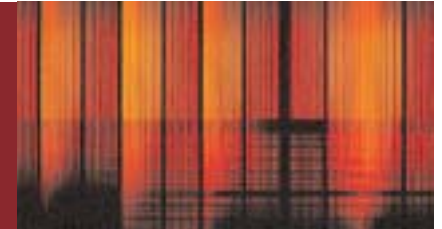


## Executive summary



Welcome to the tenth report in our global financial services briefing programme, entitled **From aspiration to achievement: Improving performance in the financial services industry.**

### PricewaterhouseCoopers Global Financial Services Briefing Programme

This briefing, written in association with the Economist Intelligence Unit, addresses the key issues that financial institutions are facing with regard to improving performance across a number of key business areas.

The research effort for this briefing comprised two global initiatives:

- The Economist Intelligence Unit held over 14 one-on-one interviews with senior executives at financial institutions in Asia, Europe and North America.
- The Economist Intelligence Unit and PricewaterhouseCoopers conducted a special online survey of senior executives in financial institutions on the subject of improving performance. Executives from 227 institutions in Asia, Europe and North America participated in the survey, which was conducted during October and November 2004.

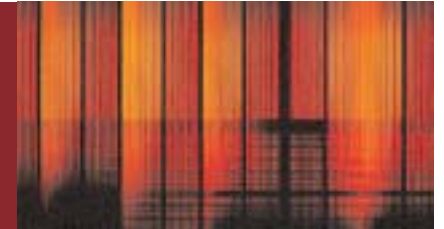
The interviews and survey findings were further supplemented by significant desk research.

I am confident that you will find this briefing thought-provoking and insightful. Soft copies of this, along with our previous briefings on **Wealth Management, Economic Capital, Risk Management '02** (and the follow-up risk management survey), **The Trust Challenge, IFRS, Compliance, Restructuring, Governance and Risk Management '04** are available from our web site [www.pwc.com/financialservices](http://www.pwc.com/financialservices)

If you would like to discuss any of the issues addressed in this briefing in more detail in relation to your organisation please speak to your usual contact at PricewaterhouseCoopers. We would also appreciate your feedback on this briefing as it helps us to ensure that we are addressing the issues that you are focusing on.

**Jeremy Scott**  
Chairman, Global Financial Services Leadership Team

## Executive summary continued



Most financial institutions would agree that better performance is a critical objective. But translating aspiration into achievement has proved an elusive goal.

Performance improvement can be defined as the successful implementation of change to achieve desired results. It requires a common view of the desired outcome and its benefits. It also needs clear accountability for the ownership and execution of tasks designed to change organisational behaviour and the use of resources such as people, processes and technology. Ultimately, success must be measured by the delivery of the planned benefits, not the elegance of the execution of the project.

Over the years we have seen organisations adopting a range of approaches to improve performance. Enterprise Resource Planning and Straight Through Processing emphasised cost savings and efficiency. Customer Relationship Management applications concentrated on increasing the value of institutions' individual customers. Measurement programmes, such as the balanced scorecard and EVA (economic value added), zeroed in on drivers of corporate value. Most recently, outsourcing has held out the promise of cost reduction and a focus on core competencies as the drivers of improved performance.

Yet responses to a survey of 227 industry executives carried out especially for this briefing, written by the Economist Intelligence Unit for PricewaterhouseCoopers, show low levels of satisfaction with performance across a string of business areas. Some institutions perform better than others, of course, but if so many executives remain generally disappointed, even after this diverse and expensive string of initiatives, what are they doing wrong and how can they ever deliver improved performance?

It appears that many financial institutions are not organised to deliver successful change, and that several are trying to do too many things at the same time.

Not surprisingly, the survey showed that revenue generation was management's top priority for delivering performance improvement, with over half the respondents citing customer service as the single most important factor in building competitive advantage. However, customer service can be easily replicated and is itself dependent on the rest of the organisation to deliver the infrastructure to sustain it. Brand is also a critical factor, one which is much more

difficult to replicate but requires constant management focus to build and maintain. Success in both these areas will require a commitment to organisational change.

The need to establish optimally-efficient operations, delivered in the most cost effective way, is essential to enable the organisation to focus on its key goals without getting distracted by the need to constantly fix internal problems. This becomes even more critical in the light of continued upward pressures on costs due to factors such as regulation, and the continued downward pressure on revenue due to increased competition. To respond to these major challenges, companies will need to focus their attempts to improve performance in three key areas:

**Goal-setting.** Management needs to retain a clear focus on strategic goals to ensure success in attempts to improve performance. There remains a high degree of correlation between the factors that drive competitive advantage and those that drive performance improvement initiatives in organisations. The key factors of sales, branding and marketing (53% of respondents), providing customer service (49% of respondents) and

## Executive summary continued



the quality/performance of actual products (39% of respondents) were ranked significantly higher than all other issues when seeking to understand the sources of competitive advantage. For most organisations, the fact that there remains a high level of dissatisfaction with performance improvement initiatives is due to a failure in *delivering* the vision, rather than the absence of a strong vision in the first place.

**Assessment.** Performance cannot be optimised if it is not measured. The survey results show that where there is a paucity of data, levels of satisfaction with performance tend to be lower. The flow of accurate, timely information to management enables financial institutions to identify, assess and rectify performance shortfalls. What's more, the right things need to be measured. 'Too many organisations quantify performance improvement by focusing on financial measures,' says Etienne Boris, European Financial Services Leader for PricewaterhouseCoopers. 'But a financially-driven approach to performance improvement can lead to a short-term focus on cost savings at the expense of long-term improvements in quality.' To judge by their

attitude to outsourcing, the survey respondents are keenly aware of this potential trade-off, pointing to a less developed understanding of the business and lower quality of service as two principal risks of moving processes out of house.

**Implementation.** Performance improvement, whether in-house or outsourced, depends on active leadership. The engagement of senior management is regarded by survey respondents as the single most important ingredient in implementing successful performance initiatives. 'It's about more than communicating change,' says David Cross, country operating officer for Greater China at ABN AMRO in Hong Kong. 'We have to facilitate the process, helping our staff get acclimatised to dealing with change. That's our biggest task.'

The commitment of senior managers is particularly important when the focus of performance improvement is on front-office functions such as sales, marketing and customer service. 'The emphasis on performance initiatives, and the skills associated with them, have traditionally focused on operational areas in the back

office,' says Andrew Gray, Partner at PricewaterhouseCoopers in London. 'To maximise the effect of changes, the organisation must look to improve the entire business process including client-facing activities. To be effective, senior management must actively steer the process.'

