economies, doubled between 1995 and 2003.

The 2008/9 recession resulted in reduced volumes and margins in the banking industry globally. Goolsby (2011) predicts that the global financial crisis of 2008 will lead to more outsourcing of processes such as treasury, cash management, and custody services. Driven by the impact of the credit crunch and a continued focus on improving efficiencies, and as a way of deferring investment in technology infrastructure, more banks will be outsourcing key business processes to keep costs down. And as banks look to deliver more innovative services, innovation in outsourcing itself is also taking on greater importance (Conroy, 2008).

Economic events in 2008 and the resultant uncertainty of trends in transactional volumes, highlighted the requirement for a flexible approach to capacity planning. Paradoxically, the events resulted in dramatic volume increases in certain areas, such as call centre volumes (Corporate Executive Board, 2008).

The gradual shift of economic power and consumer wealth from the West to the East makes it imperative for financial services organisations to become truly ‘global’, and it has prompted many banks and outsourcing organisations to invest more of their resources in emerging markets (Conroy, 2008; Murphy, 2011). Outsourcing represents a vehicle through which financial services organisations can become globally integrated businesses, as it allows organisations to enter new markets, locate new business opportunities and tap into local centres of skills and knowledge to boost growth opportunities.

Because of the associated shift in jobs the practice of outsourcing is often controversial: while business leaders view it as a management strategy for achieving competitive advantage, the consequent job exports are often criticised by politicians, economists and organised labour representatives. Proponents of outsourcing argue that through a global BPO business network (Click and Duening, 2005), it can create a source of new prosperity for workers everywhere. However, the sustainability thereof depends on the ability of developed economies to replace exported lower-paying jobs with higher-paying high value-adding jobs, such as creation of new goods and services through innovation (Bardhan and Jaffee, 2011).

African business is expected to experience growth from regional shared services operations, where companies consolidate their back-office operations for the African region (Karthik and Rajpal, 2010). The key variable influencing outsourcing service exports, and a literature-based assessment of South Africa's corresponding capabilities, are summarised in the table included in Appendix A.

2.3 Drivers for outsourcing operations to external service providers

Outsourcing is a significant undertaking in terms of time and resources, and organisations need to be clear and confident about the benefits they expect to achieve before executing this strategy.

2.3.1 *Organisational effectiveness drivers*

The literature reports that by assisting organisations to focus on their strengths, outsourcing can enhance organisational effectiveness. It can increase flexibility and the ability to respond to changes in the business environment. It is a vehicle that can assist organisations to transform to different business models, thus facilitating increases in product and service value-adding and improved customer service levels (Chase et al., 2006; Fung et al., 2008).

2.3.2 *Operating efficiency drivers*

A number of drivers that assist organisations to improve their operations are described in the literature. Some sources propose that outsourcing can bring about improvements in quality, productivity and turn-around times. It may enable organisations to gain access to skills, expertise, technology, industry leading practice, methodologies and standards. If implemented successfully, outsourcing can bring about improved management and control, as well as improvements in risk management. Their relationships and association with respected service providers can help organisations to acquire innovative capabilities and improve their corporate image and credibility (Chase et al., 2006). Where outsourcing leads to improved measurements and management information systems (MIS), it could lead to improved compliance and enable organisations to better quantify improvements, such as changes in customer satisfaction levels (BIS, 2005; Casale, 2005; Halvey and Melby, 2007; Conroy, 2008; Fung et al., 2008; Norman and Zaidi, 2011).

2.3.3 *Cost reduction drivers*

The literature suggests that cost is a primary reason why organisations outsource tasks and activities. This pertains to potential savings as well as reduced investments. Conroy (2008) points out that the core banking and main applications systems of some of the big western banks have been in place for more than two decades and have now reached the end of their life spans. These systems need to be replaced and future-proofed for the next 20 years. Sources in the literature propose through using external service providers, organisations can turn fixed costs into variable costs, and avoid, reduce or postpone investment in infrastructure and other assets, thus conserving or reducing capital.

It might be possible, for example, where ownership of assets are transferred to external service providers, for organisations to use outsourcing as a method for generating cash. And, apart from helping to reduce headcount or freeing-up resources to focus on other cost saving activities, organisations can reduce costs by gaining access to service providers' superior capabilities and/ or lower-cost structures; albeit related to wages or other input costs. Some organisations might be able to gain access to better MIS, which could assist to improve cost predictability. Where outsourcing uses an external service provider's existing infrastructure or capabilities, it could increase scalability (BIS, 2005; Chase et al., 2006; Halvey and Melby, 2007; Conroy, 2008; Luvison and Bendixen, 2011; Norman and Zaidi, 2011).

2.3.4 *Revenue growth drivers*

Conroy (2008) explains as a strategy to grow revenue, some of the large banks in developed economies plan to expand into emerging markets. Some literature sources support the view that outsourcing could indeed be a vehicle to grow revenue.

Through their partnership with external service providers, organisations can gain market access to the service provider's network or capabilities, such as infrastructure, language, market insight or skills. Access to service providers' resources and infrastructure could help organisations to accelerate business expansion, achieve rapid product development or even reinvent the business. They could expand production capacity to meet volume demands without having to finance such expansions and could commercially exploit existing skills. It could also enable outsourcers to transfer or mitigate risks, such as demand risks. Reductions or postponements of capital expenditure could assist organisations to increase their return on capital. External service providers' business structures or locations could assist outsourcers to navigate or circumvent global restrictions (Casale, 2005; Conroy, 2008; Fung et al., 2008; Norman and Zaidi, 2011).

2.3.5 *Human resources development drivers*

Back-office functions of many organisations have been exposed to decades of extensive cost cutting, business process reengineering and efficiency programmes. They have recruited fewer resources and failed to retain or attract fast-track managers, often due to the absence of clear and attractive career paths (Berger and Gattorna, 2001). Chase et al (2006) propose that, through outsourcing, organisations can provide employees access to clear career paths and broker an increase in commitment and energy in areas deemed to be non-core to the business.

2.3.6 *Proposition 1*

The business drivers for banks to outsource wholesale banking operations to external service providers include cost reductions, revenue growth, operating efficiency, increased organisational effectiveness and human resources development.

2.4 Outsourcing constraints and risks that lead organisations to conduct operations processing internally

2.4.1 *Environmental factors*

Some of the risks and constraints that prevent organisations from following an outsourcing strategy, stem from the external business environment.

Such risks and constraints include national regulations, tax legislation, currency and political risks (Fung et al., 2008) and protectionism of jobs (Contractor et al, 2009). Bardhan and Jaffee (2011) identify constraints related to outsourcers' sensitivity about security and intellectual property rights protection.

According to the Bank of International Settlements (BIS), growth in offshoring compels banks to monitor "country risk" on an on-going basis; focusing on aspects such as foreign government policies, as well as the political, social, economic and legal conditions in the home countries of external service providers. The BIS argue that banks need to develop appropriate contingency plans and exit strategies to guarantee business continuity (BIS, 2005).

2.4.2 *Loss of strategic control*

Sources in the literature reveal that due to concerns about remaining in charge of aspects that facilitate execution of their business strategy, (BIS, 2005) some organisations may steer clear of outsourcing.

Chase et al (2006) argue that termination of a relationship with a service provider could lead to a loss of strategic control. Organisations may be unable to recover substantial investments, perhaps in the form of relationship-specific assets, co-located facilities, brand-equity, proprietary learning or R&D investments. Risk of intellectual property (IP) losses would be higher under circumstances of weak or unclear IP protection frameworks, or where such IP or technology is easy to copy.

Contractor et al (2009) point out that it is generally not possible for organisations to cover all contingencies in an outsourcing contract, more so when related knowledge is tacit or organisation specific.

Luvison and Bendixen (2011) argue that the tendency of organisational capabilities to change over time, may cause firms to lose such capabilities and not be able to regain these if the service provider fails; which may result in competitive capabilities being levelled-out across the market.

A further constraint relates to the difficulty in distinguishing between, and the changeability of, core and non-core activities. Rapid changes in the industry may bring about a situation where an outsourced activity, previously not deemed to be strategic, might take-on a strategic role. The IT operation within banks is an example of an area of activity that is unlikely to be a sustainable source of competitive advantage, despite it being deemed as core to its business (Chase et al, 2006).

2.4.3 *Competitive threats*

Some sources argue that outsourcing could undermine the ability of firms to remain adaptive and maintain a strategic advantage. Outsourcers face a risk that service providers, once proficient in the outsourced service and having gained full access to the outsourcer's business network, could become competitors through forward integration (Chase et al., 2006; Contractor et al., 2009; Luvison and Bendixen, 2011). Organisations may also shun outsourcing due to risks of information leakage to competitors, albeit through relocation of skilled resources to the service provider or leakages as a consequence of staff-turnover at the service provider (Contractor et al., 2009).

2.4.4 *Cost escalations that off-set savings*

Whilst cost saving is a primary driver for outsourcing, many organisations are weary of consequent cost escalations that could off-set anticipated savings. A study by Deloitte Consulting found that half of organisations who shifted processes offshore, failed to achieve the anticipated financial benefits (Fung et al., 2008).

Organisations might underestimate the up-front fixed costs or due diligence efforts to set-up appropriate contract structures (Bardhan and Jaffee, 2011).

Rising labour costs are a major area of concern: for example, growth in emerging markets such as India and China has led to reduced labour surpluses, higher living standards and increased wage levels; making it much more expensive for service providers to recruit and retain staff (Conroy, 2008; Chowdhury, 2011; Tarakad, 2011b). It requires service providers in these locations to move up the value chain and broaden their portfolio of offerings, to offer compelling value propositions.

Costs associated with office rental and infrastructure development or maintenance in popular offshore destinations have also risen (Contractor et al, 2009).

Contractor et al (2009) list governance overheads, monitoring and coordination costs as other areas of cost escalation. They believe organisations find it harder to transfer knowledge between two unrelated organisations than in-house, especially where the knowledge is tacit in nature. They argue that vertical integration makes it possible to avoid or reduce many transactional costs. Compared to outsourcing, vertical integration has the advantage that, whilst associated costs are once-off, the benefits of accumulated expertise and routines are enduring.

Luvison and Bendixen (2011) have found increased efficiency associated with outsourcing brings about increased learning requirements. The "increased expediency” associated with outsourcing results in increased managerial and strategic complexity. In order to contend with risks and complexities, organisations revert to building reserves in the form of inventory, capacity or redundant suppliers, which result in the intended benefits of outsourcing being eroded.

2.4.5 *Management capability*

Sources in the literature suggest some organisations may not have the management skill to properly implement and realise benefits from an outsourcing strategy.

Constraints in management capability may be exacerbated by limited management capacity (or “bandwidth”) as well as budgetary constraints (Casale, 2005).

Spatial separation of business activities brings about inefficiencies and challenges easily dealt with through face-to-face communication, may be exponentially harder to resolve over distance. Inefficiencies may also relate to lack of trust between parties, existence of disparate incentive policies, cultural differences or time-zone differences (Contractor et al, 2009).

