



Could financial services companies create a competitive advantage through a good sourcing strategy?

Technology Strategy & Architecture – Business of Technology

Times of change in the financial services industry

Uncertainty. A word that captures the current environment for financial services (FS) companies in the UK. Brexit, tighter regulations and security requirements and the rise of FinTechs all contribute to the ever-changing FS industry, and the resulting pressure on profit margins. Additionally, customers have increasingly digital needs and expect speed, flexibility and easy-to-use services. This is forcing corporations to innovate from within, to build their capabilities to support new technologies. Ten years ago, competitive advantage could be achieved by embracing innovations already underway. This reactive approach is no longer enough to maintain competitiveness and stay ahead of the game.

Every FS business is a technology business

The FS industry is not the only thing that is changing nowadays. *Cloud, Blockchain, Cognitive*, etc. are terms that were rarely part of regular conversations ten years ago but now seem to find their way into working vocabulary on a daily basis. These are already revolutionising the way that businesses operate by challenging existing processes and allowing businesses to connect with customers in ways that were previously unheard of. For example, the customers of retail banks can interact through chat bots instead of being 'forced' to visit their local branch.

Interestingly, there seems to be an intrinsic bidirectional link between the changing business environment and disruptive technologies. An increasingly competitive environment forces FS companies to innovate and discover new technologies and the technologies themselves drive changes to the industry via new digital customer expectations, such as the expectation of interacting exclusively with your bank through the mobile app.

How the new paradigm is affecting sourcing decisions in FS companies

Financial Services, EMEA's largest outsourcing industry, generated a total contract value of £4.8 billion in 2017-2018, almost quadruple the amount reached in the 2015-2016 period¹. However, cost-reduction is no longer considered the most important criterion for outsourcing. Indeed, according to the *Deloitte Global Outsourcing Survey 2018*, the main driver for outsourcing is to enable competitive advantage and it shows how organisations are embracing disruptive solutions to achieve this. There is increased demand for shared services and embedding automation within the organisation, limiting reliance on humans, thereby reducing the scope for errors and increasing compliance.

¹ *Arvato outsourcing index 2015-2018*

Since 2005, sourcing models have shifted from single to multi-sourcing, allowing FS institutions to take advantage of specialist vendors. The challenge now is to strengthen relationships between vendors in the supply chain, in order to ensure seamless and fully integrated service delivery to the business. We are seeing a movement away from static monolithic contract agreements to a multi-vendor environment, where the relationships change over time, providing more agility and flexibility to adjust services and service levels to adapt to changing business needs. We are also witnessing an increase in demand for new service companies, as a response to operational continuity regulation and Brexit uncertainty. These have the skills and resources required to successfully exploit emerging technologies and offer a new wave of disruptive sourcing opportunities for companies without the in-house capabilities to utilise these new technologies themselves.

How a (good) sourcing strategy can help FS companies

It is often the case that some financial institutions fail to allocate sufficient attention and effort into developing and defining a robust sourcing strategy. Some of the main consequences of this are having the wrong services in scope, inappropriate supplier selection, inadequate service performance and increased operational risk. However, a good sourcing strategy can help organisations to navigate through this complex environment and avoid the problems outlined above, providing multiple sources of competitive advantage:

1. Incentivise growth

- Integrate supply chains, with active management of vendors, allowing funds and resources to be invested in revenue-generating business activities instead of supporting functions.
- Help the business to build and manage an efficient innovation ecosystem where the right players operate at the right time with the right arrangements. This will enable the business to introduce disruptive innovations capable of improving the customer experience and the associated revenue.

2. Optimise Cost

- Develop agile and flexible contracts that evolve over time to ensure cost-effective pricing and removing hidden costs.
- Embrace supplier cloud offerings that optimise costs by offering easily available, secure and scalable services without the need for costly up-front expenditure.

3. Minimise Risk

- Shift some risks (investment, talent obsolescence, etc.) to suppliers, allowing firms to focus on their revenue-generating offerings instead of being forced to spend time navigating red-tape.

- Create a robust vendor management framework to minimise the operational risk associated with outsourcing to third parties.

4. Enable successful M&A processes

- Understand the third party contract environment affected by a merger / acquisition, allowing the assessment of contract performance and identification of opportunities for renegotiation or exit.
- Build up new service companies through joint ventures, where the alliances with external vendors can be really fit for purpose where the companies do not have the right level of technical expertise.

5. Transform their Business / Technology

- Ensure faster speed to change through the right contractual mechanisms.
- Utilise suppliers that are experienced in *DevOps* and *Agile* approaches, providing the business with services that are better tailored to their changing needs.
- Shift from the traditional operational SLAs to business outcome metrics, aligning the services to the end customer.

The challenges associated with operating in a rapidly changing business ecosystem is not unique to FS companies, but speed to change, driving a digital agenda and managing the associated risk are important items on the board agenda. Having a good sourcing strategy can help companies to navigate through these challenges and create a sustainable competitive advantage. Now is the time for action.

Investing in a clear sourcing strategy that focuses on managing ongoing supplier relationships and driving commercial value will allow FS businesses to release working capital, reduce operational risk and create a competitive advantage that leads them into the future.

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