**'Improving performance is a key priority for the financial services industry, given competitive pressures, customer demands and challenging market conditions,' says Jeremy Scott, Chairman of the Global Financial Services Leadership Team at PricewaterhouseCoopers.**

The fact that so many institutions remain dissatisfied with their performance underscores the challenges of changing processes, cultures and organisations. Meeting those challenges requires a rigorous definition of objectives, a transparent assessment of current performance problems, a balanced evaluation of the appropriate solution and committed leadership from above.

### Ten pillars of performance improvement wisdom

- 1. Don't think in silos.** Processes and functions overlap and affect each other. Improvements in one depend on, or are manifested in, improvements in others. For example in insurance companies, management frequently does not have a complete view of its most profitable products (or for that matter, its least profitable ones). The ability of different parts of the business to implement changes can also be impacted by events elsewhere in the business. For example, it is often the case that effectiveness in the operational department is in part dependent on the quality of data received from the sales teams. Yet it is rare to see sales teams rewarded for the accuracy of data.
- 2. Management must make decisions and provide an effective governance structure.** A third of respondents are unhappy with the speed and quality of management decision-making, an area where performance is also rarely measured. Some institutions already use

Continued overleaf

## Executive summary continued



### Ten pillars of performance improvement wisdom continued

confidential in-house surveys to benchmark the management of specific functions such as finance, but effective and transparent reporting is also needed to establish clear links between management decisions and actual outcomes.

- 3. Reward and recognise improved performance.** Respondents and interviewees acknowledge the importance of performance-related compensation – alignment of incentives and performance is one of the top three ingredients of successful performance improvement, in the eyes of survey respondents. This mantra should also extend to agreements with third-party service providers. Work with a firm that compensates its own people according to how well they meet their performance targets in dealing with your organisation, while still adhering to the highest standards of governance.
- 4. Gauge success by non-financial performance gains as well as financial ones.** For example, cost has traditionally determined the choice between keeping processes in-house or moving them to a third-party provider or shared services platform. But a more balanced assessment of the benefits and risks is needed if long-term improvement goals are to be met. Headline savings may be short-lived if the provider fails to live up to expectations in the longer-term. Third parties will need to prove scale and competence in all aspects of performance in order to win new business.
- 5. Aim for a continuous culture of performance improvement among staff.** Individual initiatives are all very well but rising competitive pressures and customer demands mean that the bar on standards of performance is perpetually being reset. The concept of lasting improvement needs to be firmly embedded within the organisation. More than two in five respondents identify an organisational culture of constant performance improvement as a major driver of initiatives at their firms. Achieving cultural change is notoriously difficult, of course. Senior managers are critical in this regard as role models, facilitators and enforcers of change. So too are human resources activities such as educational, training and communications programmes.
- 6. Plan holistically.** Performance improvement rests on a number of factors, all interconnected. Technology implementations are most effective when accompanied by the re-engineering of related processes and supported by training and education. A centralised planning approach, drawing on the efforts of a number of different functions and pulling all the levers that lead to successful change within organisations, is the best way to maximise improvement potential.
- 7. Prioritise rationally.** Performance improvement involves change and change can be painful, prolonged and politically charged. Without a sense of priority, there is a danger that the organisation will take on too much and become 'change fatigued'. The survey respondents have a number of ways to prioritise projects, from increasing revenue to improving customer service to meeting compliance requirements. What's important is to have a system for ranking projects that is consistent with the organisation's overall strategy and considers the relative difficulty of implementation and scale of expected benefits.
- 8. Use specialist resources.** More than two in five survey respondents have specialist teams tasked with identifying and solving inefficiencies in the areas of compliance, risk management and IT management.
- 9. Think through the mind of the customer.** Our survey group is agreed that the primary sources of competitive advantage for financial institutions are sales, branding and marketing, and customer service. Since contact with the customer is so critical, use this perspective to identify the areas of performance improvement that would make the greatest difference to the customer experience.
- 10. Clarify roles, responsibilities and benefits.** Who are the key stakeholders in driving projects through to completion? Who monitors and reports on performance levels? What are the criteria for bringing performance failures or issues to the attention of senior management? What are the expected benefits of improvement and how can they be measured and managed? Clear answers to these questions will enable problems to be identified quickly and solutions to be implemented more efficiently.

## Introduction



To a large degree, performance improvement in financial services institutions still depends on external factors – movements in the capital markets or changes in the economic cycle. Declining interest rates favour commercial banks by lowering their funding costs and widening interest margins. Asset managers benefit from rising stock or bond prices as their percentage-based fees increase with assets under management.

But the pressure on financial services institutions to improve performance and to deliver low cost reliable products has reached new and exacting heights. Rising customer expectations, fierce competition at the global and local level, the need to invest heavily in technology and the escalating cost of regulatory compliance are all part of a tightening squeeze on profitability. With the economic cycle expected to moderate in the short term, relying on the vagaries of the capital markets is not a tenable strategy. Institutions must also look inwards at their processes, organisation and culture, where properly executed initiatives can bring performance enhancements quite unrelated to market swings.

Financial services institutions are keenly aware of the need to do better. A survey of 227 senior industry executives carried out for this briefing reveals that satisfaction levels with the performance of specific business areas are generally low. On a scale of 1 (extremely satisfied) to 5 (extremely dissatisfied), almost every function has an

How satisfied are you with the performance of the following areas of your business?  
(Average respondent score; 1 = extremely satisfied and 5 = extremely dissatisfied)

Compliance	2.33
Risk management	2.48
Finance and accounting	2.50
Quality/performance of actual products and services	2.54
Transactions and processing	2.60
Customer service	2.70
Procurement	2.87
Sales and marketing	2.86
Product development	2.89
Speed and quality of management decision-making	2.89
IT management	2.97
Human resources	3.00

Source: PricewaterhouseCoopers/Economist Intelligence Unit survey, October-November 2004

average score of worse than 2.5. Dissatisfaction is highest in the areas of information technology management and human resources. But if the need for performance improvement is recognised, the path from aspiration to achievement is less clear.



## Defining the goals



The first challenge facing institutions as they seek to improve their performance is to decide what to improve. Three factors should feed into this decision – the needs of the market, the strategy of the organisation and the current state of performance levels. Ideally, of course, all three should be in close alignment. In practice, they often are not.