Luvison and Bendixen (2011) argue that it requires specific skills and competencies to design and implement service level agreements and to manage outsource relationships. Organisational changes associated with outsourcing are often far-reaching, both operationally and behaviourally and causes organisational complexity that necessitates increased management effort. Chase et al (2006) propose that management skills associated with coordinating relationships between mutually supportive, but separate organisations are not traditionally part of the armour of organisations’ core management skills. Fung et al (2008) suggest that managers may not even be aware of, let alone skilled in, the orchestration role they need to perform across a business network brought into being through outsourcing. They define three fundamental changes associated with the orchestration role of management. Firstly, managers are tasked to empower, rather than control. Secondly, value creation becomes the result of integration, rather than specialisation. Thirdly, the management focus shifts from the firm to the network.

Fung et al (2008) further point out that constraints may be inherent to the management culture of organisations, such as a fear of losing control and sharing rewards or a resistance to networking. Although transactions can be digitised, the prerequisite trust and business relationships needed to make it work, cannot.

In summary, successful delivery of an outsourcing strategy requires organisational change proficiency, as well as adaptive leadership styles and cultures (Luvison and Bendixen, 2011).

2.4.6 *Human resources interests*

Some organisations may be hesitant to pursue an outsourcing strategy, due to concerns about the interests of their human resources. Outsourcing is often associated with staff lay-offs or where staff gets transferred from the outsourcer to service provider, it is often associated with reduced wages or benefits. Certain stakeholders might see an outsourcing strategy as an attempt to circumvent trade union contracts (Chase et al., 2006).

2.4.7 *Process control and operational risk*

A review of the literature reveals that organisations may refrain from outsourcing tasks and activities for fear of loss of process control, service deterioration or breakdown. Tarakad (2011a) reports that a growing number of financial services firms have moved offshored activities, such as call centres, to onshore locations, due to customer complaints about offshore operations.

Fung et al (2008) points out that process control risks are greater where outsourced activities involve inter-linked systems. Various sources are concerned that organisations may find it challenging to integrate outsourced, internal and other third-party services across end-to-end business processes. It may be as a consequence of complex process or systems interfaces, or because the knowledge to be exchanged between parties is of a tacit nature (Chase et al., 2006; Halvey and Melby, 2007).

This view is supported by Luvison and Bendixen (2011), who point out that, apart from the process control difficulties associated with tacit knowledge, learning challenges may occur due to a lack of motivation to transfer knowledge to the service provider, or the inability to absorb such knowledge. Furthermore, it may be challenging to manage service failures in an outsourcing environment, especially where services outsourced to different vendors need to be integrated (Halvey and Melby, 2007).

Contractor et al (2009) argue that greater location and organisational form diversification, increases organisations' overall supply chain risk. This is echoed by Luvison and Bendixen (2011), who add that outsourcing may expose organisations to the same risks faced by their external service providers.

Operational risk management is a trade mark of wholesale banking operations, driven both internally and by the obligation to comply with ever changing external regulatory requirements. Outsourcing may well increase the administrative burden associated not only with understanding and controlling business processes, but also the ability to demonstrate as much to regulators. The BIS notes specific concerns related to banks' over-reliance on outsourced services that are critical to their on-going viability. Over-reliance on external service providers, if not adequately constrained through the market and regulatory environment, (BIS, 2005) may also lead to systemic problems.

Banks are obliged to take steps to mitigate risks to the financial and infrastructural resources of external service providers. Preservation of strong corporate governance is a prerequisite and banks must ensure that governance is not diluted as a consequence of an outsourcing strategy. Regulatory compliance obligations may not be transferred to another entity and banks need to ensure that internal and outsourced operations meet the same standards (BIS, 2005; Loader, 2006).

Banks' outsourcing decisions must be made with due consideration to governance and performance metrics, as much as financial merits (Loader, 2006).

The various forms of risk banks need to contend with when pursuing an outsourcing strategy are strategic, reputational, compliance, operational, exit strategy, counterparty, country, contractual, access, concentration and systemic risk (BIS, 2005). Please refer to the table in Appendix C for definitions of each of these.

2.4.8 *Proposition 2*

The constraints associated with BPO, which include risks and constraints embedded in the external business environment, loss of strategic control, increased competitive threats, cost escalations, insufficient management capability, HR interests, loss of process control and operational risk, cause organisations to perform operations processing internally.

2.5 Conclusion of literature review

The literature review reiterates the significance of outsourcing as a management strategy, in terms of the key decisions with regard to locations and organisational forms that business leaders need to contemplate on an on-going basis.

The literature review revealed a number of trends in international business, including ever finer decomposition of organisational value chains, increased modularisation and greater codification of tasks and activities. These trends lead to more and more processes becoming eligible for BPO; including aspects that were traditionally deemed to be core and of strategic business importance.

The prevalence of outsourcing must be considered against the background of a number of enabling factors in the international business environment; these include increasing globalisation of business, growth of free trade arrangements, national cost differentials, and growing skill levels in emerging markets. Advancements in information and communication technology and infrastructure roll-out makes it possible for “service” tasks and activities to be delivered electronically from remote locations, and to roll-out services outsourcing at a faster rate than manufacturing.

It is apparent that BPO is already a feature of wholesale banking operations and indications are that present-day market circumstances, characterised by subdued revenue levels, will further incentivise banks to reduce cost-to-income ratios and increase scalability (upwards or downwards) through BPO strategies.

2.5.1 *Research propositions*

The literature review confirms the existence of numerous drivers for organisations to embark on BPO strategies. These form the basis of the **first research proposition** that drivers to reduce costs, grow revenue, achieve operating efficiency, increase organisational effectiveness and develop human resources, will cause organisations to pursue BPO strategies.

However, it is also apparent that organisations need to be mindful of several risks and constraints that may render the pursuit of a BPO strategy worthless. This forms the basis of the **second research proposition**, which is that risks and constraints embedded in the external business environment, loss of strategic control, increased competitive threats, cost escalations, insufficient management capability, HR interests, loss of process control and operational risk cause organisations to perform operations processing internally.

3 RESEARCH METHODOLOGY

This section describes the methodology used to address the propositions put forward in the literature review.

3.1 Research paradigm and approach

This research represented a simple, interpretive study and followed a qualitative research approach.

The research topic in question required an understanding of the phenomena in a natural (rather than experimental) setting, focusing on the views and experience of representatives from the industry, to address the defined research propositions through an inductive approach.

The major factors influencing research strategy and design, include the research topic and methods considered appropriate for the topic, the research audience, as well as the availability of time plus other resources (Walsham, 2006; Greener, 2008)

The interpretivist paradigm promotes seeing the world through the eyes of those involved in the study and gaining multiple perspectives of the content, rather than the single reality-view that underscores positivism. The assumptions of the interpretivist paradigm, which embraces inductive (or evolutionary) research processes, active researcher interaction, and subjective and multiple realities (Greener, 2008), are well suited to researching this topic.

Researchers who subscribe to the interpretivist paradigm typically use qualitative research methods, such as semi-structure or unstructured interviews, to investigate perceptions of reality by stakeholders in industry (Greener, 2008). A qualitative approach is suitable for research of an exploratory nature, and permits the researcher to form an in-depth understanding of the topic. It is also suitable for capturing complexity and is sufficiently flexible to incorporate unexpected findings (Mouton and Marais, 1989; Thompson, 2004)

3.2 Research design

The research commenced with a comprehensive literature review that explored general, non-industry specific drivers and constraints on outsourcing. The findings from the literature review formed the basis of two researchable propositions, which were tested using a qualitative research approach.

In-depth, semi-structured interviews were used to do cross-sectional (as opposed to longitudinal) research amongst experts in the selected industry. It was expected that participants in the study would deem this to be a valid method for addressing the research propositions, thus contributing to greater face validity (Greener, 2008).

This research method was deemed to be appropriate for the study, as it allowed for collection of first-hand input from experts on the defined research problems.

The selected method had several advantages and disadvantages.

Advantages included the ability to control how the questions were asked, to immediately confirm and address misinterpretations and to probe for additional information (Greener, 2008). These advantages provided the researcher with the opportunity to not only build on the findings from the literature review, but also to explore nuances or complexities specific to the selected industry and location, and to discuss and form a detailed understanding of any unexpected findings. It is proposed it would not have been possible to accomplish similar results using other methods.

Mouton and Marais (1989) point out that researchers need to contend with researcher attributes, such as the researcher's affiliation, image and researcher-subject distance, as well as the research subjects' orientation, e.g. inherent in their role, motivations and response sets. Thus, when conducting interviews, the researcher was conscious of bias that might be brought about through his presence and conduct, e.g.in his capacity as a colleague, superior or subordinate, a representative of a competitor organisation or a prospective client contact to external service providers. The researcher was cautious not to cause ambiguity when presenting questions or to give his own views when presenting questions or recording and interpreting responses. Mouton and Marais (1989) further caution against issues such as 'memory decay', the 'know-it-all syndrome' and 'over saturation' of the researcher and subjects.

3.3 Population and sample

The population in this research was executive management in the wholesale banking operations industry in South Africa, including banks, service providers and industry bodies, who may consider pursuing BPO as a management strategy, in their capacity as client, service provider or advisor.

Thirteen people participated in the research, including:

- Six executives in the employ of the big four South African banks, being:
    - ABSA,
    - First National Bank,
    - Nedbank and
    - Standard Bank.
- Six executives in the employ of BPO firms or consultancies, namely:
    - Accenture,
    - BankservAfrica,
    - Elix-IRR,
    - IBM,
    - KPMG and
    - Perago.
- One representative from a banking industry body, being the International Payments Framework Association.

Sample selection may have had a significant bearing on external validity, i.e. the extent to which research findings could be generalised (Mouton and Marais, 1989).

A purposive sampling method was used to select representatives from the ranks of experts in the South African wholesale banking industry. Greener (2008) explains that the purposive sampling method is often used when conducting qualitative research amongst smaller populations, which is limited in absolute terms due to the concentration of the South African wholesale banking operations sector. Whilst the method constrained the researcher from making statistical inferences about the population, it did permit a degree of generalisation. Selecting representatives from various sub-groups in the industry also brought about a degree of triangulation.

The respondents were invited to participate in the study. They were provided with details of the purpose of the study, the research process and expected interview duration. The respondents were assured their responses will remain confidential, and they were offered a copy of the research report as an incentive to participate in the study. Interviews were conducted in-person or via telephone.

3.4 The research instrument

Semi-structured interviews were based on a set of guide questions asked of all respondents, but the interviewer was permitted freedom to ask further questions. Interviewees were permitted to divert the conversation to other points , whist the interviewer was responsible for managing the process (Greener, 2008).

A covering letter example and the guide questions used are included in Appendixes D and E.

3.5 Data analysis and interpretation

Outcomes from the semi-structured interviews formed the source of research data. The contents of these were transcribed and subjected to content analysis, with the aim of identifying patterns. The steps followed, which align with the key requirements for qualitative data analysis, as defined by Greener (2008), included:

- Using descriptive codes to cluster themes from the data in a manner that aligns to the framework from the literature review.
- Creating additional codes and code levels to accommodate new themes or factors that emerge.
- Recording the frequency of factors, as well as respondents' view of the relative importance thereof.
- Completing these steps iteratively until it led to a saturation of categories.
- Identifying patterns that emerge from the data through the categorisation process.
- Synthesising and generalising the outcomes so as to construct overall outcomes and conclusions.

No quantitative analysis was performed on the data.

3.6 Validity and reliability

3.6.1 *External validity*

External validity refers to the extent to which the results of the study could be generalised (Mouton and Marais, 1989; Greener, 2008).

