



# The Emerging Global Labor Market: The Demand for Offshore Talent in Retail Banking

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Retail Banking

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## Guiding Principles

Any job that is not confined to a particular location has the potential to be globally resourced, or performed anywhere in the world. Broadly speaking, this includes any task that requires no physical or complex interaction between an employee and customers or colleagues, and little or no local knowledge.

Such jobs can be performed wherever a company deems most attractive. A company may choose to have a particular location insensitive job performed in the demand market (that is, in the market in which the resulting output is sold), in a border zone (nearshore), or remotely (offshore). Therefore, not all location insensitive jobs will move offshore.

We evaluate only service sector jobs. Although manufacturing jobs may be insensitive to their location as well, this study focuses on service jobs, whether they are in service sectors or in a back-office service function (e.g., accounting) in a manufacturing sector.

We focus on the demand for low-wage employment from high-wage countries. To estimate potential demand for globally resourced labor, we treat countries as neither inherently on the supply side nor inherently on the demand side in the global labor market. However, since cost is a major determinant of companies' location decisions, developed countries are most likely to provide the bulk of demand for offshore labor, and developing countries the bulk of supply. When we evaluate the actual rate of offshoring today and how fast it will grow, we examine only the demand for low-wage labor from high-wage countries.

We assume that demand for labor for a particular activity is the same onshore and offshore. In reality, capital/labor tradeoffs and increased service levels may cause high-wage countries to seek more labor in low-wage countries than they would for performing the same activity in the demand market. Productivity differences between the original location and the new location may also influence demand for labor. Since these effects can be either positive or negative and tend to level over time, our default assumption is that the number of FTEs<sup>1</sup> needed for an activity is the same whether located onshore or offshore.

For the demand evaluations we do not consider any supply constraints. All evaluations are made under the assumption that global supply will be able to meet demand. Actual supply conditions are examined in the second report in this series, "The Supply of Offshore Talent in Services".

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<sup>1</sup> Full time equivalent

# The Emerging Global Labor Market: The Demand for Offshore Talent in Retail Banking

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## **SUMMARY OF FINDINGS**

Retail banking was one of the early sectors to adopt the global resourcing of services. As early as 1996, players such as Citibank were separating the demand and supply for services by moving part of their operations to remote locations. The uptake of global resourcing in retail banking is noticeable, though retail banking players vary widely in the degree to which they are using global resourcing opportunities. Some players are still in the initial or pilot phases while others have global operating models and are leveraging global resourcing to create global process architectures. Despite the fast movement of multinational companies, only 2 percent of the jobs in retail banking in high-wage locations are offshored.

\* \* \*

Retail banking employed, in 2003, approximately 13 million people worldwide. In 2008, this number is projected to be approximately 12.7 million, or a 0.6 percent annual decrease. This is a consequence of continued industry consolidation, operational enhancements, and automation. More than half of these employees work in the branches in customer-facing functions, in either services or sales. An additional 24 percent are employed in back-office and call center functions. Consequently, retail banking employs mostly generalists and support staff.

The theoretical maximum for globally resourced labor in retail banking is 25 percent, translating into approximately 3.1 million jobs in 2008. This value

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stems from the large amount of back-office work and from the increasing use of call centers and e-banking by customers. As expected, the functions particularly amenable to global resourcing are call centers (90 percent), IT services (54 percent), back-office functions (50 percent), and general and administrative (G&A) functions (40 percent). Derived from these functions, the occupations most required in global resourcing are the generalists and engineers.

Yet, the degree of adoption for global resourcing in retail banking is far from the theoretical maximum. We estimate that approximately 93,000 jobs are performed away from the location in which they are demanded. Part of the explanation for the low adoption is the result of the need for a clear cost differential in the global resourcing process for players to prioritize global resourcing over other profit-enhancing options. Currently, 58 percent of the employment in retail banking is in developing countries where the cost differential savings barely justify the effort. Thus, most of the players that have adopted are from developed countries. When only those banks are considered, the adoption degree is 2 percent of employment in high-wage countries.

Adoption of global resourcing is mainly driven by intensifying cost pressure. Other enablers are the players' global presence and interest in pursuing additional revenue streams. Main existing inhibitors are a perception of low returns, local legal barriers (e.g., some countries prohibit the storage of financial information in foreign countries), lack of scale, and operational difficulties.

Historical evaluation of adoption of global resourcing shows that this is largely a step function. As players first pursue the effort and gain confidence, they are likely to pursue it even further. Additionally, as some players begin to adopt, those who were initially skeptical not only feel the pressure of the competition but also benefit from observing and learning from those that spearheaded the efforts. Global resourcing in retail banking is likely to continue growing, reaching a projected 2.4 percent of total employment by 2008, translating to 303,000 employees (versus 93,000 in 2003). Large multinational companies will drive adoption, and in 2008 globally resourced employment will translate to 5.4 percent of high-wage countries' total retail banking employment.


## SECTOR DEFINITION AND OVERVIEW

### Sector definition

When comparing of different countries, the activities performed by a single bank are highly heterogeneous. In most countries the prevailing concept is that of a universal bank, where both retail and wholesale banking activities are performed; in addition, these banks are suppliers of associated products such as insurance. In this study, only retail banking employment is included. For universal banks, the wholesale or investment portions of employment were excluded, as were those relating to insurance products. Insurance (P&C, health and life) is treated separately in this project. Our study thus covers depository services, lending services, and credit card services offered by commercial banks. "Credit card only" companies, such as American Express, are not within the scope of the study (Exhibit 1).

### Exhibit 1

#### RETAIL BANKING SECTOR CASE FOCUSES ON DEPOSITORY AND LENDING SERVICES AND CREDIT CARDS

 Focus segments

|                            | Description   | Example products  | Example companies  |
|----------------------------|---|---|--|
| <b>Depository services</b> | <ul style="list-style-type: none"> <li>Standard account relationship functions performed by traditional banking branches</li> </ul>   | <ul style="list-style-type: none"> <li>Account opening</li> <li>Check processing</li> </ul>                 | <ul style="list-style-type: none"> <li>HSBC</li> <li>Citigroup</li> </ul>              |
| <b>Lending services</b>    | <ul style="list-style-type: none"> <li>Standard lending functions performed by retail banks</li> <li>Excludes lending services done by non-bank financial institutions</li> </ul> | <ul style="list-style-type: none"> <li>Mortgage loans</li> <li>Consumer loans</li> <li>Overdraft</li> </ul> | <ul style="list-style-type: none"> <li>GE Capital</li> </ul>                           |
| <b>Credit cards</b>        | <ul style="list-style-type: none"> <li>Range of credit or debit cards</li> </ul>  | <ul style="list-style-type: none"> <li>Credit cards</li> <li>Debit cards</li> </ul>                         | <ul style="list-style-type: none"> <li>Any retail-bank-issued card*</li> </ul>         |
| <b>Asset management</b>    | <ul style="list-style-type: none"> <li>Wealth management</li> </ul>   | <ul style="list-style-type: none"> <li>Institutional asset management</li> <li>Retail brokerage</li> </ul>  | <ul style="list-style-type: none"> <li>Fidelity</li> </ul>                             |
| <b>Insurance</b>           | <ul style="list-style-type: none"> <li>Standard insurance coverages</li> </ul>  | <ul style="list-style-type: none"> <li>P&amp;C</li> <li>Health</li> <li>Life</li> </ul>                     | <ul style="list-style-type: none"> <li>Conseco</li> <li>Willis</li> <li>AIG</li> </ul> |

\* Credit card only companies, such as American Express, were excluded from the definition of the study.  
Source: McKinsey Global Institute analysis

### Sector overview

The main trends in the retail banking sector over the past few years have been increasing consolidation, improved productivity, higher challenges to assure customer loyalty, and tighter regulation:

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- *Consolidation.* The growth of players in retail banking has occurred in part through organic growth but mostly through mergers and acquisitions. These are widespread across the financial services landscape and within individual business lines. Larger financial services firms have been on an acquisition spree to build scale and scope.<sup>1</sup> Consolidation is much more prevalent domestically than internationally, as the merging partners' networks overlap and integration is much easier. However, skilled players are expanding internationally, particularly in border regions, and are seeking a presence in developing markets such as Eastern Europe, Brazil, Mexico, Korea, and India; the emergence of an affluent class and the expansion of the middle class in several developing countries is driving growth in financial services in new geographies outside the United States and Western Europe.<sup>2</sup>
  - *Productivity.* Overall, financial services firms are becoming more cost-efficient thanks to consolidation and, more importantly, automation. As a consequence, the variance between best-in-class players and the rest is increasing.<sup>3</sup>
  - *Customer loyalty.* The variety of players is wide, so customers frequently have more than one banking relationship and can switch banks easily. Good customer relationships thus lie at the heart of customer loyalty.<sup>4</sup> Customers prefer domestic providers, value established brands, and want personal advisory services; they increasingly expect customized product solutions and multichannel delivery of products and services. There is a continued demand for anytime, anywhere access and increased transparency. The usage of distribution channels has evolved, particularly in the 1990s, through increased use of ATMs, online access, wireless access, and call centers. Yet, although it was believed that online customer contact would grow exponentially, the growth of this channel has stabilized. Counterintuitively, there has recently been an increase in the number of branches in the United States.<sup>5</sup>

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<sup>1</sup> Bigger footprint, *The Economist*, April 17, 2004, page 24.

<sup>2</sup> Citigroup looks abroad for future growth, *The Wall Street Journal*, March 15, 2004; Westward, ho! Retail banking, *The Economist*, May 8, 2004; GE Banks on Emerging Markets. *The Wall Street Journal*, August 24, 2004

<sup>3</sup> How IT enables productivity. Retail banking case. McKinsey Global Institute.

<sup>4</sup> An Immeasurable asset, *The Economist*, April 17, 2004, page 1.

<sup>5</sup> Branching out—American banks' new love affair with branches, *The Economist*, February 17, 2004, page 4; Rooting for branches, *The Economist*, April 17, 2004. See also additional articles in the same issue.

- *Regulatory issues.* Regulations and standards across the sectors are being increasingly homogenized and tightened. Recent regulation has affected: accounting standards (e.g., IASB), risk management (e.g., Basel II), and corporate governance (e.g., Sarbanes-Oxley). Even national security regulations in the United States (e.g., Patriot Act) have affected retail banking. Similarly, consumer protection laws and privacy standards have become more strict.

## SECTOR EMPLOYMENT

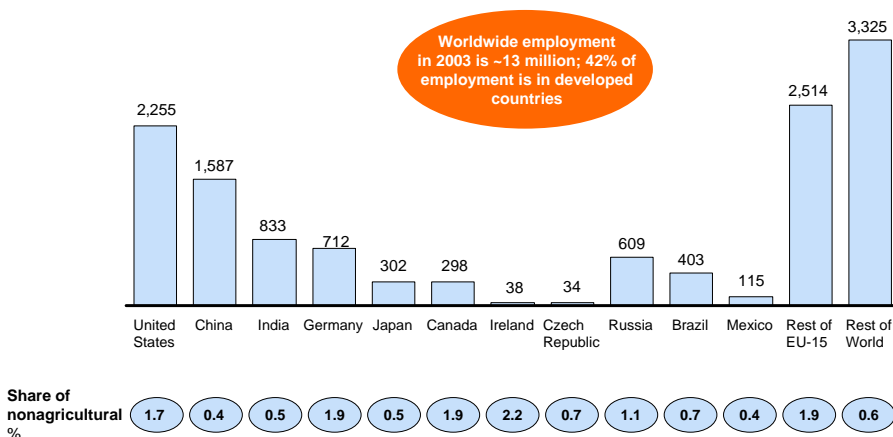
### Sector employment overview

Worldwide, the retail banking sector employed 13 million FTEs in 2003 (Exhibit 2). Employment in the sector varies between developed and developing countries. In developed countries, employment in retail banking accounts for approximately 2 percent of the total nonagricultural employment, whereas in developing countries this value falls to nearly 0.7 percent (see Exhibit 2). This difference is due to the fact that in developing countries, a smaller percentage of the population is "banked" (i.e., has a bank account) and in general, saving and lending practices are less developed.

### Exhibit 2

#### RETAIL BANKING EMPLOYED APPROXIMATELY 13 MILLION FTEs IN 2003

2003, thousand

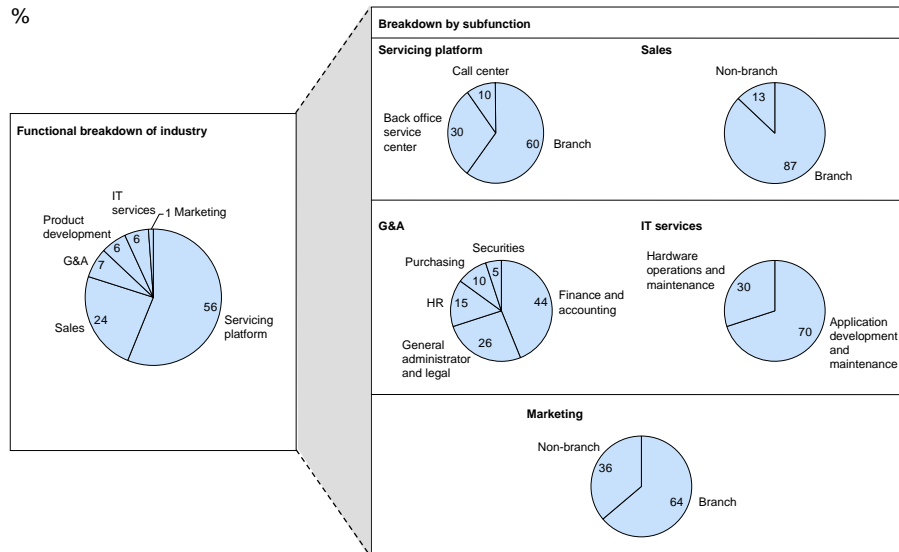


Source: SNL; Japanex Banken Association; AGV Banken; AVG Versicherungen; 2001 Canadian Census; India Banking Association; Almanac of China's Financing and Banking; Febraban; Exame Maiores e Melhores; CNBV

- Employment share by function.** The sector may be defined as a highly customer-facing industry with a large back office supported by a strong sales force (Exhibit 3). As a result of the strong customer service function, more than half of the employees (56 percent) are in the service platform. This encompasses services provided at branches, call centers, and back-office service centers. Despite the launch of and the increase in the use of ATM and internet banking, bank branches still account for the highest portion of employment in the sector. This employment is in service provision (mostly tellers), which accounts for 34 percent of total employment, and in the sales force, which provides an additional 21 percent of the employment. Corporate back-office service centers are responsible for an additional 17 percent of the employment in the sector. Additional non-customer-specific functions such as G&A, product development, non-branch sales, marketing, and internal IT support are responsible for smaller employment shares within the sector.

**Exhibit 3**

**MOST RETAIL BANKING EMPLOYEES ARE IN THE SERVICE PLATFORM AND SALES FUNCTIONS**

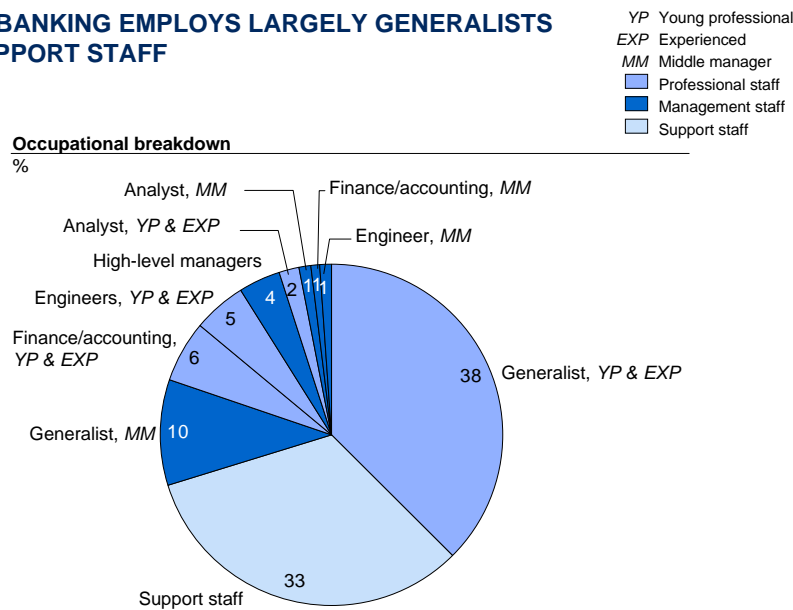


Source: McKinsey Global Institute analysis

- Employment share by occupation.** The main occupations in retail banking are generalists and support staff, which together represent approximately 70 percent of employment (Exhibit 4). This high number of employees in support staff is explained by the relatively limited training required for the functions that employ the most people:<sup>6</sup> branch customer-facing functions (e.g., tellers) account for more than 30 percent of the employment (Exhibit 5). In many countries covered in this study, only a high school degree (or technical equivalent) is required to be a teller at a bank. This is particularly true in high-wage countries.