Most institutions rightly regard their interaction with customers as a key source of competitive advantage. In our survey, 53% of respondents picked quality of customer service as one of their top three critical advantages, compared with 49% who select sales, branding and marketing and 38% who opt for quality and performance of actual products and services.

At Equity Offices Property Trust, the largest publicly held building owner and manager in

the US, CFO Marsha Williams says the company’s overriding goal has been to improve customer service, both internally and externally. ‘Internally, financial systems and IT provide the infrastructure that impacts the efficiency and effectiveness of every Equity Office company function. Externally, our team can contribute to lowering the cost of occupancy for our customers. If we keep our costs down, we can help keep our customers’ costs down over time,’ she says.

In the investment management industry, which is struggling with tepid markets in addition to ongoing regulatory probes, individual investors are demanding not just higher returns but quicker and better customer service, both in the form of account access and investment advice. This is compounded by the ease and frequency with which customers can switch from one provider to another. ‘In my view, fund performance is not the overriding factor in investors’ minds when they are selecting a fund manager,’ says Thomas Barrett, a partner at PricewaterhouseCoopers in Boston. ‘Service, product offerings and minimising charges are equally important. If a manager can preserve, even enhance, an investor’s capital and provide quality customer service that individual will not turn around and go to a low-cost provider.’

Despite its importance, however, very few financial institutions count themselves extremely satisfied with their performance in areas of customer service, sales and marketing. What’s more, although rising customer expectations are one of the main factors that drive performance improvement initiatives, many more respondents (63%) prioritise these initiatives on the basis of opportunities for increased revenue than do so on the basis of impact on customer service (34%).

Which areas of your business are the key sources of competitive advantage for your organisation in the marketplace? Please choose up to three areas.

Customer service	53%
Sales, branding and marketing	49%
Quality/performance of actual products and services	39%
Product development	29%
Risk management	26%
Transactions and processing	26%
Speed and quality of management decision-making	15%
Human resources	13%
Finance and accounting	11%
IT management	11%
Compliance	9%
Procurement	1%
Other	4%

Source: PricewaterhouseCoopers/Economist Intelligence Unit survey, October-November 2004

## Defining the goals continued



### Case study: Zurich sharpens up its act

Zurich Financial Services (Zurich) is no stranger to the imperative of performance improvement. Just over two years ago it announced a programme of strategic initiatives to sharpen its business focus, improve operational efficiency, strengthen its balance sheet and enhance its capital base. This followed a calamitous year in 2001 when Zurich recorded a loss and cut its dividend, partly as a direct result of the September 11 terrorist attacks but also because of lower earnings from life insurance and asset management.

A focus on core activities and markets was the first step towards restoring profitability. Zurich now concentrates on (life and general) insurance, having sold its asset management arm, Zurich Scudder Investments, to Deutsche Bank in April 2002, and Threadneedle to American Express in October 2003. It has two clearly-defined markets: North America and Europe.

The effort went beyond a typical revenue-enhancing, cost-saving programme, although this was clearly a crucial element in the early days. It had to become part of the group's long-term time horizon so that today, for example, Zurich has operational imperatives that pay dividends as far out as 2007.

John Lynch, executive vice president, market management and a board director of Farmers Group, Inc in the US, was put in charge of the programme. 'Every element of the operational improvement plan was identified, quantified, monetised and then placed in a rigorous database linked to a programme management office in each business unit,' he recalls.

To begin, an exhaustive cost-cutting campaign through process improvement was initiated. But the real effort was devoted to making underwriting profitable or, as Mr Lynch puts it, learning the discipline of being an underwriting company. 'We were frequently pricing a product when we did not know the ultimate cost,' he says.

'We had to do a better job of tending to our knitting in the underwriting area.'

Zurich assessed its operating performance relative to a target business operating return on equity after tax of 12% over the medium term, benchmarking against its competitors and by drawing on the experience of its most efficient business units. By the end of 2003 it had achieved a 9.3% return for the year as a whole and in the first nine months of 2004 return on equity increased to 12.5%.

The transformation effort is still huge. 'We have around 62,000 people in this organisation so, although we have strong alignment around the programme at the senior management level, our goals and methodology must be communicated constantly to individual employees,' remarks Mr Lynch.

Reflecting performance improvement in individual compensation is also a challenge. While North American institutions tend to have a culture that is more accepting of performance-based rewards, this approach is still not the norm in Europe.

If performance improvement priorities are poorly aligned with organisational strategy, who is responsible for putting matters right? Leaders in the performance mission agree that the impetus for improvement needs to come right from the top of the institution, where senior managers have both the clout to push through change and the information to judge the impact of initiatives across the organisation. When questioned about the critical factors behind successful performance improvement initiatives, 65% of survey respondents cited active involvement by senior management and another 34% chose active involvement on the part of business unit managers.

Ms Williams, the CFO at Equity Offices, is leading a major effort, involving departments across the company, to evaluate priorities for IT spending taking into account not only the cost of investment but potential increases in revenue and/or expense savings. This effort will focus the IT department on the most high-impact programmes and will align departments, which often compete for IT time, with the priorities that provide the most value for the company as a whole.

## Defining the goals continued



**What are the critical factors behind successful performance improvement initiatives? Please choose the top three.**

Active involvement on part of senior management	65%
Clear and measurable project milestones	44%
Alignment of incentives with improved performance	35%
Active involvement on part of business unit managers	34%
Finding the right people	32%
Availability of high-quality internal management data	20%
Availability of recognised external benchmarking data	14%
Centralised control of the initiative	10%
Track record of performance improvement success	10%
Access to external expertise and advice	10%
Specialised project teams	7%
Utilising the right technology	7%
Competitive processes to find the right service provider	2%
Other	1%

Source: PricewaterhouseCoopers/Economist Intelligence Unit survey, October-November 2004

‘Our CEO, Richard Kincaid, has fully supported the new initiatives within the finance and IT teams,’ she notes. ‘Equally important is the buy-in of senior leadership across the company. We make a clear case for our programmes early in the process, communicating the time, investment and results we anticipate.’

Since the majority of the finance team’s customers are internal, Ms Williams relies heavily on the company’s annual employee survey to gauge the service levels her finance and IT teams are achieving. The surveys ask employees to rank their satisfaction with each department at Equity Office.

At Zurich, the Group Executive Committee sets performance targets for the various

businesses. The chief operating officer and the two heads of life and general insurance are then responsible for driving performance at the operational level.