Mouton and Marais (1989) suggest the major determinants of external validity are the sampling method, the context in which the research is being conducted, and the time or period when the research is conducted.

The external validity of this study was limited by the inability to select a random sample from the population. The researcher thus used his familiarity with the industry network to select representatives from various sub-groups deemed to be representative of the broader population.

The context and timing of the research had a lesser impact on external validity as it took place in a real-life setting. All the respondents were actively involved in the industry and the strategic and long-term nature of BPO interventions largely negates concern associated with timing, despite the existence of exceptional economic circumstances at the time of the research.

Although not the primary aim of the study, it was possible to make some inferences from the finding to outsourcing of operations and other group enabling functions in retail banking and other financial services organisations.

3.6.2 *Internal validity*

Internal validity is associated with causality, i.e. the extent to which conclusions can be drawn regarding cause-and-effect or other relationships within the data (Mouton and Marais, 1989; Greener, 2008) e.g. the extent in which cost saving considerations drive organisations to pursue BPO opportunities.

The selection of semi-structured interviews, combined with a purposive sampling method, yielded good internal validity. This approach largely circumvented issues associated with the validity of theory, measurement, reliability and inferential reliability, which – according to Mouton and Marais (1989) – are the major determinants of internal validity.

3.6.3 *Reliability*

Reliability deals with the question of being able to produce the same results different researchers achieved, using the same methods at different times. Reliability is determined by the researcher, the subject, the research instrument and the research context (Mouton and Marais, 1989).

The combination of researcher bias (based on his experience in the industry), using qualitative research methods and a purposive sampling method, makes it unlikely that the same study conducted in a different context and at a different time will yield the same conclusions.

The reliability was however improved through using semi-structured interviews, based on a set of guide questions grounded in the outcomes of a comprehensive literature review.

3.7 Limitations of the study

There are a number of limitations associated with the research, based on:

- Using a qualitative research instrument, permitting inconsistent responses.
- The small sample size.
- Using a purposive sampling method.
- The researcher’s bias and affiliation with respondents, including competitor or vendor organisations or wanting to portray a positive image.
- Time constraints, e.g. associated with selecting participants, conducting interviews and analysing outcomes.

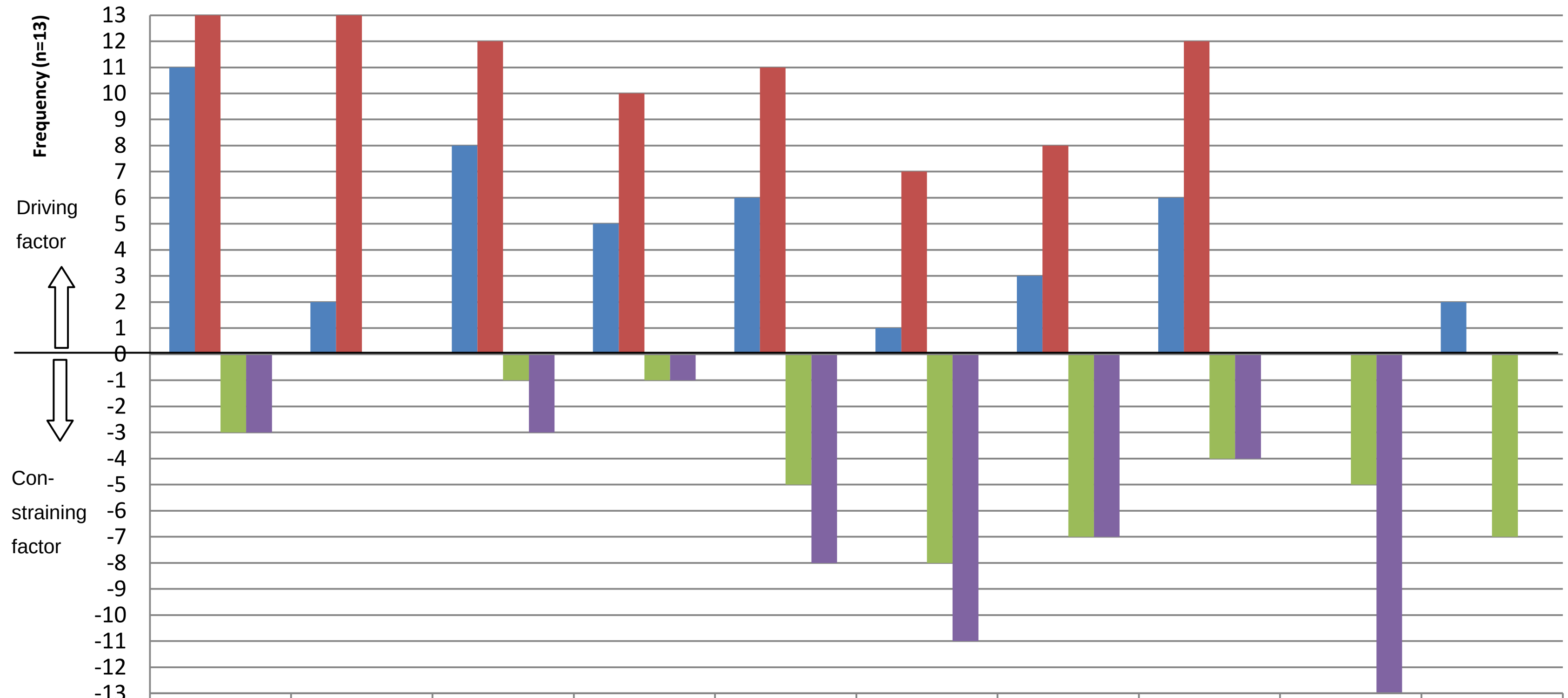
4 RESULTS

4.1 Results summary

The results from the semi-structured interviews, detailing the driving and constraining factors identified by the participants, were summarised in Table 1.

Table 1 depicts the various driving and constraining factors on the x-axis, with the y-axis indicating the frequency count of each of the factors. The table reflects that several factors transpired to be both drivers and constraints of outsourcing. Factors found to be drivers were allocated positive values (ranging between 1 and 13, there being 13 research participants); whilst constraints were allocated negative values, thus providing a holistic view – indicative of the overall driving or constraining tendency thereof. The frequency count was noted in terms of the number of participants who identified the factor outright, and after further prompting by the researcher.

Table 1: Results summary



	Cost	Revenue	Organisational effectiveness	Operating efficiency	HR management and development	Strategic organisational control	Process control & operational risk	Market competitive ness	Management capability	Environmental factors
Outright	11	2	8	5	6	1	3	6	0	2
Prompted	13	13	12	10	11	7	8	12	0	0
Outright	-3	0	-1	-1	-5	-8	-7	-4	-5	-7
Prompted	-3	0	-3	-1	-8	-11	-7	-4	-13	0

4.2 Cost

N=13	Driver		Constraint	
	Outright	Prompted	Outright	Prompted
Cost reduction	11	13	3	3

All the research participants identified prospective cost reductions or containment as a principal driver for outsourcing.

Participants argued cost reductions, and consequent cost-to-income ratio improvements, could be realized through greater economies of scale, by using existing operations capabilities and infrastructure to process greater transactional volumes. Outsourcers could benefit from fixing processing costs as contracted, thereby providing them with greater cost control and a firm base for financial planning. It also presents an opportunity to move expenses from fixed to variable or consumption-based costs – an attractive prospect to small or mid-tier banks, where processing volumes are sub-scale and of a seasonal nature. They might also transfer the risks associated with operational cost increases, losses and insurance obligations to the BPO vendor.

By using a BPO vendor's resources and infrastructure, organisations can limit or reduce capital expenditure, which also permits them to allocate capital to revenue generating business opportunities. It presents innovative investment opportunities, e.g. jointly developing processing solutions based on an arrangement where the outsourcer benefits from the solution, without incurring development cost, whilst the BPO vendor retains license to the solution and associated future revenue generating opportunities. Consequent strengthening of the outsourcer's balance sheet is particularly significant in the banking industry, given the regulatory requirements for increased capital holdings , such as the Basel III requirements.

However, three of the participants highlighted constraining factors associated with the cost theme. They were concerned about wage inflation eroding cost reduction opportunities: whilst the banking industry in developed economies has realised substantial savings due to international cost differences, such cost saving opportunity is considered to be much lower in South Africa. They also had reservations about the potential scale-benefits that could be realised, given the lower levels of maturity and scale of the South African banking industry. Potential benefits are limited by comparatively low levels of maturity of enabling technology infrastructure, education-levels, skills and available intellectual property in South Africa. Also tax (particularly VAT) implications may erode any cost savings, although the effect of this could be mitigated through contract structures.

Initial costs of implementation projects, including severance packages payable to impacted human resources may erode cost savings. Consideration must also be given to project costs to be incurred by implementing changes during the contract term, e.g. change orders to accommodate new products or processes – depending on the terms as contracted.

Cost savings are not likely to materialise without a well-defined operating model, e.g. if isolated processes are outsourced with arbitrary cut-off points, it may lead to the same processes being re-established internally.

4.3 Revenue

N=13	Driver		Constraint	
	Outright	Prompted	Outright	Prompted
Revenue growth	2	13	-	-

All the research participants identified potential revenue growth as a driver for outsourcing. None of the participants pointed out any associated constraining factors.

The supporting arguments raised in favour of outsourcing included opportunities to increase the scope of service offerings, to increase the client base through reciprocal arrangements with vendors, or to increase sales activities and grow transactional volumes based on access to greater processing capacity.

It was argued that banks could leverage the BPO vendor's resource to perform sales activities or generate leads. Examples were cited where resources of a BPO vendor were able to achieve higher rates of cross and up-selling, and avoid revenue leakage, presumably based on being more consistent in applying processing discipline and routines, based on contracts and the need to prove adherence thereto. Better achievements are further ascribed to higher motivation levels of the BPO vendor work-force, who are seen as part of the front-office of the outsourcer, rather than being resigned to a back-office role.

Bank might also use the capabilities (infrastructure, functionality and knowledge) of BPO in given markets to introduce new products or access markets more rapidly and at lower cost. Their superior functionality or quality standards could provide a competitive edge in revenue generation in a chosen target market. In general, an operations outsourcing arrangement permits focus of management energy on revenue generation, rather than operations activities and cost containment.

At a more foundational level, it was argued outsourcing may provide an opportunity to rapidly implement a target operating model that is better aligned to the market circumstances, and thus obtain a competitive advantage to grow revenue. This may include a model in which operations processing is commercialised, i.e. using existing assets and infrastructure to offer process services to third parties and thus create an additional revenue stream.

Some participants qualified the revenue growth opportunities, pointing out that positive effect on revenue will only occur if the outsourcing arrangement is very mature and if outsourcing relates to the bank's core capabilities.

4.4 Organisational effectiveness

N=13	Driver		Constraint	
	Outright	Prompted	Outright	Prompted
Organisational effectiveness	8	12	1	3

Twelve of the research participants identified prospective improved organisational effectiveness as a driver for outsourcing. It was pointed out these may refer to the outsourced capabilities, as well as the retained organisation.