**Exhibit 4**

**RETAIL BANKING EMPLOYS LARGELY GENERALISTS AND SUPPORT STAFF**



Source: Interviews; McKinsey Global Institute analysis

The second broad group of employees are generalists—both young (29 percent) and experienced (10 percent) professionals. These employees serve call centers, corporate back-office, sales (account managers), and product development. Finally, finance and accounting trained professionals, despite making up a small percentage of total employment (about 4 percent) are at the core of the services provided by banking institutions (Exhibit 5).

<sup>6</sup> According to our occupational definition, employees in support staff positions have completed high school degrees and may have any level of work experience.

## Exhibit 5

### THESE OCCUPATIONAL GROUPS ARE DISTRIBUTED THROUGHOUT THE DISTINCT FUNCTIONS

YP Young professional  
EXP Experienced  
MM Middle manager

#### Share of occupational categories per function

| Occupational categories   | Function            |       |           |                 |             |             |     |             | Total in sector |     |
|---------------------------|---------------------|-------|-----------|-----------------|-------------|-------------|-----|-------------|-----------------|-----|
|                           | Product development | Sales | Marketing | Service/support |             |             | G&A | Internal IT |                 |     |
|                           |                     |       |           | Branch          | Back-office | Call center |     |             |                 |     |
| • Professional staff      |                     |       |           |                 |             |             |     |             |                 |     |
| – Engineer, YP            |                     |       |           |                 |             |             |     | 29          |                 | 2   |
| – Engineer, EXP           |                     |       |           |                 |             |             |     | 45          |                 | 3   |
| – Finance/Accounting, YP  |                     |       |           |                 | 15          |             |     | 5           |                 | 3   |
| – Finance/Accounting, EXP |                     |       |           |                 | 13          |             |     | 18          |                 | 3   |
| – Generalist, YP          | 10                  | 5     | 13        | 23              | 20          | 69          | 10  |             |                 | 29  |
| – Generalist, EXP         | 26                  | 16    | 25        | 2               | 12          |             | 17  | 4           |                 | 10  |
| – Analyst, YP             | 5                   |       | 8         |                 |             |             |     |             |                 | 1   |
| – Analyst, EXP            | 26                  |       | 25        |                 |             |             |     |             |                 | 2   |
| • Management staff        |                     |       |           |                 |             |             |     |             |                 |     |
| – Engineer, MM            |                     |       |           |                 |             |             |     | 12          |                 | 1   |
| – Finance/Accounting, MM  |                     |       |           |                 | 5           |             | 5   |             |                 | 1   |
| – Generalist, MM          | 5                   | 10    | 5         | 15              | 5           | 20          | 5   |             |                 | 10  |
| – Analyst, MM             | 5                   |       | 5         |                 |             |             |     |             |                 |     |
| – High-level manager      | 3                   | 4     | 4         | 3               | 5           | 5           | 5   | 4           |                 | 4   |
| • Support staff           | 20                  | 20    | 15        | 57              | 25          | 6           | 35  | 6           |                 | 33  |
|                           | 100                 | 100   | 100       | 100             | 100         | 100         | 100 | 100         |                 | 100 |

Source: Interviews; McKinsey Global Institute analysis

### Sector employment projections, 2004–2008

Employment in retail banking is projected to decrease at the rate of 0.6 percent annually for the years 2004–2008 (Exhibit 6), reaching a worldwide employment demand of 12.7 million people in 2008. These values were derived by individual analysis of the retail banking employment for the period of 1994–2003 and of the underlying trends driving changes in employment of 11 countries. Of these 11 countries directly analyzed, only three (United States, Canada, and Ireland) showed growth in employment. All other countries showed a decrease in employment. The major factors associated with this decrease and which are projected to continue to impact employment in the sector are consolidation, outsourcing, and technological improvements:

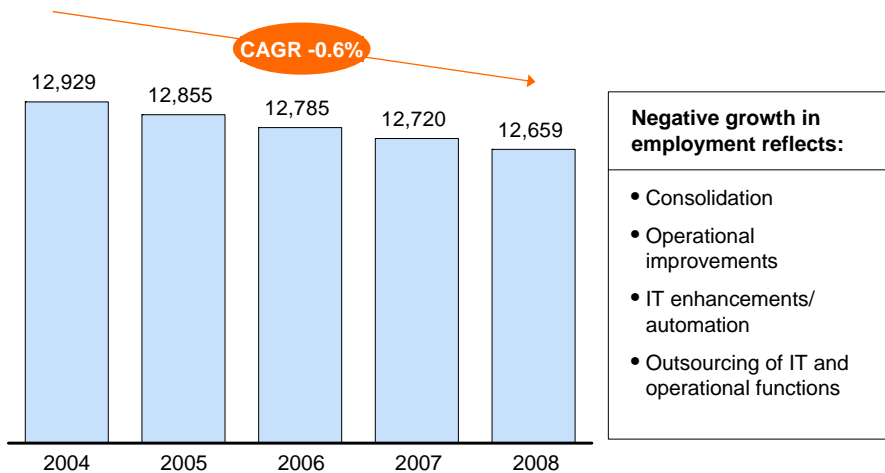
- *Consolidation.* Financial institutions have merged in both developed and developing countries. In most cases consolidation results in a decrease in employment in the sector, a reduction that can be dramatic. As an example, in the Brazilian retail banking sector, between 1994 and 2002 the market

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## Exhibit 6

### EMPLOYMENT IN RETAIL BANKING IS PROJECTED TO DECREASE MODESTLY IN THE NEXT FIVE YEARS, REACHING 12.7 MILLION EMPLOYEES BY 2008

2004–2008, thousand



Source: McKinsey Global Institute analysis

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share of the top 10 players increased from 66 percent to 78 percent and employment dropped at the rate of 4.3 percent annually, resulting in the loss of 169,000 jobs or 30 percent of the total number of 1994. The phenomenon of consolidation was also observed in the US market, where share for the top 10 players increased from 23 percent in 1994 to 43 percent in 2004. In this case, however, employment grew 3.4 percent annually resulting in an additional 411,000 jobs. The main explanation for the difference is that in developing countries, several of the banks bought were inefficient (many were government owned) and were primed for operational restructuring.

- *Outsourcing of internal IT functions and of specific G&A functions.* Several banking institutions have pursued the outsourcing of these functions to external IT and G&A service providers, and this is likely to continue to grow as cost pressure intensifies. Gartner Research estimates that the retail banking sector outsources approximately 5 percent of its IT workers. In

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addition, banks (as markets mature) also outsource support jobs such as security, cleaning, and transportation.<sup>7</sup>

- *Operational and technological improvements.* The advent of technological advances, especially those associated with automated systems, played a role in reducing the demand for manual labor. Emerging technologies such as voice recognition systems (substituting for call centers) and faster and more secure Internet access will likely continue to reduce employment in the sector.

An example in the United States is Check 21, a federal law designed to enable banks to handle more checks electronically.<sup>8</sup> Banks can capture a picture of the front and back of the check along with the associated payment information and transmit this information electronically. This process enables banks to reduce the cost of physically handling and transporting original paper checks, which can be expensive. It should be noted, though, that approximately 300,000 employees in the United States work in check processing (of a total 2.3 million employees in the United States). It is unclear what impact Check 21 will have on employment in the sector.