Accurate and timely data is also critically important to the process of defining performance goals – institutions must be able to assess and measure their achievements in different parts of the business, and also be able to set clear and measurable performance targets by which the success of individual initiatives can be gauged. 34% of respondents consider the availability of data, both internal and external, to be a key ingredient of success, and 44% regard clear and measurable project milestones as central determinants of successful initiatives.

Despite the importance of data, there are large holes in the measurements available to respondents. More than a third of respondents have no formal measures to evaluate performance in areas such as human resources, procurement and product development, and IT management scarcely scores better. Tellingly, over half of the survey respondents do not measure the speed and quality of their own management decision-

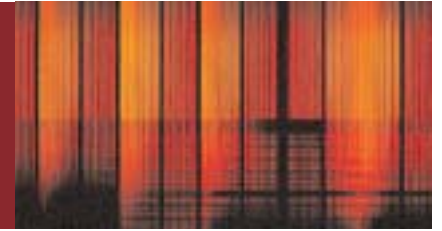
making. Each of these undermeasured areas is also the focus of greater dissatisfaction over performance.

Looking at four areas in particular – finance, compliance, risk management and IT management – it appears that while the majority have periodic reviews of performance in these areas, very few have specific programmes such as Six Sigma in place to identify and solve performance weaknesses. Fewer than half have corporate performance measurement systems in place to provide ongoing data, with the sole exception (just) of finance.

The leading institutions practise corporate performance measurement, using specific tools that allow management to monitor performance in real time against pre-determined indicators. Senior executives get a ‘dash-board’ overview of the indicators that allows them to drill down into individual areas at will. Others rely on regular audits or benchmarking of either internal or external indicators. But highly developed measurement systems appear to be the exception rather than the rule in the industry.



## Defining the goals continued



### Compliance: Conformity or outperformance?

Few would argue with the view that regulatory initiatives and compliance pressures are major drivers of change in the financial services industry. Why then does our survey of executives in financial services institutions show that expanding regulatory requirements are not a major factor behind performance improvement initiatives? Only 19% cited regulatory issues as a main driver, well behind increased competitive pressures, customer demands and dwindling profits.

One reason may be that meeting increased regulatory requirements is perceived to hinder performance, not improve it. 'Performance improvement is not just about maximising the upside and sharpening competitive advantage,' says Felix Sutter, a partner at PricewaterhouseCoopers in Zurich. 'It is also about minimising the

downside by improving compliance and risk management processes.'

The extent of that downside can be huge, as proven in a series of compliance incidents at financial institutions. For that reason alone, respondents' relative levels of satisfaction with compliance and risk management performance are no cause for complacency.

Indeed, there's clearly room to do better. Our survey shows that two in five respondents do not have periodic reviews of compliance performance, only 38% have systems in place that provide ongoing data on compliance performance and only 29% assess their performance on an enterprise-wide basis.

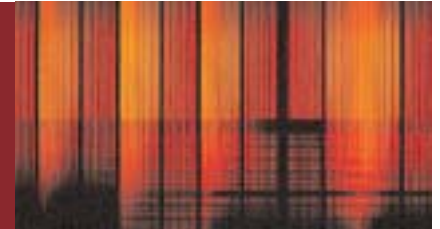
Looking forward, executives agree that more rigorous surveillance and testing of existing processes is important. At one bank the 2005 compliance plan is being drawn up based on a ranking of inherent

risks to the institution and an analysis of the quality controls needed to meet those risks.

'We should consider emulating some other institutions where the compliance unit circulates a confidential questionnaire among staff in an effort to find out about possible problems,' says the compliance chief.

Training and development of employees is also essential to improved compliance, and also to risk management. 'Breakdowns in compliance and risk management processes often occur deep within organisations,' says Richard Beaumont, a partner at PricewaterhouseCoopers in San Francisco. 'Clear definition and assignment of roles and responsibilities for monitoring and managing compliance and other risks throughout the organisation is critical. These definitions should include clear issues escalation criteria to ensure that management is kept apprised of emerging risks and significant instances of non-compliance.'

## Implementing the initiative



After assessment comes implementation. Organisational initiatives, and in particular the option to outsource, have grabbed most attention in recent years. But the choice between keeping functions and processes in-house or handing them over to third parties is a complex one. 'There are undoubtedly performance gains to be had from new organisational approaches,' says Etienne Boris at PricewaterhouseCoopers. 'But they depend on a clear-eyed analysis of the risks and benefits.'

Certainly, there is rising awareness that outsourcing can fail, even in its classic mission to deliver cost savings. Asked to identify the principal risks and benefits of outsourcing, respondents defined the principal benefit as lower costs (53%) but also included higher costs as one of the top three risks (35%). This inconsistency over costs comes soon after the findings of another PricewaterhouseCoopers survey, which found that fewer than half of the European and US multinationals to have outsourced finance functions consider them cost-effective.<sup>1</sup>

In the UK, major insurers have begun outsourcing client service functions, recognising that they need help in mapping business processes. Success has been mixed. 'There has been a lot of activity in what I would call tactical outsourcing but many deals have gone awry,' says Mark Stephen, a partner at PricewaterhouseCoopers in London. 'Requests for proposals sent out to providers are often not clearly defined and this can result in unexpected cost over-runs.'

There are also fears that there is a trade-off between improving performance in cost terms and worsening performance in terms of quality of service. Asked to identify the principal benefits of the in-house approach, by far the largest number of respondents (82%) cite greater understanding of the business. An improved quality of service is mentioned by a further 28% of respondents. By contrast, the principal risks of outsourcing are seen as less developed understanding of the business (57%) and deteriorating quality of service (34%).

Such fears may help explain survey respondents' preference for in-house approaches to performance improvement as opposed to other approaches. Only in the non-core areas of IT management and procurement do a majority of respondents prefer alternatives to the in-house approach. That's true of larger companies as well as smaller ones (see table overleaf).

Such concerns are likely to dissipate, however, as service providers mature and

focus on delivering process improvements (see box on page 12). John Vaughn, president and CEO of International Financial Data Services (IFDS) in Canada, which is owned by State Street and DST Systems, believes that service providers must think more as partners to truly add long-term value to their clients. 'Providers must move beyond being the nicest person from Hell in the eyes of their clients,' he says. 'At IFDS we have taken our relationship beyond the bounds of the service level agreement. We are becoming extensions of our client's business, adding value in a variety of ways and places.' To reinforce this behaviour IFDS measures client satisfaction, using several key drivers, at quarterly review sessions with its clients. In another pointer to the future, it also ties staff compensation directly to meeting specific satisfaction goals.