The supporting arguments participants raised in favour of outsourcing included:

The research participants discussed opportunities to leverage the depth of resources, skills, expertise and platforms of the BPO vendor; for example in areas of business process optimisation, continuous improvement practices, analytics, quality control and adherence to standards. Banks may benefit from a BPO vendor's quality certifications or capability-maturity (CMMI) ratings, which may exceed those of the outsourcer or their change execution ability. These may be related to business transformation, process solution or enabling system changes, with consequent speed-to-market benefits.

Research participants argued that outsourcing enables implementation of service level agreements (SLA), supporting metrics and reporting to demonstrate adherence to improvements to SLAs, as well as benchmarking to leading practice.

Banks might be able to leverage the capacity of BPO vendors' to keep their enabling platforms current, based on the greater scale of their operations and matching infrastructure. In general, banks could benefit from a greater commercial mind-set in traditional back-office and support environments.

However, three of the participants highlighted constraining factors associated with the organisational effectiveness theme. This related to the dynamism of corporate and investment banking and the difficulty of completing an SLA in a manner that provides the requisite levels of flexibility and risk management. Non-bank service providers may not have all the requisite infrastructure and capabilities required by banks.

Participants expressed concerns about eroded service support levels, which may be as a consequence of time-zone differences (which may impact service responsiveness), differences in language and differences in culture, which may affect communications, or ability to deal with conflict.

Participants explained that banks deal with increasingly informed and demanding customers, with very high service expectations.

4.5 Operating efficiency

N=13	Driver		Constraint	
	Outright	Prompted	Outright	Prompted
Operating efficiency	5	10	1	1

Ten of the research participants identified prospective improved operating efficiency as a driver for outsourcing. This is seen as a primary driver for outsourcing, essentially based on the premise of using the BPO vendor’s efficient processing capability to the benefit of the outsourcing organisation.

The supporting arguments that participants raised in favour of outsourcing referred to top-tier BPO vendors generally being leaders in the area of process improvement and/ or re-engineering, e.g. using lean six-sigma methods, with supporting management information and controls, which can be deployed to the benefit of the outsourcer. Their discipline and rigour in process management can also translate into benefits related to greater flexibility and agility in accommodating business changes.

Only one constraining aspect was identified, and that related to implementation of certain operating improvements that may not have the same priority to the BPO vendor as the outsourcing organisation.

4.6 Human resources management and development

N=13	Driver		Constraint	
	Outright	Prompted	Outright	Prompted
Human resources management and development	6	11	5	8

Eleven of the research participants considered human resource development opportunities to be a driver for outsourcing.

Their supporting arguments in favour of outsourcing included references to cross-training opportunities, with associated growth and productivity benefits. They argued that people could gain access to the rich intellectual property and industry leading practices that exist in many BPO firms and that resources with skills and experience in outsourcing, may become more marketable in the industry.

Participants believed that outsourcing could contribute to employment creation in developing markets plagued by high-levels of unemployment – thus fulfilling a social responsibility. It may present opportunities to improve an organisation's BBBEE ratings and achieve headcount targets. It could address key person dependencies by gaining access to the BPO vendor's human capital and enhance the career paths of human resources (often in specialist roles), potentially offering better career opportunities, which may also lead to increased levels of motivation and retention.

BPO vendors may offer leading HR management services, which may serve to guide the outsourcer through the people change process. The South African business environment presents several challenges to employers, with associated impact on management resources. Banks may welcome the opportunity to transfer this burden to a BPO firm, which may be better positioned to deal with such challenges.

However, participants highlighted several constraints associated with the human resources development theme. They explained that, at the time of announcement of an outsourcing initiative, it tended to have a negative impact on staff morale, with associated service delivery risks. The changes that affected people typically needed to contend with were to either transfer from the outsourcing firm to the BPO vendor, seek a redeployment opportunity at the outsourcing firm or be made redundant. The impact on staff morale is often broader that on just the directly affected people. Organisations may prefer to avoid the complexity and management time consumed, as well as the impact on morale of staff redundancies.

Participants were averse to the risk of losing business knowledge that may have formed the basis of a competitive advantage. A concern was raised that, even where knowledgeable people transferred to the BPO vendor, it may lead to fragmentation and dilution of the skills base over time. Loss of business knowledge may create a lock-in situation, where the outsourcing organisation can't move out of the arrangement, or move the capabilities back in-house, leaving them to contend with costs increases and/ or deteriorating service or risk levels.

People who transfer to the BPO vendor may experience an organisational cultural shock, with associated negative consequences for morale and turn-over. It was argued that the parties' ability to deal with resistance to change in an effective manner will be determinant of HR development proving to be a driving or constraining factor for outsourcing.

It was pointed out that career paths on offer to people transferring to a BPO vendor tend to be of a specialist nature, which may not align with some people's aspirations.

4.7 Strategic organisational control

N=13	Driver		Constraint	
	Outright	Prompted	Outright	Prompted
Strategic organisational control	1	7	8	11

"Strategic control can't be achieved through adherence to a SLA. The client must still feel they have a level of control of work done in an outsourcing environment, without it being construed as interfering".

Seven of the participants indicated that banks may benefit from improved strategic control as a consequence of outsourcing. They argued banks could outsource execution of processing, whilst retaining control of decision-making. The experience of some banks, that control can be retained despite outsourcing of functions, have led to more "core" work being seen as eligible for outsourcing. Control risks brought about through outsourcing could be managed, e.g. through thorough contracting, governance and service management processes. It was pointed out that outsourcing demands a hands-on control framework, e.g. in light of reduced ability to access information. Loss of control may lead to a bank re-establishing or replicating a processing capability that was outsourced, which erodes or negates the outsourcing benefits.

Research participants proposed that outsourcing could bring about greater transparency, e.g. better metrics and management reporting, which may enable banks to identify and pursue strategic options. Improving control technology solutions can be used to address historical concerns.

There should be no loss of control in an organisation that is relatively stable and given the existence of a properly designed operating model. However, if the business is in a state of flux and there is a lack of strategic stability, being locked into an outsourcing contract might become an impediment to change

Eleven of the participants stated that banks risk losing some strategic control as a consequence of outsourcing. Arguments were made that outsourcing of core organisational capabilities present higher strategic control risks. The change may alter the relationship with clients and third parties.

There were concerns that South African banks may face a situation where they need to compete for prioritisation with change requests from other global BPO firm clients. This prospect is particularly worrisome where the BPO firm has major international banks as clients.

Participants were sceptical about banks having to “fit the mould” and align to the offering delivered to various BPO firm clients, thus limiting their own ability to innovate. Outsourcing arrangements may introduce legal dependencies on BPO firms and banks consequently face risks associated with the financial failure of BPO firms.

Participants argued that, in certain specialist sections of corporate and investment banks, e.g. global markets trading, the front-office prefers operations processing to be “close to the business”, associated with a front-to-back organisation design, due to business benefits associated with direct influence and control. Risks associated with loss of control are lower where outsourced processes are highly commoditised.

Participants made the general point that the strategic control risk or benefit will depend on the relationship with the service provider, cultural fit and the strategic importance of the arrangement for both parties - the existence of “shared destinies”. Such real strategic partnerships must address key change initiatives and skilled staff allocation. It was pointed out that strategic control becomes a bigger risk in later stages of the (typically 5 year) outsourcing contract period.

"Later contract years are normally the stage when vendors break even and start generating profits, meaning they are unwilling to make any further investments".

Participants suggested that banks should refrain from outsourcing functions they don't understand properly, as outsourcing will exacerbate control risk under such circumstances.

Participants did not express any real concerns of BPO firms becoming competitors to banks, as provision of financial services is not deemed to be a core capability of BPO firms.

4.8 Process control and operational risk

N=13	Driver		Constraint	
	Outright	Prompted	Outright	Prompted
Improved process control, reduced operational risk	3	8	7	7

Eight of the research participants identified prospective improved process control and associated reduced operational risks as a driver for outsourcing.

They argued BPO firms often claim to be advanced, diligent and disciplined in adhering to process standards and controls, including using metrics and generating management reports, as this is a core competency area to them. It was acknowledged that there are several areas in corporate and investment banking operations characterised by high loss potential, e.g. corporate action losses, derivative payments, where banks could benefit from external party's superior control capability. Depending on delivery expertise of the BPO firm, it may even be possible for them to make leading practice-based recommendations, which can be implemented based on a bank's sign-off. Banks that are expanding abroad could achieve their goals to manage process controls and risks consistently on a global basis through outsourcing to a BPO firm.

Participants stated that outsourcing doesn't fundamentally change the level of risk. And some leading BPO firms are prepared to carry operational risk (i.e. absorb related losses, incur insurance costs etc.).

Seven participants identified constraints associated with process controls and operational risks. They raised the point about in-house resources having a greater appreciation of criticality of processes and embedded reputational risk. One participant expressed doubts if an external party will apply the same amount of diligence.

Participants further argued that process control becomes harder under outsourcing, due to the bank's loss of autonomy and reliance on a third party (particularly when outsourcing to an offshore BPO firm with time-zone differences). The bank may be left with a reduced ability to influence process controls and be reliant on what was stipulated in a SLA. Process control failures on the side of the BPO firm may impact the bank's clients or business partners, with consequent commercial losses and detrimental effects on business relationships, adherence to contracts and associated legal consequences.

Information (including of clients and transactions) and intellectual property available to operations processing areas is often of a sensitive nature and outsourcing may translate into increased information security risks.

A concern was raised that BPO firms may not invest in and maintain process control and security resources and infrastructure that are peculiar to banking, e.g. with reference to SWIFT messaging. Outsourcing may result in legal complexities in terms of obligations to customers.

Ultimately, customers still see a bank as the responsible party (despite outsourcing of operations processing), leaving banks exposed to reputational risk in case of service issues.

Some participants pointed out that achievement of benefits will be dependent on how the topic of operating efficiency is addressed in the outsourcing contract: If outcome based, with regards to target cost and efficiency ratios, it will drive operating improvements. But if input based, for example based on number of full-time equivalent staff members (FTEs) used, charged against a rate card, it does not drive operating improvements. This model is also hard to sustain over time.

Participants further argued that success depends on the extent to which the outsourcing arrangement allows the BPO vendor to take an end-to-end process view: if a critical mass of processes is moved to the outsourcer, it permits for significant operating improvements.

"Managing risk has been top of the agenda in the banking industry for the past five years".

It was proposed that operational risk needs to be managed on a front-to-back basis and thus requires integration of processes and systems, front-to-back, for the sake of alignment and integrity. Process control and operational risk constraints and benefits will depend on a bank's importance to the service provider and the ability of the service provider to respond to a bank's changing control requirements. Risks would be lower in a captive model, i.e. where ownership of the BPO firm resides with the outsourcer.

4.9 Ability to deal with competitive threats and opportunities

N=13	Driver		Constraint	
	Outright	Prompted	Outright	Prompted

Ability to deal with competitive threats and opportunities	6	12	4	4

"Outsourcing has resulted in enhanced delivery of service and improved customer facing experience."

Twelve of the participants believed that outsourcing can enhance the level of competitiveness of banks.

They argued that it could place banks in a better competitive position, using the strategic skills, experience and resources from service providers who specialise in operations processing. Such parties may also be in a better position to do the necessary investment in skills and infrastructure to remain current. Outsourcing may enable quick time-to-market for new market entries, e.g. the Sub-Saharan African continent, leveraging the BPO firm's skills in local market conventions - something especially appealing for small and mid-tier banks.