### **Changes in assumptions that could alter projected employment**

The factors discussed earlier have affected retail banking in most countries except China. China is responsible for approximately 10 percent of the total employment in the sector. Most of this employment is concentrated in three government owned banks. Regulatory barriers impede competition.<sup>9</sup> As the country is set to open up its financial markets in 2007, significant changes in the landscape are bound to happen thereafter. While the factors described previously—associated with changes in employment in many markets—have been taken into account in the projections made in the study for employment in 2008, we believe that if these changes in China are implemented faster than

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<sup>7</sup> To avoid double counting, outsourcing of this type is covered in relevant cases such as the IT services.

<sup>8</sup> The Federal Reserve Banks, Check clearing for the 21st century act. Accessed May 6th 2005 <http://www.federalreserve.gov/paymentsystems/truncation/faqs2.htm#ques1>

<sup>9</sup> The foreign policy center. Roundtable on China's financial services industry: Opportunities and challenges in the second phase of WTO implementation, Beijing, October 30, 2004; [www.fpc.org.uk/fsblob/347.pdf](http://www.fpc.org.uk/fsblob/347.pdf). Accessed April 21st , 2005.

anticipated, worldwide employment could fall further than our forecast. Sensitivity analysis, however, indicates that a decrease of an additional three percentage points in employment in China<sup>10</sup> (the value currently estimated for the 2004–2008 period is a 3.6 percent fall per annum) would only marginally alter our global resourcing projections.

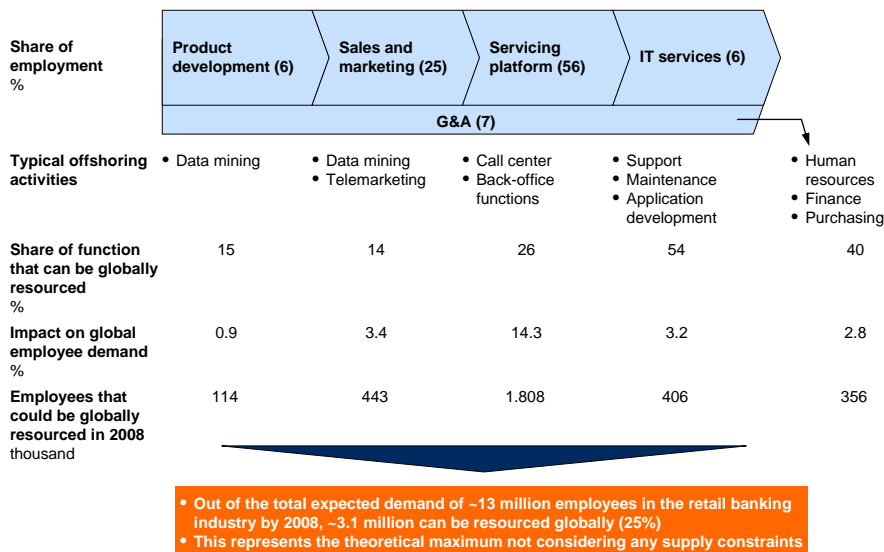
## GLOBAL RESOURCING POTENTIAL

### Theoretical maximum

Of the expected demand of approximately 12.7 million employees in the retail banking sector by 2008, 25 percent of the jobs in the sector, representing approximately 3.1 million employees, may be resourced globally (Exhibits 7-9), given suitable tools and processes design, as well as sufficient quantity and quality of labor supply.

### Exhibit 7

#### A MAXIMUM OF ~25% OF THE EMPLOYMENT DEMAND IN RETAIL BANKING IS GLOBALLY RESOURCEABLE, TRANSLATING INTO ~3.1 MILLION FTEs BY 2008

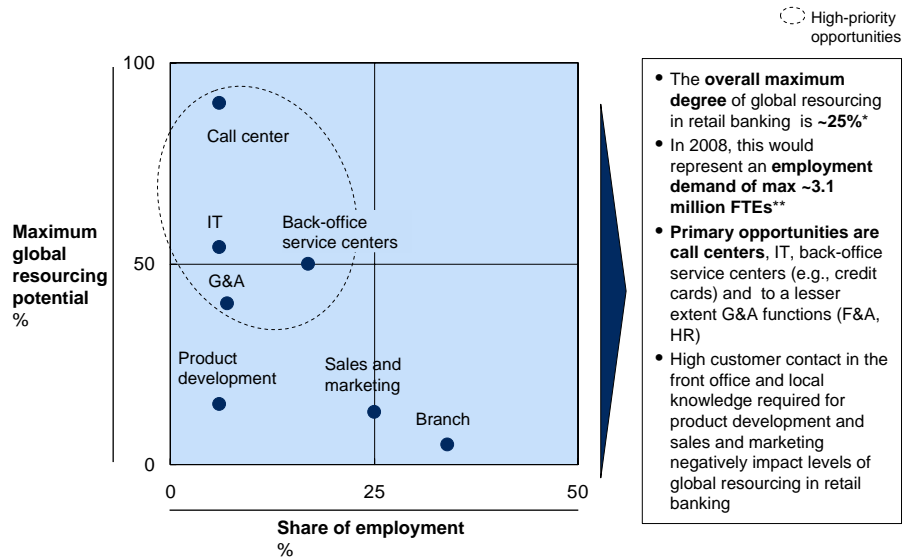


Source: Interviews; McKinsey Global Institute analysis

<sup>10</sup> Thus taking the decrease to 6.6 percent, the top value observed for decrease in employment over a five-year period in any of the countries studied.

### Exhibit 8

## CALL CENTER, IT, AND BACK-OFFICE SERVICE CENTERS ARE THE PRIME GLOBAL RESOURCING OPPORTUNITIES

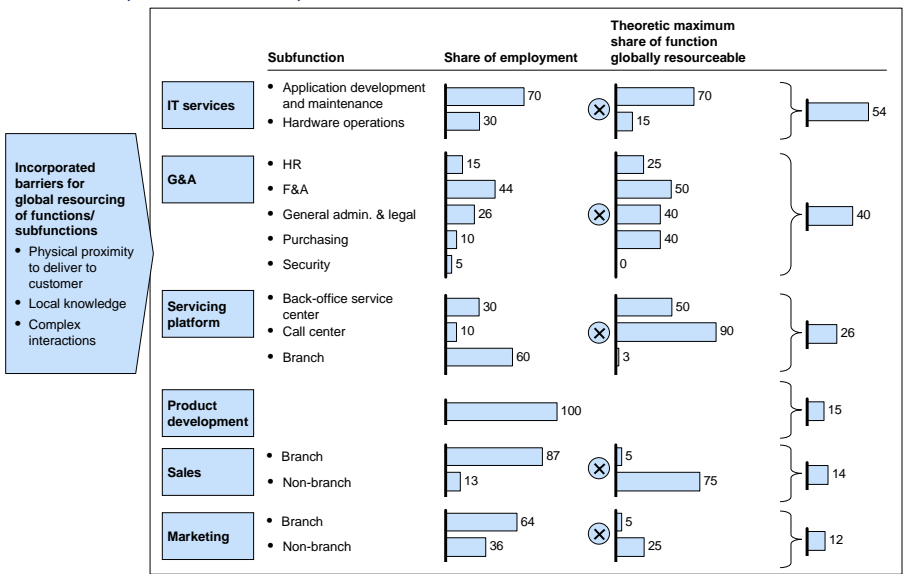


- The overall maximum degree of global resourcing in retail banking is ~25%\*
- In 2008, this would represent an employment demand of max ~3.1 million FTEs\*\*
- Primary opportunities are call centers, IT, back-office service centers (e.g., credit cards) and to a lesser extent G&A functions (F&A, HR)
- High customer contact in the front office and local knowledge required for product development and sales and marketing negatively impact levels of global resourcing in retail banking

\* Theoretical maximum not considering supply constraints.  
 \*\* Not including any markup to acknowledge capital/labor substitution.  
 Source: Interviews; McKinsey Global Institute analysis

### Exhibit 9

## FUNCTIONS MORE CONDUCTIVE TO GLOBAL RESOURCING ARE CALL CENTERS, IT SERVICES, AND BACK OFFICE



\* Theoretical maximum not considering supply constraints or lower actual pace of adoption.  
 Source: Interviews; McKinsey Global Institute analysis