Financial institutions are also learning to demand more of outsourcing than lower costs, particularly as rising wage levels in leading provider markets gradually erode the cost savings argument. The survey respondents acknowledge that dramatic

<sup>1</sup> Management Barometer, PricewaterhouseCoopers, October 2004

## Implementing the initiative continued



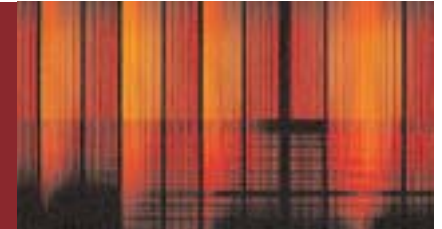
change is less likely to come in-house, with more than half of them identifying limited access to best-of-breed talent and technology and limited scope for significant organisational change as key risks of this approach. 'For some time we have outsourced selected aspects of information technology as an expense control device,' says Mr Lynch at Zurich, who now oversees the company's Small Business platform in the US. 'In the last two years or so we have been expanding our use of third parties where they can perform functions and processes better, cheaper and faster than us.'

**In your view, what is the most effective organisational approach to handling performance improvement initiatives in each of the following areas of the business?**

	In-house approach	Outsourcing to a local provider	Outsourcing to an offshore provider	Shared services in local market	Shared services in offshore market
Transactions and processing	53	22	6	16	3
Compliance	87	7	1	4	0
Sales and marketing	75	12	3	8	0
Customer service	72	12	4	8	1
Product development	75	10	4	8	3
Human resources	59	24	4	10	1
Quality/performance of actual products and services	69	18	4	5	3
IT management	35	40	7	14	4
Finance and accounting	67	19	4	9	2
Procurement	49	35	4	10	1
Risk management	83	9	2	4	0
Speed and quality of management decision-making	89	4	2	3	0

Source: PricewaterhouseCoopers/Economist Intelligence Unit survey, October-November 2004

## Implementing the initiative continued



### BPO providers: Scaling the value ladder

A US health insurance client of Wipro Spectramind, one of India's largest call centres and business process outsourcing (BPO) firms, was worried about the size of claims that were being paid out to its customers. So Spectramind, which handles call centre and BPO work for the insurance company, hired medical practitioners to check the validity of claims. That reduced the payouts to such an extent that the insurance company panicked and asked the BPO to soften up. 'The client said they were getting a reputation for being too tough so asked us to let claims up to \$200 be paid without questions,' says Raman Roy, chairman and managing director of Spectramind, which has 13,000 employees and is part of India's Wipro information technology group.

India is only one of a number of offshore destinations used by financial institutions for business process outsourcing. Other favoured offshore locations include Singapore, China, the Philippines and Vietnam. Yet the evolution of India's service

providers paints an instructive picture of how simple but valuable performance improvements can be achieved when financial processing work is moved to other locations – in addition to large cost savings that clients automatically expect. Most firms dealing with financial service businesses such as banking, insurance and credit cards say that clients go there initially for cost savings but then find better productivity, quality and performance than would be available at home.

Call-centre and processing work transferred to India covers a wide range of activities, from telemarketing to billing and dispute resolution, executing complex insurance claims and (in one or two cases) preparing company financial analysis for securities firms. Some operators say that telemarketing is too basic. 'It's too low-intellect for India,' says Mr Talwar, who employs 400-500 qualified or student accountants. He says value comes from hybrid voice and data work on processes like insurance claims plus processing work using graduate skills not available in the UK.

Ananda Mukerji, managing director and CEO of ICICI OneSource, which is majority owned

by ICICI, one of India's largest banks, adds that some high-end telemarketing – like selling extra services to credit card customers – can usefully be done in India. On collections work, OneSource decided that, though it could cope with the early stages when one payment had been missed, it did not have sufficient experience for complex later-stage work. So, in September 2004, it bought Account Solutions Group (ASG), a New York-based consumer collections agency, which specialises in third party debt collections. ASG's clients include four of the top ten US credit card issuers.

All the BPO firms stress the strength of their security and data protection procedures – including OneSource, whose work for Lloyds has been queried by trade unions in the UK. They also stress the value of Indian graduate workforces – between 25% and 33% are graduates and engineers at both Spectramind and OneSource, while the rest are undergraduates. But the attrition (staff turnover) rates are high – 35%-40% – which can mean that young people doing basic call-centre work have less experience than their counterparts in the UK.

OneSource's Mr Mukerji says that clients move voice operations before computer processes because there are greater savings to be made quickly, and because voice operations do not involve so many interlinked activities as back office and other multiple tasks, though that is changing. But few clients are yet prepared to move entire processes to one BPO operator, preferring either just to move parts of a process, or double up what is moved to India with parallel operations in their home countries. The greatest gains however are made when a BPO has entire processes linking voice and back office work, enabling productivity and process improvements to be delivered across a range of interconnected activities.

The need for client comfort is stressed by several firms. 'It is essential to have commitment from the client's management,' says Talwar. 'No provider can ever be successful without that commitment. If a client is lukewarm, there will be enough doubters and non-believers to make it not work.'

## Implementing the initiative continued



### Looking to the future

In two particular sectors of the financial services industry – insurance and asset management – outsourcing is a trend that has a long way to run, particularly outside the US and UK. The insurance sector in particular is only just waking up to the potential of outsourcing, if only as a way to reduce cost. ‘This industry is way behind other financial service sectors in the struggle to get costs under control,’ says one Canadian financial specialist. This is likely to change as competitive pressures force insurers to slim their cost base. In particular, insurers need help in mapping their business processes to determine accurately transaction volume and appropriate service levels.

The asset management industry, facing a bloated cost base and the prospect of volatile, if not declining, revenues, is placing primary emphasis on identifying its’ core competencies, whether product ‘manufacturing’, distribution, marketing or client service, and passing other functions to third parties. ‘Headline savings from outsourcing are not the issue,’ says Mark Austin, head of investor services strategy at JP Morgan in London. ‘Fund managers need to get rid of their fixed costs (mainly people) in favour of a variable cost structure.’

Overall, the major providers of investment services appear confident of future growth, especially outside the US. First, as the

investment management industry consolidates, the task of integrating middle and back offices in-house may be too daunting to contemplate. Second, also as a consequence of consolidation, investment managers are likely to leave and start their own ‘boutique’ firms, operating on a virtual basis without the traditional operational trappings.