Another argument of the twelve participants was that outsourcing of non-core capabilities could allow banks to focus time and money on those areas that distinguish them in the competitive market. This includes re-focusing management energies and attention to core revenue generating business that provides competitive advantage. Outsourcing may offer opportunities to share risks associated with operations processing.

Some participants believed that it is becoming more prevalent to outsource core capabilities that provide organisations with a competitive edge. In banking, only selected competency areas, such as developing and selling financial services and products, should not be outsourced. Outsourcing of core capabilities potentially presents much bigger returns from outsourcing endeavours. Banks should focus on "outcomes" and attempt to use other parties' capabilities to their benefit.

However, other participants believed that banks shouldn't outsource core functions and processes. Accordingly, if only non-core, transactional capabilities are being outsourced, it will not have a significant effect on the ability to deal with competitive threats.

Four participants identified constraints associated with dealing with competitive threats and opportunities through banking operations outsourcing. They raised concerns about banking evolving towards ever more complex transactions, demanding increasing levels of innovation, with complex operational requirements to process transactions in the right way. They were worried about outsourcing leading to intellectual property infringements. For example, if a bank comes up with a processing solution which gets implemented by a BPO vendor, the same solution could also become accessible to competitors.

Much management bandwidth may be consumed to put together and subsequently implement an outsourcing arrangement. Although of a temporary nature, it may reduce management focus on efforts in other key strategic initiatives, e.g. dealing with competitive threats.

Participants proposed that, given enough internal operations processing scale, a bank could develop it to become a source of competitive advantage, rather than pursuing it through outsourcing.

General comments were made by participants about the South African and regional banking industry becoming increasingly competitive to maintain historical growth rates.

"Being an average player is no longer good enough for sustainability. Banks need to play to their strengths in order to be competitive."

Global banking markets are saturated and South Africa's historically isolated market is now becoming an attractive prospect for international players. There may be an opportunity for a South African bank to be the first mover in the industry to provide outsourcing in this environment.

Ideal positioning in the competitive market requires flexibility in the outsourcing contract and the way it is governed. For commoditised products, with high margin squeeze, outsourcing could give banks an advantage. However, banks will be at a disadvantage where they need to be responsive to business changes.

Participants noted that banks may have several vendor options available for outsourcing general, run-of-the-mill business processing. However, the more specialised the processing becomes, the fewer the vendor choices.

4.10 Management capability

N=13	Driver		Constraint	
	Outright	Prompted	Outright	Prompted
Management capability	-	-	5	13

All of the participants agreed that the prerequisite management capability in banking organisations may constrain them from pursuing operations processing outsourcing strategies.

They argued that outsourcing deals requires leadership ability to negotiate and contract a win-win deal. Implementing a BPO arrangement requires mature change management capability, e.g. to take care of resources transferring to the BPO firm. Managers need to deal with ambiguity, interpret business needs and off-load these to the service provider. Outsourcing further depends on good vendor management ability and managers who are able to contend with shared responsibilities, polarised (us and them) attitudes, and possibly misaligned business cultures. Managers in the retained organisation need to change from managing people to managing a service, which requires on-going monitoring and rapid remedial actions. It requires managers to deal with metrics, exceptions and being proactive. This change could easily be experienced as a loss of personal power. Managers often have an inability to trust and lack the ability to manage services where they don’t have direct authority and control. It thus requires a fundamental mind-shift in management’s role and practices

Concerns were raised about associated SLAs needing to be comprehensive and up to date. Managers are often ill equipped to setup, maintain and monitor adherence to SLAs. The change demands high inter-personal skills, networking ability and building partner relationships.

Participants pointed out that, where managers transfer to the BPO firm, they need to contend with a fundamental change in relationships, where their ex-employer and peers are now clients.

Participants had reservations based on executives generally having a 2-year window to implement changes and be successful. Thus, there is no incentive for them to “rock the boat” with transformational change (as associated with outsourcing) and jeopardise their own rewards. They would thus tend to take a short-term view, rather than long-term future proofing the business or “protecting and growing” the business. Leaders are often unsure about their own positions, preventing them from driving an outsourcing strategy, which is deemed to be a high stakes strategy. When deal-makers aren’t secure in their role, they might hesitate to commit. Top-level executives must try to make those responsible for outsourcing feel secure.

4.11 Environmental factors

N=13	Driver		Constraint	
	Outright	Prompted	Outright	Prompted
Environmental factors	2	NA	7	NA

Two participants pointed out that environmental factors could be drivers for outsourcing.

They referred to broadband connectivity becoming cheaper and more easily accessible, which should facilitate outsourcing. This is on the back of general improvements in telecoms infrastructure, as well as higher levels of access, stability and maturity. Reference was further made to new technology developments e.g. information storage capability, including cloud storage.

Several participants raised concerns related to banking regulations: Banking regulators are generally uneasy about outsourcing, but it was felt they shouldn't dictate on management strategies. Regulators may support outsourcing if there is opportunity to outsource a "broken process" to a party trusted by regulators. In fact, it was proposed that some regulatory requirements and legislative changes (e.g. FATCA) bring about the need to build capability that banks (smaller ones in particular) may struggle to set up, but which top-tier outsourced service providers would be comfortable to put in place.

Prior to implementation, regulators will need to review governance mechanisms and approve any outsourcing arrangements and banks will retain the responsibility to adhere to regulatory requirements (or face the consequences and penalties for non-adherence). Such adherence is considered to be harder in an outsourced environment. Participants raised concerns about BPO firms, being non-financial institutions and not being constrained by the same regulations, which may cause them to take an incautious stance on compliance. Regulatory constraints may hinder outsourcing at a practical level e.g. movement of client data. Although these are not generally seen as deal-breakers, the implementation of required controls and management processes may be a constraint.

Participants argued that the South African context, characterised by pressure for job creation and risk of negative publicity for causing job losses, limits the opportunity to outsource processing to offshore BPO vendors even though these may offer greater benefits. Also, the comparatively onerous requirements, e.g. in terms of due process, imposed by South African labour legislation, contributes to high costs of staff redundancy.

One research participant was uncertain if the first-world strategy of outsourcing is appropriate for the developing world, such as South Africa. Questions were raised about suitability of supporting infrastructure, skills and education, IP, maturity and scale of business.

Participants also had a perception of increased instances of failed outsourcing deals at first-tier global banks, and of the outsourcing landscape constantly changing, for example the reduced labour arbitrage opportunity when outsourcing work to India, due to recent wage inflation in the region.

5 INTERPRETATION OF RESULTS

In this section, the research outcomes were synthesised to construct overall outcomes and conclusions. This was accomplished by integrating the results obtained from the research participants with the findings from the literature review for each driving or constraining factor.

5.1 Drivers for outsourcing operations to external service providers

5.1.1 *Cost reduction*

Research findings supported the view that potential cost reduction is a primary driver for outsourcing.

The findings from the research were consistent with the literature reviewed in a number of areas, such as scale-related benefits attainable through using a specialist BPO firm's superior processing resources, skills and infrastructure, the opportunity to convert fixed costs into variable costs (particularly relevant for smaller and mid-tier banks), as well as the opportunity to conserve capital through avoiding or sharing requisite infrastructure investments. The research participants' views echoed literature review findings regarding the opportunity to provide greater certainty in financial planning and control, and elaborated on opportunities to transfer uncertainty and cost risk (including losses) to the BPO vendor (BIS, 2005; Chase et al., 2006; Halvey and Melby, 2007; Luvison and Bendixen, 2011; Norman and Zaidi, 2011). The opportunity for banks to convert an operations processing cost-base into a revenue generating asset, by entering into a partnership agreement, was raised by the participants.

The research findings supported the proposition that potential cost reduction was a driver for outsourcing of operations processing.

5.1.2 *Revenue growth*

Research findings indicated that outsourcing could contribute to revenue growth.

The views of the participants reflected the findings from the literature review as it pertains to the opportunity provided through outsourcing to increase the scope of services offered, rapidly and inexpensively accessing markets and increasing production capacity (Casale, 2005; Fung et al., 2008; Norman and Zaidi, 2011). The business reinvention theme identified in literature was reflected in research participants' comments about outsourcing permitting rapid introduction of a new operating model that could facilitate revenue growth.

The themes of mitigating demand risk and circumventing global restrictions, as identified in the research review (Conroy, 2008), weren't reflected in the research findings.

However, the participants identified a number of points related to revenue growth through outsourcing that weren't observed in the literature reviewed. These include increasing client bases through reciprocal arrangements with vendors, and the option to use BPO vendor resources (responsible for operations processing) to generate sales leads. Participants also argued that superior BPO vendor quality capabilities and diligence could be employed to achieve a product competitive advantage, and to avoid revenue leakage. Some participants also commented outsourcing could assist to re-focus management efforts on revenue generation, rather than being distracted by operations efficiency endeavours.

The research findings supported the proposition that revenue growth was a driver for outsourcing of operations processing.

5.1.3 *Organisational effectiveness*

The research findings were supportive of the view that banks may consider outsourcing for reasons related to increased organisational effectiveness.

All the points identified in the literature review (Chase et al., 2006; Fung et al., 2008) were echoed by the research participants. Literature and research findings were congruent on outsourcing facilitating improved customer service levels and greater adherence to SLAs, that outsourcing permitting management focus on areas of organisational strength and on outsourcing enabling rapid transformation to different business models. The drivers of increased organisational flexibility and responsiveness to change, as identified in the literature, were echoed by selected participants, who elaborated on typical BPO firm supremacy in areas of business process optimisation, capability maturity levels and infrastructure investment.

Whilst not reflected in the literature review, the findings from the research indicated that BPO firms have a greater commercial mind-set in the operations processing environment, which may bolster organisational effectiveness. Participants also identified certain constraints associated with organisational effectiveness in the context of this study, which weren't observed in the literature reviewed: these relate to the dynamism of the corporate and investment banking operations environment, the high level of client service expectations, as well as the associated infrastructure requirements.

The research findings were consistent with the proposition that increased organisational effectiveness was a driver for outsourcing of operations processing.,

5.1.4 *Operating efficiency*

The research findings showed that potential operating efficiency improvements is a driver of outsourcing.

Research findings were congruent with the literature review on aspects such as improvements in quality, productivity and turn-around times, generation of management reports and controls, essentially based on superior BPO firm operations processing skills, expertise and infrastructure (BIS, 2005; Casale, 2005; Chase et al., 2006; Halvey and Melby, 2007; Conroy, 2008; Fung et al., 2008; Norman and Zaidi, 2011).

The research findings didn't support the point about possible improvements in corporate image and credibility as a result of outsourcing, as was identified in the literature review (Chase et al., 2006).

The proposal in the research findings, that outsourcing could lead to greater flexibility and agility in accommodating business changes, wasn't identified in the literature review.

The research findings supported the proposition that increased operating efficiency was a driver for outsourcing of operations processing.

5.1.5 *Human resources management and development*

The research findings showed that banks may consider outsourcing for reasons related to human resource management and development.

Research findings were consistent with the literature reviewed (Berger and Gattorna, 2001; Chase et al., 2006) about outsourcing potentially providing enhanced career paths and increased motivation levels, along with an improved ability to attract and retain skilled resources.