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- **Factors that affect theoretical maximum.** The theoretical maximum potential in retail banking is a reflection of the dampening effects of the high requirements for physical presence at the branch and the requirement for local knowledge within the sector, balanced by the high maximums for IT services, G&A, and back-office services:
    - *Physical presence required to deliver to customer.* High levels of employment in bank branches reduce the theoretical maximum of the sector.
    - *Local knowledge required.* Local knowledge is required for many functions in retail banking, such as product design, marketing, accounting, and some legal functions. For example, despite being worldwide players, banks such as ABN-AMRO, HSBC, and Santander adjusted their product portfolios to the requirements of local markets as they developed their Latin American expansion through the purchase of banks in Mexico and Brazil.
    - *Complex interactions required to create service.* Although these are the least important of the limiting factors for this sector, complex interactions are required in banks both at the strategic level (high-level managers) and in the coordination of information at medium and low levels. As one interviewee commented, "in all branches there is a group of activities—situations such as the death of a client—that need to be handled locally and immediately."
  - **Functions amenable to global resourcing.** Primary opportunities include call centers, IT functions, back-office service centers, and to a lesser extent G&A functions such as finance and accounting, and human resources (see Exhibits 8 and 9):
    - *Call centers.* Call centers are, as a function, and from a technological point of view, the strongest candidates for global resourcing. However, it is important to note that the inbound (approximately 80 percent of calls) and the outbound (approximately 20 percent) sections of a call center have different goals and consequently different potentials. The inbound call section, which deals with simple issues, ranging from address changes to fund verification, have the potential to be 95 percent globally resourced. The outbound section of a call center is a part of a bank's client relationship management and is thus a key area of customer contact.

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Consequently, it must be more sophisticated as it seeks to sell products. In this case, local knowledge, cultural fit, and in some cases the placement of the call by a branch employee (whom the client may later meet to discuss products in person) have been demonstrated to improve the chances of a call's success.

Furthermore, several countries restrict outgoing calls. In the United States, customer privacy protection laws (also known as "do not call" lists) impose limitations on calling customers. In addition, in general it is high-net-worth individuals, who tend to avoid going to branches, who most use call centers for routine issues. Given the legal restrictions and overall lack of success of telemarketing (i.e., outgoing call centers), many players see this call as an opportunity to cross-sell. Thus, what was meant to be an inbound call center, performing simple functions, requires more highly qualified and local staffing, so that it performs a dual function as a cross-sell agent. As one interviewee put it, "the cost saving potential of an offshore location is irrelevant in comparison to the cross-selling potential when a customer called to talk to you and has allocated time to do so."

- *Internal IT.* Internal IT functions (54 percent theoretical maximum) are also conducive to global resourcing. Responsible for 5 percent of the employment in retail banking, IT services is the function with the highest theoretical maximum. Application development and maintenance that does not require client contact may be globally resourced. Some hardware operations are also subject to global resourcing. It is important to note, however, that several players tend to pursue outsourcing opportunities before they pursue global resourcing opportunities. As a consequence, global resourcing of IT functions in retail banking is likely to appear within the global resourcing of IT service companies as these are often recipients of the jobs transferred out of the banks' onshore captive IT centers.
- *Back-office service centers.* Back-office service centers have a high potential (50 percent). Within the back-office, data entry functions, work related to analytical tasks, statement production, and financial calculations are responsible for a significant amount of employment—most of which can be done remotely. On the other hand, 20–25 percent of the back-office work is (as described by an interviewee) "esoteric, highly fragmented, and

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with no standardization." This refers to balancing tellers, balancing ATMs, managing accounts under judicial scrutiny, and dealing with accounts after the death of a client. In these cases, local presence is necessary.

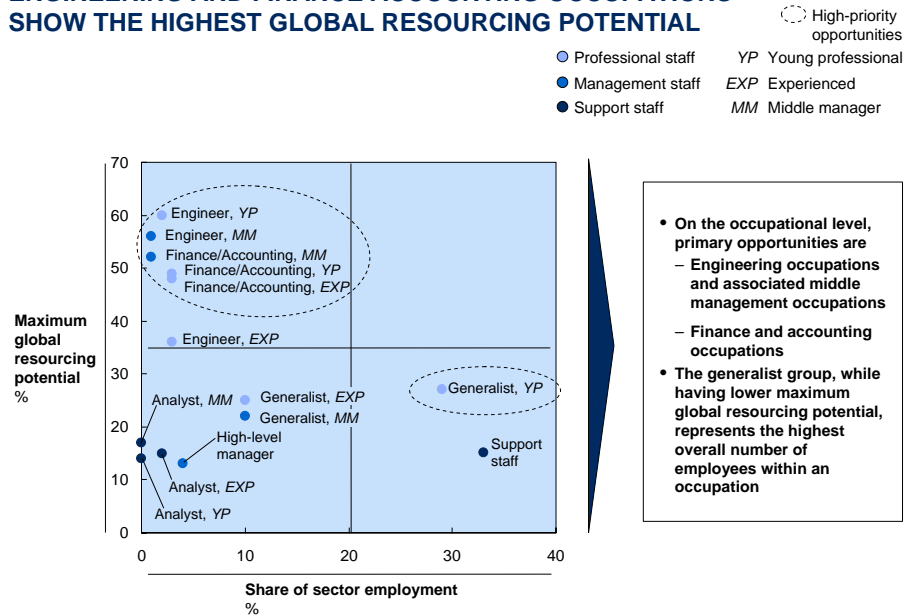
- *G&A*. Within G&A (40 percent theoretical maximum), jobs associated with general accounting, purchasing, and HR (timesheets, payroll, appraisals, training plans) may generally be located anywhere in the world. The increasing need for financial and legal compliance (such as that associated with IASB and Basel II) also represents an opportunity as several new regulations obey worldwide standards and are more related to analytical functions than to local knowledge. Even the compliance with Sarbanes-Oxley could potentially be done remotely, provided proper training. High-level accounting, local HR functions (e.g., recruiting), local purchasing, and especially legal activities show lower theoretical maxima.

The highly customer-facing functions of the branch limit the overall global resourcing theoretical maximum of the sector. Other local knowledge intensive functions such as sales and marketing also help limit the theoretical maximum. Within marketing, campaigns and other activities require local knowledge of the markets where banks operate. In these cases non-branch sales positions, particularly those associated with telemarketing, data mining, and analysis, can be performed from a remote location. Finally, product development, responsible for 6 percent of employment in the sector, is one of the functions with the lowest global resourcing theoretical maximum. Again, this is a result of the importance of local knowledge regarding market conditions and legal barriers for the development of products. In general, only the detailing of the product characteristics is globally resourceable.

- **Occupations amenable to global resourcing.** Directly derived from the functions, the primary occupations that may be globally resourced are generalists, IT engineers, and finance and accounting professionals (Exhibit 10):
  - When considering the occupations with the highest theoretical maxima for global resourcing, engineers and analysts top the list at an average of 50 percent of the positions these professionals hold. However, the low percentage of employees in these functions translates to a total of

## Exhibit 10

### ENGINEERING AND FINANCE ACCOUNTING OCCUPATIONS SHOW THE HIGHEST GLOBAL RESOURCING POTENTIAL



Source: Interviews; Press releases; McKinsey Global Institute analysis

approximately 760,000 positions that could be globally resourced (considering young and experienced professionals and the associated management positions).