Most financial services industry specialists agree that over time third-party providers will continue to make inroads, although the pace with which they win business will vary between different functions and parts of the industry.

‘The bigger financial institutions have already moved functions such as IT and call centres offshore and now they are doing the same with processing. The banks are leading this initiative; insurers and asset management firms are following some way behind,’ says Jeremy Scott, Chairman of the Global Financial Services Leadership Team at PricewaterhouseCoopers.

Traditional areas of outsourcing activity, such as IT management, remain the strongest candidate for outsourcing over the next three years, while functions that are regarded as more central to the organisation, such as risk management and compliance, are least likely to move out of house. But as the outsourcing industry matures, fears of loss of control or massive cost over-runs will subside and the benefits of improved performance will rival cost savings as the primary attraction of using outside providers.

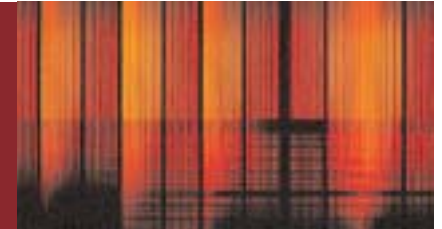
### % of respondents using or planning to use in-house organisation approach

	Now	In three years
Compliance	90	85
Risk management	90	85
Operations	83	72
Finance	82	74
IT management	60	45

Source: PricewaterhouseCoopers/Economist Intelligence Unit survey, October-November 2004



## Utilising all the levers of change



Organisation is just one driver of performance. Successful performance improvement utilises and aligns a number of interconnected levers to deliver change, among them people, processes and technology.

The focus of attention will vary from business area to business area. A majority of survey respondents picked redesign of operational processes as their key priority over the next three years in the finance area, for example, but plumped for training and development of existing employees as the main focus of performance improvement efforts in compliance and risk management.

Underpinning any successful improvement drive will be a performance-driven culture. If information on the performance of business units and processes is to be gathered and distributed efficiently throughout the organisation, a culture of transparency is critical. If compliance and risk management issues are to be recognised and acted upon, employees throughout the organisation must be encouraged to escalate concerns to senior management. If outsourcing is to bring performance gains, service providers too must be focused on quality as well as cost.

In order to inculcate a culture that delivers and rewards improved performance, organisations must align incentives with performance, construct rigorous and ongoing training and assessment of personnel throughout the organisation and provide visible measures of outcomes and benefits. HR professionals have a key part to play in all of this. 'Some firms may view HR as a candidate for outsourcing but if they don't understand core HR processes it would be

a mistake to outsource them,' says Christopher Box, a senior manager at PricewaterhouseCoopers in London.

But more important still is the tone set at the top of the organisation. From defining goals, to monitoring the progress of specific initiatives, to rewarding the achievement of targeted outcomes, senior managers must be the champions of performance improvement. Without their active and visible support, aspiration will seldom turn into achievement. □

## Appendix: Survey results



The Economist Intelligence Unit and PricewaterhouseCoopers conducted a special online survey of senior executives in financial institutions on the subject of improving performance. Executives from 227 institutions in Asia, Europe and North America participated in the survey, which was conducted during October and November 2004. Our thanks are due to all those who participated for sharing their insights with us.

Please note that totals do not always add up to 100 because of rounding, or because respondents could choose more than one answer.

### Demographics

#### 1. In which country are you based? (Top ten locations)

United Kingdom	21%
United States of America	14%
Canada	4%
Singapore	4%
India	4%
Germany	3%
Portugal	3%
Spain	3%
Poland	3%
Other	41%

#### 2. In which country is your institution headquartered? (Top ten locations)

United States of America	19%
United Kingdom	16%
Canada	4%
Switzerland	4%
India	4%
Germany	3%
Turkey	3%
Spain	3%
Netherlands	3%
Other	41%

#### 3. What is your title?

Senior management	40%
Line manager	24%
Board member (executive director)	17%
Board member (non-executive director)	2%
Other	15%

#### 4. What are your main functional roles?

Strategy and planning	34%
Finance	30%
Operations	21%
Risk management	21%
Marketing and communications	18%
Investor relations	11%
Internal audit	7%
Legal	4%
Human resources	4%
Other	17%

## Appendix: Survey results continued



### 5. What area of financial services do you personally work in?

Investment management	28%
Retail banking	19%
Investment banking	19%
Capital markets	17%
Corporate banking	17%
Non-life insurance	14%
Life insurance	13%
Private banking	12%
Private equity	10%
Outsourcing services provision	7%
Re-insurance	4%
Other	10%

### 6. What are your organisation's global annual revenues in US dollars?

\$500m or less	44%
\$500m to \$1bn	12%
\$1bn to \$5bn	15%
\$5bn to \$10bn	5%
\$10bn or more	25%

### Process & Performance

#### 7. What are the main factors that drive performance improvement initiatives at your organisation? Please choose up to three drivers.

Rising competitive pressures	52%
Customer expectations	51%
Need to improve profitability	49%
Organisational culture of constant performance improvement	41%
Pressure from senior management	21%
Expanding regulatory requirements	19%
Upward pressures on cost base	16%
Need to improve risk management	13%
Share-price movements	11%
Successful initiatives undertaken by other companies	10%
Other	4%

## Appendix: Survey results continued



8. How satisfied are you with the performance of the following areas of your business? Please rate on a scale of 1 to 5, where 1 = Extremely satisfied and 5 = Extremely dissatisfied.

	1 Extremely satisfied	2	3	4	5 Extremely dissatisfied	Average score
Compliance	16	48	23	12	1	2.33
Risk management	12	43	32	9	3	2.48
Finance and accounting	12	38	35	13	0	2.50
Quality/performance of actual products and services	8	46	33	13	1	2.54
Transactions and processing	8	42	34	14	2	2.60
Customer service	9	35	34	18	2	2.70
Sales and marketing	4	30	45	19	3	2.86
Procurement	1	31	48	16	3	2.87
Product development	6	30	38	20	5	2.89
Speed and quality of management decision-making	9	32	27	23	9	2.89
IT management	6	27	38	23	7	2.97
Human resources	5	27	37	23	8	3.00

## Appendix: Survey results continued



9. For each of the following areas, please check the primary mechanism your organisation uses to assess its performance.

	Key performance indicators	Regular audits	Internal benchmarking	External benchmarking	No formal measures
Transactions and processing	34	21	27	5	14
Compliance	8	51	15	11	15
Sales and marketing	34	7	23	17	17
Customer service	27	10	21	25	18
Product development	14	4	19	26	35
Human resources	13	5	29	15	37
Quality/performance of actual products and services	29	9	23	24	14
IT management	16	9	24	19	30
Finance and accounting	19	36	17	8	19
Procurement	13	13	28	9	35
Risk management	19	37	20	11	12
Speed and quality of management decision-making	12	4	17	7	61



## Appendix: Survey results continued



10. How satisfied are you with the management data you receive on your organisation's performance in each of the following areas? Please rate on a scale of 1 to 5, where 1 = Extremely satisfied and 5 = Extremely dissatisfied.