Research participants identified several additional points to those found in the literature review, including reducing key person dependencies, as well as better opportunities for learning, development and cross-training. The larger scale BPO firms are deemed to have mature human resource management capabilities, and banks could benefit from such capabilities and evade some complex and time consuming processes, such as dealing with under-performing resources or employment terminations. Outsourcing may also present a vehicle for creating employment opportunities and improving BBBEE ratings.

The research findings supported the proposition that improved human resource management and development was a driver for outsourcing of operations processing.

5.1.6 *Strategic organisational control*

Findings from the research proposed that banks may consider outsourcing for reasons related to improved strategic organisational control, contrary to the findings from the literature review, which didn't highlight any associated drivers.

The views of research participants were that, subject to prerequisites of retained control over decision-making, the existence of a relatively stable environment, a properly designed end-to-end operating model, service management processes, governance structures and contracts, banks could improve strategic organisational control based on BPO firms' management reporting capabilities and technology solutions.

This finding from the research indicated the proposition on the drivers for outsourcing of operations processing was incomplete, as it suggested increased strategic organisational control may be an additional driver to those identified in the literature.

5.1.7 *Process control and operational risk*

Research findings showed banks may consider outsourcing for reasons related to improved process control and operational risk management, contrary to the findings from the literature review, which didn't highlight any associated drivers.,

The views of research participants were that, in the context of the high loss-potential inherent to corporate and investment banking operations, banks stand to gain from BPO firms' superior capabilities with regards to process control, adherence to standards, metrics-based management and management reporting. Some BPO firms are willing to carry operational risks and losses, and global players could enable global banks to roll-out process controls and risk management consistently.

This finding indicated that the research proposition on the drivers for outsourcing of operations processing was incomplete, as it suggested increased process control and operational risk management may be an additional driver to those identified in the literature.

5.1.8 *Ability to deal with competitive threats and opportunities*

The research findings showed banks may consider outsourcing for reasons related to improved ability to deal with competitive threats and opportunities.

Whilst the literature review didn't expose 'increased competitiveness' as a driver for outsourcing, this finding is consistent with views expressed in support of 'revenue growth' (Conroy, 2008). Research participants argued that superior BPO firm operations processing capabilities, investment in resources and infrastructure, could assist banks to achieve rapid new market entries. The theme of outsourcing re-focusing management efforts on core capabilities (that form the basis of competitive advantages), as per the research findings, is also supportive of this line of reasoning. Some research participants also suggested, if banks can remain focused on outcomes rather than execution, they could gain competitive advantages through outsourcing some core capabilities to BPO firms who possess superior execution capability.

This finding indicated the research proposition on the drivers for outsourcing of operations processing was incomplete, as it suggested increased ability to deal with competitive threats and opportunities may be an additional driver to those identified in the literature.

5.1.9 *Environmental factors*

Research findings proposed external environment factors represent drivers for banks to outsource operations processing to external service providers.

Regulatory compliance is a key external environmental factor in the banking industry. Selected research participants proposed that, despite regulators tending to be uneasy about outsourcing arrangements, they may support outsourcing of 'broken processes' to parties trusted by regulators, and some BPO firms may be better placed to invest in infrastructure and capabilities needed to adhere to regulatory requirements.

Other external environmental factors research participants identified as potential drivers for outsourcing included:

- The overall economic down-turn, with associated cost pressure in order to maintain cost-to-income ratios, despite declining transaction volumes that impact on processing scale.
- Increasing levels of competition, which demands greater change agility, focusing and ‘playing to strengths’, including developing innovative (and often specialised and complex) products and services. This point must also be considered against the backdrop of the Southern African region becoming a prospect for international competitors.
- Clients have lost a great degree of trust in the banking industry, and are more informed and demanding of services.
- Increasing political expectations to achieve higher levels of BBBEE and create employment opportunities.
- Ever improving information and communications technology enablement, including more accessible and affordable broadband connectivity and data storage.

This research finding indicated the proposition on the drivers for outsourcing of operations processing was incomplete, as it suggested several external environmental factors represent drivers for outsourcing, in addition to the drivers identified in the literature reviewed.

5.1.10 *Conclusion - research proposition 1*

The research findings supported proposition 1, confirming the business drivers for banks to outsource wholesale banking operations to external service providers included cost reductions, revenue growth, operating efficiency, increased organisational effectiveness and human resources development.

The research findings further indicated proposition 1 was incomplete, as improved strategic control, process control and operational risk management, environmental factors, as well as greater market competitiveness represented further drivers for banks to outsource wholesale banking operations to external service providers.

5.2 Constraints for outsourcing operations to external service providers

5.2.1 *Environmental factors*

The research findings proposed risks and constraints inherent to the external environment constrain banks from outsourcing operations processing to external service providers.

The findings from the research mirrored the literature review results pertaining to regulations and legislation, including tax constraints (Fung et al., 2008). Given that banks retain full responsibility for regulatory compliance and remain liable for any associated sanctions or penalties, it was proposed that adherence to regulations often adds complexity to outsourcing arrangements, considering such arrangements would be subject to the approval of regulators. Selected research participants believed it is generally more difficult for banks to adhere to regulatory requirements under an outsourcing model, and that BPO firms (as non-regulated entities) may be prone to taking a less cautious stance in this regard.

The constraining themes of currency, country and political risks as identified in the literature review (BIS, 2005) weren't reflected in the research findings.

Research findings indicated wage inflation in developing economies, which reduces labour arbitrage opportunities, was a constraint to outsourcing – consistent with the findings from the literature review (Fung et al., 2008).

The participants further provided some insight into constraints peculiar to the context of the research, i.e. the small scale and low maturity-levels of operations processing in the South African corporate and investment banking industry (comparative to developed economies, where outsourcing is prevalent), the lack of enabling skills, IP, resources and infrastructure, restrictive human resource management legislation, as well as political pressure against staff lay-offs.

The research findings supported the proposition certain external risks and constraints may hamper outsourcing of operations processing.

5.2.2 *Management capability*

The research findings suggested management capability is a constraining factor for outsourcing.

The research findings reflected the outcomes of the literature review in terms of the need for management to possess vendor management abilities (Chase et al., 2006; Fung et al., 2008; Luvison and Bendixen, 2011). This includes not only technical skills, such as designing and implementing SLAs or change management, but also inter-personal skills, such as the ability to build trust and relationships or to deal with different organisational cultures. It also calls for an empowering style of management, content with losing an element of control, whilst still retaining accountability.

The research findings identified constraining points pertaining to personal attributes of incumbent senior management, such as their inclination to pursue shorter-term rewards, rather than transformational changes and longer-term strategies, due to a lack of security in their own roles.

The research findings supported the proposition that management capability constrained outsourcing of operations processing.

5.2.3 *Human resource interests*

The research findings showed considerations related to human resources may constrain banks from outsourcing operations processing.

The research findings mirrored the literature review findings as it relates to risks and complexities associated with staff lay-offs or transfers, with associated impact on morale and service delivery (Chase et al., 2006).

The research findings elaborated on risks of losing key resources and inherent knowledge and skills, which may jeopardise the ability of banks to change service providers. Some research participants also had reservations about the career paths on offer at BPO firms being restricted to specialist roles, which may not meet the aspirations of some affected people.

The research findings supported the proposition that human resource interests constrained outsourcing of operations processing.

5.2.4 *Process control and operational risk*

Although the research findings reflected those from the literature review, there were few similarities in the underlying reasons, beyond possible contractual and reputational risks (BIS, 2005; Loader, 2006).

The constraints related to rolling-out integrated, complex, end-to-end inter-linked systems, found in the literature review (Halvey and Melby, 2007; Fung et al., 2008), weren't directly raised in the research findings.

The research results highlighted constraints associated with reliance on external parties for regular changes to be implemented (rather than having direct control), as well as commercial, legal, information security and reputational risks to banks as a consequence of control or service failures on the side of BPO firms.

The research findings supported the proposition that concerns about process control and operational risks constrained outsourcing of operations processing.

5.2.5 *Competitive threats*

Findings from the research suggested banks may refrain from outsourcing operations processing due to reduced ability to contend with competitive threats.

The research and literature review findings were congruent as they pertained to concerns about knowledge or technology leakage to competitors as a consequence of outsourcing (Contractor et al., 2009).

The concerns about BPO firms potentially becoming competitors, as identified in the literature review (Chase et al., 2006; Contractor et al., 2009; Luvison and Bendixen, 2011), weren't reflected in the research findings.

The research results elaborated about banks' levels of competitiveness being affected by the extent to which outsourcing covers core functions, and the ability of outsourced operations processing to cope with on-going change and ever increasing transactional complexity.

The research findings also proposed that, where banks have sufficient scale of internal processing, they do idnot stand to gain a competitive advantage through outsourcing.

The research findings supported the proposition that concerns about dealing with competitive threats may constrain the outsourcing of operations processing.

5.2.6 *Costs*

The findings from the literature review and research were consistent as it pertained to the risks of wage inflation, initial costs of implementation and on-going changes eroding intended cost savings (Conroy, 2008; Bardhan and Jaffee, 2011; Chowdhury, 2011; Tarakad, 2011b).

The costs incurred to monitor, coordinate and govern the outsourced processing, costs associated with learning and knowledge transfer, as well benefits of accumulated expertise and routines not accruing to the outsourcer, as identified in the literature review (Contractor et al., 2009; Luvison and Bendixen, 2011), weren't reflected in the research findings.

The research highlighted a number of findings not reflected in the literature review. These included the tax implications of outsourcing, as well as the risk of insufficient scale of processing in the South African market.

The research findings supported the proposition that concerns about cost escalations offsetting any savings may constrain the outsourcing of operations processing.

5.2.7 *Strategic control*

Findings from the research and literature review were consistent on the notion that outsourcing of core functions may lead to reduced strategic control of banks and the financial failure of a BPO firm would jeopardise strategic control (Chase et al., 2006; Contractor et al., 2009; Luvison and Bendixen, 2011).

The potential erosion of IP, learning, R&D investments, as identified in the literature review (Chase et al., 2006), were not reflected in the research findings.

However, the research results highlighted some strategic control constraints not identified during the literature review. These included the notion of having to compete with other clients of BPO firms for prioritisation of changes, as well as the view that certain corporate and investment banking processes ran more effectively due to the improved strategic control of a vertically integrated model.

Other arguments collated in the research proposed outsourcing may impede strategic control where a bank is in a state of strategic flux, where it is implemented on the back of a poorly defined operating model, where it leads to altered relationships with clients and third parties, the absence of cultural fit between partners, varying degrees of strategic importance of the arrangement to the parties or the strength of the strategic relationship between the parties.

The research findings supported the proposition that concerns about maintaining strategic control may constrain the outsourcing of operations processing.

5.2.8 *Organisational effectiveness*

The research findings indicated outsourcing of corporate and investment banking operations may lead to reduced organisational effectiveness, which was not identified in the literature review.

Research participants were cautious about the ability to retain appropriate levels of service support, flexibility and infrastructure maintenance, given the level of dynamism inherent in corporate and investment banking operations.

This research finding indicated the proposition on the constraints for outsourcing of operations processing was incomplete, as it suggested reduced organisational effectiveness could be a constraint, in addition to the constraints identified in the literature reviewed.

5.2.9 *Operating efficiency*

The research findings highlighted concerns about reduced organisational efficiency due to outsourcing, which was not identified in the literature review.