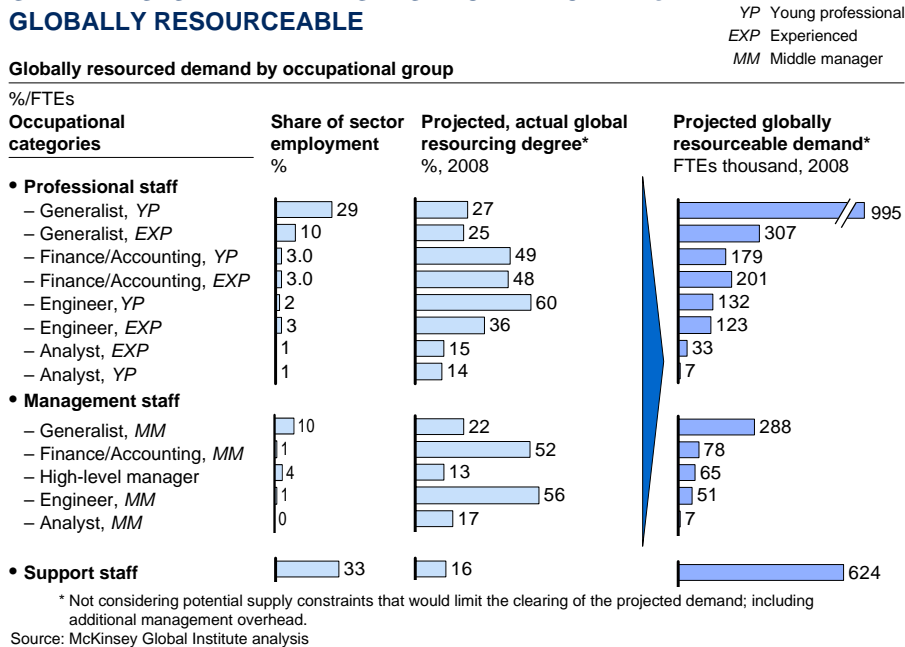
- Generalist positions average an approximate 25 percent global resourcing theoretical maximum. However, given the high percentage of employees in these occupations, 1.5 million generalist positions may be globally resourced, representing half of the total potential of the sector.
- Finally, approximately 600,000 support staff positions could be globally resourced. These may be described as "follower positions" in that, true to the concept of support staff, their global resourcing is dependent on the movement of the "leading positions" such as the IT engineers, the call center attendants, or the back-office analysts (Exhibit 11).

#### Change in assumptions that could alter projected theoretical maximum

The evaluation of the sector already considered that several developing markets are evolving to the operational efficiency of developed markets. As such, it considered the inefficiencies present in developing markets in 2003 and

**Exhibit 11**

**GENERALISTS HAVE THE HIGHEST NUMBER OF FTEs GLOBALLY RESOURCEABLE**



predicted a drop in employment likely to occur as a result of automation, consolidation, and outsourcing—particularly of IT functions. Consequently, it is unlikely that these factors will play an additional role in the projected demand for globally resourced positions.

The one exception is the increase of telebanking and Web-based banking. Should telebanking increase at a rate higher than predicted in this study, it would affect to a lesser extent the functional breakdown and to a greater extent the occupational breakdown we presented. The impact would be a decrease in the number of tellers, but this would not affect the theoretical maximum, as tellers are positions that are not globally resourced. It could potentially increase the need for call center agents and IT personnel. However, both telebanking and Web-based banking have been available for several years and in the recent past the increase in the pace of adoption of these technologies has been constant, growing at about 30 percent a year, leading us to conclude that no major unpredictable changes are likely to happen in the next five years. Therefore, demand trajectories are likely to remain unchanged.

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### **Near value chain spillovers**

In most countries banks are universal. As players adopt global resourcing practices for their retail banking business, they are likely also to take a similar approach to their wholesale and insurance businesses (in fact using the same setup). As insurance business units are typically conservative, it is likely that the retail banking business units will lead the way. A few banks have globally resourced wholesale bank business units first and the retail bank business unit second.

## **DEGREE OF ADOPTION OF GLOBAL RESOURCING**

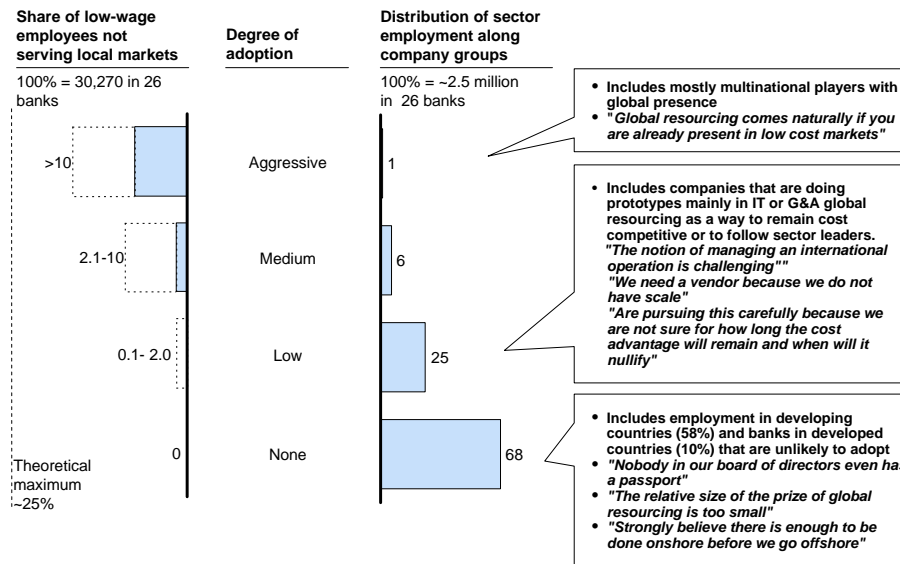
### **Current degree of global resourcing**

Despite the 25 percent theoretical maximum for global resourcing in retail banking, currently, approximately 2 percent of the positions in high-wage countries are being sourced from low-wage countries. This number, however, needs to be interpreted with care given the breakdown of players within the industry and the likelihood that each group of banks will adopt:

- Of the total employment in the industry, 58 percent of the positions are in low-wage countries. We found no cases of global resourcing in retail banking in these countries and believe this is the case because of the lack of cost savings global resourcing offers (Exhibit 12).
- Within high-wage countries, players may be further subdivided according to the geographical reach of their businesses. These fall into regional/local, national, and multinational players:
  - For the purpose of this study, regional/local players are defined as those with presence limited to specific cities or portions of a country (e.g., most credit unions). These players usually have few branches and the corporate centers generally are already centrally organized.
  - National players are defined as those with a countrywide span of activities yet with limited international presence or experience (e.g., Wells Fargo, Wachovia). These players pursue organizational and operational improvements in models very similar to global resourcing: moving jobs to low-wage locations within the same country of origin is quite common

## Exhibit 12

### RETAIL BANKS HAVE A VERY LOW DEGREE OF ADOPTION



Source: Press releases; Company filings; Company Web sites; Techsunite.org; McKinsey Global Institute analysis

practice. For example, a leading US player has moved part of its IT facilities from downtown Manhattan to New Jersey. Yet, even these traditionally national players are starting to participate in the global resourcing arena, particularly by leveraging IT services and call center vendors located abroad.

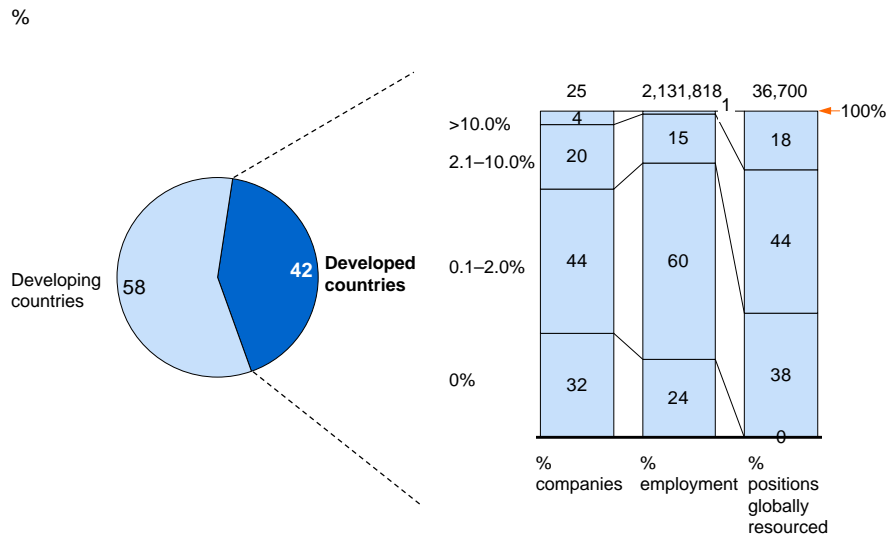
- Multinational players are defined as those with international presence, regardless of the number of clients or the percentage of assets outside their home country (e.g., HSBC, Citibank). These players are the ones that have largely pursued global resourcing. In some cases, the offshoring sites are continents apart as is the case with Citibank's Bangalore site. Sometimes the operation is better described as nearshore, like Deutsche Bank's operations in the Czech Republic.
- Despite the recent media coverage suggesting that a large portion of financial services employees are already located offshore or soon will be, analysis of the global resourcing activities pursued by players in high-wage countries (based on publicly available data regarding a sample of 25 banks) shows that eight of the 25 players (responsible for 23 percent of employment) in our

sample have not pursued global resourcing. Eleven players (60 percent of the employment) have globally resourced less than 2 percent of their positions, while five players (15 percent of employment) have globally resourced between 2 percent and 10 percent of their positions and one player (1 percent of the employment) has globally resourced more than 10 percent of its positions (Exhibit 13). Extrapolated to the subsector (i.e., all players in developed countries) the degree of global resourcing averages approximately 2 percent of the total employment of the banks in high-wage nations.