	1 Extremely satisfied	2	3	4	5 Extremely dissatisfied	Average score
Finance and accounting	12	36	35	13	2	2.57
Transactions and processing	9	38	37	12	3	2.60
Compliance	9	38	35	12	3	2.61
Risk management	11	38	33	14	4	2.62
Sales and marketing	9	33	40	15	3	2.70
Quality/performance of actual products and services	7	31	45	14	3	2.75
Customer service	8	31	39	18	4	2.80
Product development	4	24	40	24	7	3.04
IT management	7	22	40	24	8	3.05
Procurement	3	20	50	21	5	3.05
Speed and quality of management decision-making	4	24	31	31	11	3.21
Human resources	4	16	41	31	8	3.22

11. Which areas of your business are the key sources of competitive advantage for your organisation in the marketplace? Please choose up to three areas.

Customer service	53%
Sales, branding and marketing	49%
Quality/performance of actual products and services	39%
Product development	29%
Risk management	26%
Transactions and processing	26%
Speed and quality of management decision-making	15%
Human resources	13%
Finance and accounting	11%
IT management	11%
Compliance	9%
Procurement	1%
Other	4%

## Appendix: Survey results continued



12. How does your organisation prioritise which performance areas to concentrate on? Please choose up to three answers.

Greatest opportunities for increased revenue	63%
Alignment with strategic priorities of the organisation	36%
Greatest impact on quality of customer service	34%
Greatest opportunities for cost savings	33%
Projected increases in market share	31%
Response to compliance and regulatory drivers	24%
Enhancement of brand proposition	12%
Reduction in processing times	11%
Cost of undertaking initiative	11%
Greatest opportunities to improve risk management	9%
Overall cost associated with business area	9%
Value-chain/differentiation analysis	7%
Other	2%

13. How well aligned are each of the following business functions in terms of their ability to deliver on your organisation's overall strategy? Please rate on a scale of 1 to 5, where 1 = Extremely well-aligned and 5 = Extremely poorly-aligned.

	1 Extremely well-aligned	2	3	4	5 Extremely poorly-aligned	Average score
Compliance	11	47	31	9	2	2.43
Transactions and processing	12	42	35	10	1	2.47
Finance and accounting	12	41	37	9	2	2.48
Risk management	13	41	30	14	2	2.51
Customer service	13	42	28	12	4	2.50
Quality/performance of actual products and services	12	38	38	11	1	2.52
Sales and marketing	12	38	34	12	3	2.54
Product development	8	35	37	14	5	2.72
Speed and quality of management decision-making	14	26	32	19	9	2.82
IT management	6	32	37	21	4	2.85
Procurement	4	22	51	19	3	2.95
Human resources	7	19	44	23	6	3.04

## Appendix: Survey results continued



14. In your view, what is the most effective organisational approach to handling performance improvement initiatives in each of the following areas of the business?

	In-house approach	Outsourcing to a local provider	Outsourcing to an offshore provider	Shared services in local market	Shared services in offshore market
Transactions and processing	53	22	6	16	3
Compliance	87	7	1	4	0
Sales and marketing	75	12	3	8	0
Customer service	72	12	4	8	1
Product development	75	10	4	8	3
Human resources	59	24	4	10	1
Quality/performance of actual products and services	69	18	4	5	3
IT management	35	40	7	14	4
Finance and accounting	67	19	4	9	2
Procurement	49	35	4	10	1
Risk management	83	9	2	4	0
Speed and quality of management decision-making	89	4	2	3	0

15. In your experience/view, what are the principal benefits of taking an in-house approach to improving performance? Please choose up to three answers.

Greater understanding of the business	82%
Greater focus on core competencies	42%
Improved quality of service	28%
Improved business continuity	27%
Lower costs	24%
Enhanced standards of compliance and control	22%
Improved security of data and IP	22%
Improved quality of management data	17%
Limited organisational upheavals	11%
Access to better talent and technology	5%
Other	3%

## Appendix: Survey results continued



16. In your experience/view, what are the principal risks of taking an in-house approach to improving performance? Please choose up to three answers.

Limited scope for significant organisational change	59%
Limited access to best-of-breed talent and technology	58%
Higher costs	44%
Less focus on core competencies	23%
Exposure to political instability	17%
Deteriorating quality of service	15%
Worsening standards of compliance and control	13%
Less developed understanding of the business	8%
Deteriorating quality of management data	7%
Reduced business continuity	7%
Reduced security of data and IP	5%
Other	4%

17. In your experience/view, what are the principal benefits of outsourcing areas of the business to third parties in order to improve performance? Please choose up to three answers.

Lower costs	53%
Access to better talent and technology	50%
Greater focus on core competencies	46%
Improved quality of service	29%
Limited organisational upheavals	21%
Improved quality of management data	15%
Enhanced standards of compliance and control	13%
Improved business continuity	10%
Greater understanding of the business	9%
Improved security of data and IP	3%
Other	4%

## Appendix: Survey results continued



18. In your experience/view, what are the principal risks of outsourcing areas of the business to third parties in order to improve performance? Please choose up to three answers.