This concern related to the outsourcing vendor's responsiveness to changing requirements of corporate and investment banking operations, and the resulting negative impact on operating efficiency.

This research finding indicated that the proposition on the constraints for outsourcing of operations processing was incomplete, as it suggested reduced operating efficiency could be a constraint, in addition to the constraints identified in the literature reviewed.

5.2.10 *Conclusion – research proposition 2*

The research findings supported proposition 2, confirming the constraints associated with BPO, causing organisations to perform operations processing internally, included the external business environment, loss of strategic control, reduced responsiveness to competitive threats, cost escalations, insufficient management capability, HR interests, reduced process control and operational risk.

The research findings further indicated proposition 2 was incomplete, as reduced organisational effectiveness and operating efficiency represented further constraints causing organisations to perform operations processing internally.

5.3 Conclusion

The findings from the research, as it pertains to the drivers for outsourcing of operations processing in corporate and investment banking in South Africa, were consistent with the research proposal as it pertained to cost reductions, revenue growth, operating efficiency, organisational effectiveness and human resource development. However, the research findings proposed improved strategic control, improved process control and operational risk management, environmental factors, as well as increased competitiveness were additional drivers for outsourcing.

The findings from the research were consistent with the research proposal that risks and constraints embedded in the external environment, loss of strategic control, reduced ability to contend with competitive threats, cost escalations, insufficient management capability, HR interests, loss of process control and increased operational risk, constrained the outsourcing of operations processing in corporate and investment banking in South Africa. However, the research findings proposed reduced organisational effectiveness and operating efficiency represented further constraints causing organisations to perform operations processing internally.

6 CONCLUSION

6.1 Summary

The research revealed a number of concepts foundational to the drivers and constraints for outsourcing of corporate and investment banking operations, as summarised in Figure 2. Figure 2 shows the relative positioning of the driving and constraining factors emanating from the research results, the foundational concepts underlying these as well as the driving and constraining factors in the external environmental.

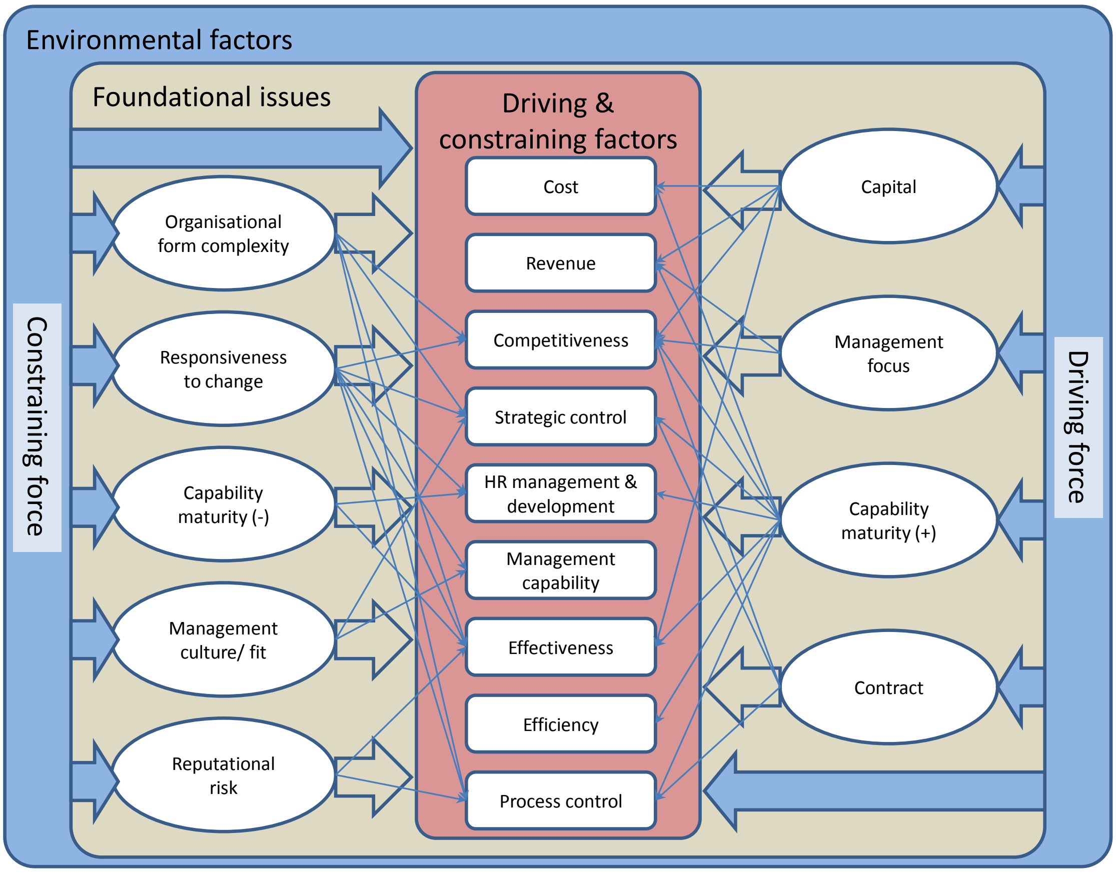


Figure 2: The relationship between environmental factors, foundational concepts and drivers and constraints for outsourcing

Outsourcing service providers often exhibit greater capability maturity in operational processing niche areas which appear to be foundational to most of the drivers for outsourcing. In the research findings, there was evidence of links between superior vendor capability maturity and all the drivers identified, except for 'environmental factors'. Inversely, selected constraints for outsourcing identified by research participants, such as reduced effectiveness and HR management and development, are linked to concerns about the capability maturity levels of prospective outsourcing vendors. It appears the drive towards outsourcing of operations processing will be stronger the more the capability maturity levels of prospective outsourcers are perceived to exceed those of banks.

The notion of outsourcing of operations processing removing a significant burden from incumbent management and leadership, permitting them to focus on endeavours that could bring about competitive advantages, also appears to be foundational to some driving factors, such as 'revenue increase' and 'increased competitiveness'.

Outsourcing normally establishes formal arrangements between banks and outsourcing vendors, with associated formality around planning, forecasting, legal documentation and service level agreements, which represents a further foundational element to the driving factors identified, such as improved 'process control', 'strategic control' and 'competitiveness'.

The opportunities for banks to benefit from capital investments of outsourcing service providers represent a further fundamental factor for drivers of outsourcing. This concept was linked to drivers such as 'cost reduction', 'revenue increase', 'competitiveness' and 'organisational effectiveness'.

Several constraints identified in the research trace to the fundamental question of the continued ability of outsourced operations processing providers to be responsive to changes required by their clients. Constraints linked to this foundational issue include 'HR management and development', 'management capability', 'organisational effectiveness', 'efficiency', 'process control', 'strategic control' and 'competiveness'.

A further foundational issue identified is the organisational form complexity that may result as a consequence of outsourcing. The research revealed links between this concern and constraints such as ‘organisational effectiveness’, ‘process control’, ‘strategic control’ and ‘competitiveness’. Accordingly, it appears the constraints for outsourcing will be bigger where operating model designs are immature and complex.

The research revealed corporate and investment banks are exceedingly averse to reputational risk, and acutely sensitive about the image projected to clients, regulators and the industry in general. This lies at the root of several constraints identified, including ‘process control’ (which incorporates management of operational risk) and ‘organisational effectiveness’.

The prevailing management culture and the cultural fit between banks and prospective outsourcers were identified as foundational issues at the root of the ‘management capability’ and ‘strategic control’ constraints identified in the research.

Lastly, the research indicated that South African corporate and investment banks are being affected (as much as other industries and regions with long outsourcing track records) by macro-level changes in the local, regional and global political, economic, social and technological spheres, and that these variables generally lie at the root of drivers such as ‘cost’, ‘competitiveness’ and ‘HR management and development’. However, the corporate and investment banking industry is intensely impacted by changes in the legal environment, and the intensified regulatory requirements and controls being imposed by governments and industry regulators generally have a constraining effect on outsourcing of operations processing.

In summary, the drivers identified for outsourcing will be more compelling where operations processing capability maturity levels of potential outsourcing service providers substantially exceed those of corporate and investment banks. The drivers will also be more compelling where the outsourcing arrangement will free-up incumbent senior management and leadership to focus on core responsibility areas. In addition, drivers for outsourcing will carry more weight where they bring about formal partnerships providing greater certainty and control, and where capital resources of outsourcing vendors could be leveraged by their clients.

Furthermore, it appears that the constraints for outsourcing will be elevated where arrangements will not permit implementation of rapid yet controlled changes, where operating model simplicity cannot be attained, where there isn't a good fit between the management cultures of partner firms, where concerns about reputational risk cannot be adequately addressed and where there are doubts about the capability maturity levels of outsourcing vendors in specialist processing areas.

6.2 Recommendations

6.2.1 *Overview*

The research was undertaken with the intention of assisting executives within the South African corporate and investment banking operations industry to make more informed decisions about, and minimise risks associated with, outsourcing as a management strategy. The research yielded a clear set of drivers and constraints executive management teams of corporate and investment banks may use as a framework for information gathering and analysis when making decisions about the optimal configuration of the operational processing activities of their organisations.

6.2.2 *Outsourcing of corporate and investment banking operations*

It is recommended outsourcing should only be pursued in the presence of strategy and operating model stability and simplicity, and where there is comfort in the parties' proficiency in change management and in the presence of real strategic partnership, with associated alignment in strategies, cultures and values. Decisions to outsource operations processing should be taken with a broad perspective in mind: findings from the research show outsourcing decisions ought to consider integrated, end-to-end processes (not just those deemed to form part of operations) and must be aligned with the overall operating model for the business and the industry.

Outsourcing deals must be considered in the context of being temporary arrangements, and it may be necessary to move outsourced services in-house at a point in the future. This specifically needs to be contemplated in terms of the on-going responsibility to the operations workforce, to provide them opportunities to learn, develop and grow professionally.

Executive management teams ought to seize outsourcing opportunities where they will lead to increased scale and where cost structures can be clearly defined and controlled, ideally permitting smaller banks to move from fixed to variable costing models. They should aim to transfer cost risks to outsourcing service providers and seek opportunities to leverage capital investments of outsourcing service providers, thus preserving in-house capital resources. At the same time care should be taken to anticipate cost escalations during implementation and business-as-usual phases, inclusive of any on-going change requirements. Management processes, service controls and legal agreements must permit banks to retain strategic control by retained control of decision-making, rather than execution. Any perceived need for in-house replication of elements of outsourced processing should serve as indicators of loss of strategic control and erosion of intended benefits from outsourcing.

Executive management teams should exploit the capabilities of outsourcing vendor partners to grow revenue, e.g. by stopping revenue leakage, deepening and broadening service offerings, rapidly accessing markets and creating sales leads. They ought to consider outsourcing as an opportunity to improve effectiveness, efficiency, process control and risk management, on the back of outsourcing vendor partners' advanced capability maturity levels. It should only be contemplated where it will be possible to retain the flexibility to absorb changes to outsourced processes, and given access to management resources equipped with the hard and soft skills needed to negotiate contracts and manage services on an on-going basis.

Reputational risk and adherence to regulatory requirements are significant constraints to outsourcing of operations processing, but do not represent deal-breakers. It is proposed these risks can be adequately mitigated through clear definition of responsibilities and diligent execution of management processes and controls.