- Primary engagements so far have been in internal IT, call centers, and back-office functions mostly at captive centers in India and to a lesser extent Eastern Europe. For the major players, as competitive pressure intensifies and, more importantly, their experience with managing a global R&D footprint grows, individual pace of adoption is likely to increase.

**Exhibit 13**

**EVEN WITHIN DEVELOPED COUNTRIES, NOT ALL PLAYERS ARE ADOPTING**



Source: The Banker; Hannover; press releases; Company Web sites; McKinsey Global Institute analysis

## Exhibit 14

### INHIBITORS STILL OUTWEIGHT DRIVERS IN THE ADOPTION OF OFFSHORING IN RETAIL BANKING

|  | Drivers/inhibitors   | Importance for sector degree of adoption |
|--|--|--|
| Sector characteristics and dynamics                | • Cost pressure  | +  |
|  | • <b>Cost differential (perceived or real)</b>   | ++                                       |
|  | • Availability (perceived or real) of quality vendors  | -  |
|  | • Availability (perceived or real) of suitable labor   | -  |
| Organizational, operational, and technical factors | • <b>Global presence and experience in managing global footprint</b>   | ++                                       |
|  | • Scale of business processes to be globally resourced   | +  |
|  | • <b>Suitability of process to support global resourcing</b>   | --                                       |
|  | • Intensity of paper-based processes in sector   | -  |
|  | • Suitability of IT to support global resourcing   | -  |
|  | • Alignment of management incentives with profit maximization  | -  |
|  | • Comparison of global resourcing Return On Investment (ROI) (perceived or real) with alternative profit-maximization strategies | -  |
| Legal, regulatory, political, and social factors   | • Access to attractive markets   | ∅  |
|  | • Social/political position towards global resourcing  | ∅  |
|  | • Labor market regulation in the home country  | -  |
|  | • Product market regulations in the home country   | ∅  |
|  | • Intellectual Property (IP) regulation in the producing country   | ∅  |

+++ Strong driver  
 ∅ Neutral  
 --- Strong inhibitor

Source: Interviews; McKinsey Global Institute analysis

### Determinants of degree and pace of adoption

By mapping the drivers and inhibitors of global resourcing we can better explain the retail banking sector's current degree of adoption. These determinants fall into three broad groups referring to (1) industry characteristics and dynamics; (2) operational, technical, and organizational trends in the sector; and (3) regulatory, political, and legal factors affecting the sector (Exhibit 14). Banks adopt offshoring to contain costs; however, the scale of business processes, the need for process and IT reengineering, and the prioritization of other opportunities markedly reduce the degree of adoption.

- **Sector characteristics and dynamics:**

- *Cost pressure.* The main driver for banks moving operations has been increased cost pressure. Banks that are not suffering intense cost pressure are less prone to consider global resourcing. (In fact, most banks we studied were not under significant cost pressure.) Even within a single

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bank, business units with tighter margins tend to consider global resourcing earlier. A prime example is the use of offshore locations for mortgage handling. One expert commented that "mortgage operations have razor thin margins. A bank will do almost anything to pick up a few more points."

- *Cost differential (perceived or real).* For banks that consider global resourcing, it is important that there be a significant cost differential between the original location of operations and the new location of operations. Thus, global resourcing ends up being a solution applicable mostly for banks in high-wage countries.
- *Availability of quality vendors.* Several players have expressed concerns regarding quality at offshore sites. This is particularly true if the vendor is providing a service that contacts the bank's customers (such as call centers). While the vendor base has increased very fast in IT services, there is less confidence that there are mature and suitable vendors for other functions such as back-office or G&A. A move by large industry players might provoke confidence and follower reactions.
- **Organizational, operational, and technical factors.** Real or perceived operational and technical difficulties are inhibitors to global resourcing for banks that consider pursuing it:
  - *Global presence and experience in managing global footprint.* Players that already have a presence in a country where global resourcing may occur tend to move more easily into global resourcing by tapping into existing management teams to set up the centers, acquire the right talent, and oversee operations. As one interviewee said "we are in the country anyway... Our existing presence equals existing management." For national and local players, the simple notion of managing an international operation is challenging, as no previous experience exists. One of our interviewees commented "in our board of directors nobody even has a passport... How can we think of doing anything abroad?"
  - *Scale of business processes to be globally resourced.* An additional important factor is the need for scale. Given the initial investment

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necessary to set up captive centers, or the cost and time needed to negotiate with vendors, it is important that a significant volume of business be amenable to movement to offset initial set up costs. Consequently, smaller/local banks are less likely to move call centers or back-office functions on their own.

- *Suitability of process to support global resourcing.* For many players, the intricate operations of several of their BUs ultimately becomes an inhibitor as these players have difficulty separating out portions of functions that can be moved. This is particularly true when a bank grows through mergers and acquisitions. In these cases banks have a diversity of products and systems requiring reengineering in order to move. The legacy systems of the purchased banks remain, and players opt not to pursue changes, which then become inhibitors to global resourcing.
- *Intensity of paper-based processes in sector.* Particularly in the back office, banks have historically had a large paper trail—ranging from paper mail to check processing to account- or credit-related applications. Improvements are possible through the use of advanced imaging technology. However, not all players have the necessary infrastructure.
- *Alignment of management incentives with profit maximization.* Management has a strong impact on whether global resourcing is pursued when it is a convenient and reasonable option. Management commitment is necessary to overcome the operational difficulties in the setup of a captive center or to push through negotiation with vendors. In these cases, strong leadership defines the path: "Nobody doubted it when Jack Welch said that GE was setting up a center abroad," commented an interviewee. Consequently, global resourcing within some companies will require a change in mind-set. One expert commented that "offshoring is not one of the five most important items in the top management agenda."
- *Comparison of global resourcing return on investment (ROI) (real or perceived) with alternative profit maximization strategies.* As players suffer cost pressures, they react by seeking improvements. Yet there are two schools of thought on how to pursue a portfolio of improvement opportunities. In the first, there is a belief that whatever may be done onshore has to be pursued before anything goes offshore. In these cases

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players stagger the processes: first they seek operational improvements such as the centralization of back offices, before considering global resourcing. In the second school of thought, players use global resourcing as a catalyst to seek change. In these cases, players "parallel process" the improvements—they identify where the opportunities are while at the same time mapping which of those could benefit from global resourcing.

- **Legal, regulatory, social, and political factors.** The main problem openly faced by players in this arena is the social and political pressure applied to players by their communities and governments. Additional legal issues are rare but play a role in a few countries:
  - *Social position toward global resourcing.* Local and national players are often associated with the communities where they started. These players adopt a "pillar of the community" stance and seek to avoid the disapproval of their customers. In many cases, players seek to address cost-cutting needs through local employment changes and negotiation (e.g., increase in weekly hours) before considering offshoring. One player stated, "Offshoring is inconsistent with our values."
  - *Political position toward global resourcing.* It is observed that in countries such as the UK where the government has openly declared that "offshoring is a business problem and not a government problem," the degree of adoption by the players is higher and information is publicly available. In countries such as the United States, players are quite secretive about their movements. In fact, one player appeared to oppose global resourcing in public while offshoring certain functions. "Politics get in the way... but it gets removed quickly... Appetite for offshoring is more significant today than it was three months ago," commented an expert.
  - *Labor market regulations in the home country.* Rigid labor laws in some developed countries (particularly in Germany) prevent a more rapid large-scale global resourcing.
  - *Product market regulations in the home country:* Restrictions regarding the storage of financial information outside a country's borders were observed in a few of the countries evaluated, particularly in Eastern Europe.