Less developed understanding of the business	57%
Higher costs	35%
Deteriorating quality of service	34%
Reduced security of data and IP	29%
Worsening standards of compliance and control	27%
Deteriorating quality of management data	21%
Limited scope for significant organisational change	17%
Less focus on core competencies	13%
Reduced business continuity	13%
Exposure to political instability	8%
Limited access to best-of-breed talent and technology	3%
Other	3%

19. What are the critical factors behind successful performance improvement initiatives? Please choose the top three.

Active involvement on part of senior management	65%
Clear and measurable project milestones	44%
Alignment of incentives with improved performance	35%
Active involvement on part of business unit managers	34%
Finding the right people	32%
Availability of high-quality internal management data	20%
Availability of recognised external benchmarking data	14%
Centralised control of the initiative	10%
Track record of performance improvement success	10%
Access to external expertise and advice	10%
Specialised project teams	7%
Utilising the right technology	7%
Competitive processes to find the right service provider	2%
Other	1%



## Appendix: Survey results continued



### 20. Which of the following statements apply to your organisation's performance in the area of finance?

We have specific programmes (e.g., Six Sigma) in place to identify and solve finance performance weaknesses	16%
We have specialist teams tasked with identifying and solving finance process inefficiencies	32%
We have corporate performance measurement systems in place that provide ongoing data about finance performance	51%
We have structured assessments of the quality and suitability of personnel in the finance function	20%
We have periodic reviews of our finance performance	69%
We review finance performance on an ad hoc basis	15%
We do not formally review finance performance	7%
We assess finance performance at the business unit level	49%
We assess finance performance on an enterprise-wide basis	35%
We use external advisers to assess and improve finance performance	16%

### 21. Over the next three years, on which performance drivers will your organisation primarily focus in order to improve performance in the area of finance? Please choose up to three drivers.

Redesign of operational processes to ensure greater efficiency	59%
Increased use and leverage of technology	49%
Training and development of existing employees	44%
Development and reporting of better performance measurement data	42%
Changes to organisational approach to finance	23%
Investment in new staffing capabilities	19%
Other	2%

### 22. Which of the following statements apply to your organisation's performance in the area of compliance?

We have specific programmes (e.g., Six Sigma) in place to identify and solve compliance performance weaknesses	16%
We have specialist teams tasked with identifying and solving compliance process inefficiencies	43%
We have corporate performance measurement systems in place that provide ongoing data about compliance performance	38%
We have structured assessments of the quality and suitability of personnel in the compliance function	26%
We have periodic reviews of our compliance performance	60%
We review compliance performance on an ad hoc basis	15%
We do not formally review our compliance performance	11%
We assess compliance performance at the business unit level	35%
We assess compliance performance on an enterprise-wide basis	30%
We use external advisers to assess and improve compliance performance	20%

### 23. Over the next three years, on which performance drivers will your organisation primarily focus in order to improve performance in the area of compliance? Please choose up to three drivers.

Training and development of existing employees	58%
Redesign of operational processes to ensure greater efficiency	41%
Increased use and leverage of technology	35%
Changes to organisational approach to compliance	34%
Development and reporting of better performance measurement data	33%
Investment in new staffing capabilities	18%
Other	0%

## Appendix: Survey results continued



### 24. Which of the following statements apply to your organisation's performance in the area of risk management?

We have specific programmes (e.g., Six Sigma) in place to identify and solve risk management performance weaknesses	19%
We have specialist teams tasked with identifying and solving risk management process inefficiencies	46%
We have corporate performance measurement systems in place that provide ongoing data about risk management performance	45%
We have structured assessments of the quality and suitability of personnel in the risk management function	23%
We have periodic reviews of risk management performance	63%
We review risk management performance on an ad hoc basis	15%
We do not formally review risk management performance	8%
We assess risk management performance at the business unit level	37%
We assess risk management performance on an enterprise-wide basis	36%
We use external advisers to assess and improve risk management performance	14%

### 25. Over the next three years, on which performance drivers will your organisation primarily focus in order to improve performance in the area of risk management? Please choose up to three drivers.

Training and development of existing employees	49%
Increased use and leverage of technology	49%
Redesign of operational processes to ensure greater efficiency	43%
Changes to organisational approach to risk management	39%
Development and reporting of better performance measurement data	33%
Investment in new staffing capabilities	19%
Other	1%

### 26. Which of the following statements apply to your organisation's performance in the area of IT management?

We have specific programmes (e.g., Six Sigma) in place to identify and solve IT management performance weaknesses	15%
We have specialist teams tasked with identifying and solving IT management process inefficiencies	44%
We have corporate performance measurement systems in place that provide ongoing data about IT management performance	31%
We have structured assessments of the quality and suitability of personnel in the IT management function	25%
We have periodic reviews of IT management performance	45%
We review IT management performance on an ad hoc basis	20%
We do not formally review IT management performance	20%
We assess IT management performance at the business unit level	22%
We assess IT management performance on an enterprise-wide basis	27%
We use external advisers to assess and improve IT management performance	22%

### 27. Over the next three years, on which performance drivers will your organisation primarily focus in order to improve performance in the area of IT management? Please choose up to three drivers.

Increased use and leverage of technology	64%
Redesign of operational processes to ensure greater efficiency	48%
Training and development of existing employees	46%
Investment in new staffing capabilities	27%
Development and reporting of better performance measurement data	22%
Changes to organisational approach to finance	11%
Other	1%

## Appendix: Survey results continued



28. Which of these organisational approaches does your institution currently prefer to use in each of these areas?

	In-house approach	Outsourcing to a local provider	Outsourcing to an offshore provider	Shared services in local market	Shared services in offshore market
Operations	84	10	2	2	1
Compliance	92	7	0	1	0
IT management	61	28	3	6	1
Finance and accounting	84	14	1	1	0
Risk management	92	5	1	1	0

29. Which of these organisational approaches does your institution plan to use over the next three years in each of these areas?

	In-house approach	Outsourcing to a local provider	Outsourcing to an offshore provider	Shared services in local market	Shared services in offshore market
Operations	73	15	4	5	3
Compliance	86	7	2	4	0
IT management	46	33	7	9	4
Finance and accounting	75	16	2	4	1
Risk management	86	7	3	2	0

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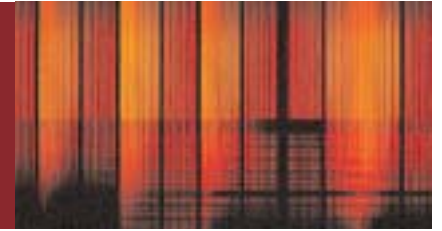
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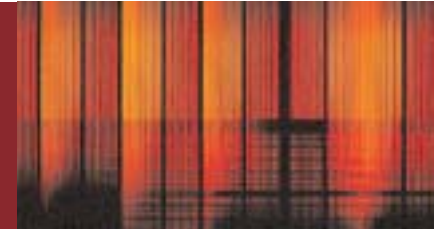
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