6.2.3 *Outsourcing sales strategies*

From a sell-side perspective, vendors of outsourcing services of operations processing in the South African corporate and investment banking industry could use the drivers, constraints and underlying factors identified as a basis for tailoring their sales strategy in a manner that addresses the concerns of prospective buyers on the one hand, and fully emphasizes the potential gains and benefits on the other.

6.2.4 *Strategic sourcing and project implementation*

The research focused on the basis for strategic decisions-making and assumes proficient strategic sourcing and implementation of an outsourcing venture. Aspects such as prerequisite engagement principles, integration of processes and dealing with resistance to change, fall outside the scope of the research. However, strategic sourcing and implementation processes, pertaining to outsourcing of operations processing in the South African corporate and investment banking industry, should benefit from an understanding of drivers and constraints in the context of a given organisation. In this manner implementation projects could maximise positive outcomes and benefits associated with drivers, and minimise negative outcomes associated with constraints.

6.2.5 *Outsourcing of core capabilities*

It is recommended banks do not veer away from outsourcing core capabilities. Research findings indicate, where a bank has an opportunity to benefit from the advanced capabilities of an external party, and assuming it is possible to retain strategic control, outsourcing of core capabilities presents greater leverage opportunity, compared to outsourcing of non-core capabilities.

6.3 Suggestions for further research

This research project analysed the drivers and constraints for business process outsourcing in the South African corporate and investment banking operations industry. A number of ideas and suggestions that could be investigated arose from this study and are listed below:

- The determinants of success for managing outsourced operations processing in the South African corporate and investment banking industry.
- The criteria for selecting an outsourcing service provider for outsourcing of operations processing in the South African corporate and investment banking industry.
- The attributes of management teams needed for successful implementation of outsourcing of operations processing in the South African corporate and investment banking industry.
- The success factors for change management when implementing operations outsourcing in the South African corporate and investment banking industry.
- Compare the drivers and constraints for outsourcing of operations processing in the South African corporate and investment banking industry, as seen from the perspectives of banking executive leadership, BPO vendors and consultants.

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APPENDIX A – VARIABLES INFLUENCING OUTSOURCING SERVICE EXPORT DECISIONS

Table 2: Variables influencing outsourcing service export decisions

Variables influencing outsourcing service export decisions	**South Africa's capabilities**
1. Geographic distance between the outsourcer and service provider, as it has an influence on management costs (e.g. travel costs) and alignment of time-zones (Norman and Zaidi, 2011).	Time-zone aligned with continental Europe and the UK, difference of two hours at most during periods of day-light saving.
2. The outsourcer's home language being a local language (Norman and Zaidi, 2011).	South Africa has good English language skills, and substantial cultural alignment to Western countries (Mukherji, 2010). English language skills: one of 11 official languages, primary language of business, mandatory in schools. Other European language skills are also available, including German, Italian and Portuguese. High degree of alignment with European and North American business cultures.

Variables influencing outsourcing service export decisions	South Africa's capabilities
3. Infrastructure, including technological and aspects such as level of internet access (Norman and Zaidi, 2011).	South Africa has a superior infrastructural ability to deliver high quality services compared to other African countries. The recent commissioning of new undersea communication cables and availability of redundant bandwidth is bound to reduce telecommunications costs (Cairns, 2010). Telecommunication costs are high, around 5 – 7 times higher compared to India and the Philippines. However, telecoms costs have reduced considerably over the past 3-4 years. The advent of new cables (e.g., SEACOM) is expected to further reduce telecom costs and strengthen cost competitiveness of several countries in the region (Karthik and Nikhil Rajpal, 2010). Economic development: Telecommunications, power and transport infrastructures are well developed relative to other outsourcing destinations. Infrastructure: property is relatively inexpensive and well equipped compared to developed world equivalents.

Variables influencing outsourcing service export decisions	South Africa's capabilities
	Geographic location: dry climate with moderate temperatures, few concerns relating to seismic events (earthquakes, volcanos). Security: whilst external security is not a risk, businesses face perennial internal security issues. Some areas of economic infrastructure are inadequate (e.g. telecommunications) or in a state of neglect (e.g. roads, ports, power, water).
4. Labour and other input costs (Norman and Zaidi, 2011).	Wages are much lower than in UK and Europe, labour is plentiful.
5. Regional or national comparative advantages, such as engineering and technical services capabilities in India (Click and Duening, 2005) (Karthik and Rajpal, 2010).	
6. Talent availability (Karthik and Rajpal, 2010).	South Africa's skills base has limited the country's ability to benefit from growth in areas such as finance and

Variables influencing outsourcing service export decisions	**South Africa's capabilities**
	accounting, human resources and other knowledge process outsourcing (Cairns, 2010). Education and training: very divergent, ranging from world-class education in areas of Engineering, Information Technology, Finance & Accounting, Business and Medical Science, to segments with high adult illiteracy. Education and training: Low level of adult literacy among certain population groups; labour is largely unskilled, leading to high levels of structural employment.
7. Operating risks (Karthik and Rajpal, 2010).	Foreign investors' perception of Africa as a high-risk business environment is deemed to be a combination of real issues and perceptions. Real risks can arguably be contained by making the necessary investments, e.g. in the area of security services (Karthik and Rajpal, 2010).
8. Local parties' understanding of the local or regional culture, distribution processes and regulatory practices (Contractor et	

Variables influencing outsourcing service export decisions	South Africa's capabilities
al., 2009).	
9. Government incentives (Cairns, 2010).	Whilst government is supportive of the practice, South Africa lacks a unified national BPO marketing strategy required to attract international clients (Cairns, 2010). Ease of doing business: compares favourably with regards to business entry, enforceability of contracts, political and economic stability, financial services sector, corruption, tax systems. Inefficient service delivery from local governments, town councils and state departments.

APPENDIX B – FACTORS THAT ENABLE OUTSOURCING

Table 3: Factors that enable outsourcing

Enabling factor	**Externalise**	**Offshore**
1. Globalisation and intensified competition in the market place (Contractor et al., 2009).	Y	Y
2. Free markets and liberalisation of trade and investments (Contractor et al., 2009).		Y
3. The advent of a well-established and reliable global communication and information infrastructure, characterised by: a. Broadband communication, b. Abundant data storage, c. Collaborative software allows distributed teams to work on tasks simultaneously or according to a shift system, d. Analytic software, such as expert and decision support systems, which reduce the need for decision-making based on human logic, e. Internet security, which makes it possible to send information over the Internet, without fear of data loss or leakage. This is a combination of technological advances, as well as advances in national legislation and regulation, global compliance benchmarks and standards (e.g. the ISO17799 standards for information security management), f. The reduction in IT costs, as a consequence of large investments in communication bandwidth, as well as technology advances that permit cheaper and easier communication over longer distances, and g. The accelerating rate of technological change, which compels organisations to greater externalisation in order to keep with change and remain competitive.	Y	Y

Enabling factor	Externalise	Offshore
4. National differences in costs, such as: a. Wages and input costs, b. Premises, and c. Services, e.g. energy and local government.		Y
5. Growing education and skills in developing economies, as well as a shortage of skilled technical and managerial resources in traditional Western business centres.		Y
6. Greater codification of corporate knowledge, which resulted in formerly tacit knowledge being published in specifications, manuals and expert systems. It permits increased quality monitoring and control and reduces associated costs. Codification permits re-use of knowledge and thus reduces the costs of repeated exercises.	Y	Y
7. Modularisation of functions, with objective criteria for inputs and outputs and the interfaces between functions, makes it easier for geographically distributed teams to interact and operate effectively.	Y	Y
8. Reductions in costs of transportation.		Y
9. A revolution in management strategy, in which managers seek to share control with various service providers for the sake of increased efficiency (Contractor et al., 2009).	Y	Y

APPENDIX C – KEY RISKS OF OUTSOURCING TO BANKS

Table 4: Key risks of outsourcing to banks (BIS, 2005)

Type of risk	**Description**
Strategic	Risks associated with service providers conducting activities that are inconsistent with the bank's strategic goals, as well as insufficient oversight of the service provider.
Reputation	Risks where conduct from the service provider impacts the reputation of the bank, for example relating to service levels, or adherence to regulatory standards or ethical practices.
Compliance	Risk of non-compliance with legislation, for example pertaining to consumer, prudential or data privacy laws, possibly due to inadequate compliance systems or controls.
Operational	Risks associated with processing error, fraud, technology failure and financial capacity to meet obligations.
Exit strategy	Risks due to over-reliance on a service provider, preventing the movement of business processing to another service provider or in-house, due to prohibitive contractual obligations or skill shortages.
Counterparty	Risks relating to the quality of receivables, due to inadequate credit assessments and controls.
Country	Risks associated with the political, social and legal circumstances of the service providers' country of domicile.

Type of risk	**Description**
Contractual	Risks relating to the ability to enforce contracts.
Access	Risks associated with providing timely and accurate information to regulators, due to banks being constrained from accessing such information.
Concentration and systemic	Risks due to significant exposure to a service provider at an industry level.

APPENDIX D - COVERING LETTER TO RESPONDENTS

Dear Sir/ Madam

I am in the process of conducting academic research related to the business drivers and constraints associated with business process outsourcing in the corporate and investment banking operations in South Africa. This research is being conducted as part of an MBA degree being completed at Wits Business School.

The study endeavours to fill a gap in the knowledge in this area and the research outcomes will presumably assist executives within the South African corporate and investment banking operations industry to make more informed decisions about, and minimise risks associated with, outsourcing as a management strategy.

I am conducting a series of interviews with senior stakeholders in the industry; including management representatives from banks, office bearers at industry forums, service providers and consultants, and would like to invite you to participate in such an interview. The research protocol requires that input from various respondents be kept strictly confidential, and respondents may choose to remain anonymous. All research participants will receive copies of the final research report.

The interview will be conducted by myself and will take roughly 45 minutes. I hope shortly to contact your office to make arrangements for a convenient date and time to meet.

Please feel free to contact me for any further information you may require in this regard.

Your participation and assistance will be highly appreciated.

Yours faithfully,

Sarel van der Westhuizen

APPENDIX E – QUESTIONS GUIDE FOR SEMI-STRUCTURED INTERVIEWS

Introductory/ context setting questions:

1. What is your view of outsourcing functions and activities deemed to be core organisational capabilities?
2. Can you provide examples in your own organisation or in the South African industry, of corporate and investment banking functions or services that are currently being/ due to be outsourced to an external service provider?

Questions associated with the research propositions:

3. What are the business drivers that may lead corporate and investment banks to outsource operations processing to external service providers in South Africa?
4. What are the business constraints and risks that may lead corporate and investment banks to prefer to conduct operations processing internally?
5. What effect could outsourcing of corporate and investment banking operations functions and activities have on:
    a. Costs of operations?
    b. Revenue of corporate and investment banks?
    c. The implementation of operating improvements?
    d. Organisational effectiveness (e.g. adherence to defined service levels)?
    e. Human resources development and other people interests?
    f. Strategic organisational control?
    g. Process control and operational risks?
    h. Dealing with competitive threats?
6. What are the management capabilities needed to ensure successful outsourcing of operations processing?
7. What are the recent changes or circumstance (if any) in the business environment that either drive corporate and investment banks to outsource operations processing functions and activities or constrain them from doing it?

* * *