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## Pattern of adoption

In the process of adopting global resourcing, organizations face the barriers previously described. Some of these barriers, such as a lack of quality vendors, are easier to overcome; others, such as labor market rigidities or potential regulatory barriers, may be considered hard barriers:

- Barriers that can be more easily overcome are the suitability of processes, management incentives, availability of quality vendors, and the scale of business processes to be offshored:
  - Multinational companies are more likely to continue implementing global resourcing either by starting new centers or by expanding their existing centers. For these players, performing certain functions from low-wage locations seems to be a logical step in the same global direction they have been pursuing for years.
  - Most of the inhibitors to global resourcing by these large retail banks are operational and relate to suitability of processes. Classic examples are legacy products—products that were transferred when mergers took place. The processes that handle these products vary widely. In addition, the low scale of the legacy products diminishes potential returns. With time, banks tend to phase out these products and are left with a more homogeneous portfolio, making adoption easier.
  - As for management incentives, our research does not suggest the existence of players that follow a completely different strategic direction from each other. They merely differ in their pace of adoption. As such, the increase in successful cases of retail banks that have adopted leads us to predict that followers will benefit from the experience of early adopters.
  - For smaller players we believe that the use of vendors offers a viable differentiation strategy. This process would mimic one of the multiple examples all over the developed world, where local, small- to medium-size players outsource activities (particularly IT) to local players that are able, in this format, to gather the necessary scale to offshore and pass on the savings to their customers. In fact, large IT services vendors already offer their clients the option to have projects performed onshore or offshore at different price levels.

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- Labor market rigidities and potential regulatory barriers are considered the hardest to overcome:
    - Some countries have regulatory barriers that inhibit pace of adoption. Most of these refer to the supply of financial data outside the home market. Yet it is recognized that offshoring involves primarily low-risk IT work but also some higher-risk, customer-database-type work, including loan servicing and customer assistance/help-desk services. As more offshoring occurs, in addition to improved security measures on the part of players and vendors, regulatory agencies are providing the necessary advice on mechanisms to be put in place by the banks to mitigate any risk associated with offshoring. An example of this is a recent publication by the FDIC providing guidance to financial institutions as to how to mitigate risks associated with offshoring.<sup>11</sup>

### **Projected growth in adoption**

Given the current growth of globally resourced positions in retail banking of 24 percent p.a., by 2008 approximately 2.4 percent of worldwide employment in retail banking-translating to 303,000 jobs-will be globally resourced. This represents an additional 210,000 jobs over the 2003 levels (Exhibit 15). As discussed earlier, the players likely to adopt are multinational players. For high-wage countries, we project that approximately 5.4 percent of employees will be located remotely. This translates to tripling the number of employees currently globally resourced within five years. This expansion should continue mostly in traditional areas such as IT services, call centers, F&A, HR, and other back-office processes.

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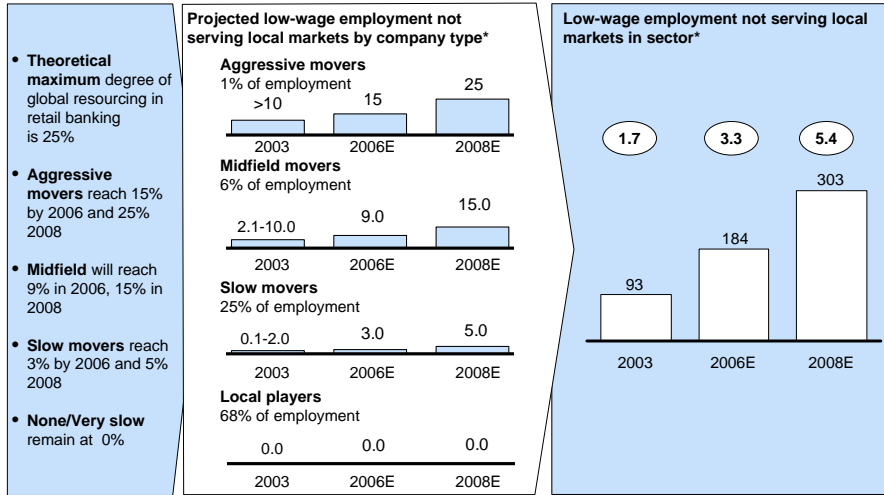
<sup>11</sup> Offshore outsourcing of data services by insured institutions and associated consumer privacy risks. FDIC. June 2004; <http://www.fdic.gov/regulations/examinations/offshore>.

## Exhibit 15

### BY 2008, ABOUT ONE FIFTH OF THE MAXIMUM GLOBAL RESOURCING POTENTIAL IN RETAIL BANKING WILL BE EXPLORED

FTEs, thousands

○ Share of high-wage employment demand covered



\* Not considering supply constraints or potential markup to account for increased service levels or increased management overhead.

Source: Interviews; press search on company plans; Company press releases; McKinsey Global Institute analysis

## IMPLICATIONS

Global resourcing is already impacting players and the competitive arena of the retail banking sector. At a company level, players need to address their organizational strategy. Given the need for disaggregation of the value chain to be able to offshore, companies might need to redesign processes to pursue this opportunity. As it is usually seen, it is the centralized functions, such as call centers, payroll, and benefits, which are most easily offshored. As other cost containment opportunities are fully tapped, companies should start considering offshoring in the face of other cost-reduction alternatives such as automation.

The opportunity to leverage low-wage labor pools is providing the retail banking sector with a wide range of opportunities from the obvious cost reduction for call centers and back-office functions to the creative use of technology and knowledge to provide unique products to their customer base. Low-wage labor allows retail banks to enhance revenues by pursuing opportunities deemed, in the past, to be unjustifiably expensive. Other activities, such as state-of-the-art

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micro-marketing deemed cost prohibitive in high-wage locations, may be done for a fraction of the cost offshore. Finally, global resourcing opens the possibility for more customized services, such as private financial advisors for customers with balances below the traditional cutoff point for private banking.

From a sectoral perspective players who have adopted global resourcing have already seen improvements in their cost-to-income ratios. As a consequence, as the leaders increase offshoring, players in high-wage locations that are not currently offshoring, will likely have to in order to remain competitive.

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## Methodology

### EMPLOYMENT

**Functions.** Sectors were broken down along their value chains, resulting in functions and subfunctions. These breakdowns are sector specific. However, several functions (e.g., R&D, sales and marketing, IT, and G&A) appear across sectors. Other functions, such as nursing, are sector specific.

**Occupations.** Employees in specific occupations perform tasks in the above functions and subfunctions. For the purpose of this study, nine broad occupational groups were defined based on their required educational background.

Double counting of employment was avoided by considering only the employees who are directly employed in companies in that sector. Outsourced employment is not considered within the sector being evaluated but rather in the recipient sector (e.g., outsourced IT services employees in retail banking are included in the IT services sector analysis).

### GLOBAL RESOURCING POTENTIAL-THEORETICAL MAXIMUM

Theoretical maximum describes the percentage of a function or subfunction that may be globally resourced in the absence of supply constraints. To construct the theoretical maximum of each function or subfunction, we determined the percentage of the positions that could potentially be performed anywhere in the world.

**Factors that affect theoretical maximum.** Three factors explain why a function cannot reach a 100% theoretical maximum: physical presence, local knowledge, and complex interactions are required to some extent in each sector.

### DEGREE OF ADOPTION

Degree of adoption assesses the current and projected levels of global resourcing from low-wage locations within a sector.

**Determinants of pace of adoption.** Three broad categories of determinants were identified: (1) sector characteristics and dynamics, (2) operational, organizational, and technical factors, and (3) legal, regulatory, social, and political factors.



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