

**Further information:**

Simon Katalin
Tel: 887-6676
Fax: 887-7201
e-mail: katalin.simon@kpmg.hu

Budapest, 28 February, 2008

KPO: Outsourcing's third generation comes of age

Knowledge Process Outsourcing becomes a reality; set to be worth US\$5billion in the financial sector alone.

Knowledge Process Outsourcing (KPO) has now come of age, with the market for KPO services in the Financial Services sector alone expected to be worth US\$5billion by 2010, a report from professional services organization, KPMG International reveals. The prediction shows that KPO – seen as the third generation of the outsourcing process – may now be considered a bona fide, mainstream outsourcing option. “Central and Eastern Europe is also expected to be a sought-after location for KPO provider,” Mark Bownas, Head of KPMG’s Sourcing Advisory Practice in the Europe, Middle-East and Africa region commented.

KPO involves outsourcing more highly skilled processes than has previously been the case with other outsourcing methods, basing its appeal on intellectual arbitrage rather than the cost reduction potential of its counterparts. Within the financial sector, KPO has already been used to handle – amongst other things - credit scoring, loss protection calculations and fraud analytics.

KPMG’s view of the potential within this market was revealed in a White Paper launched at the NASSCOM outsourcing industry event in Mumbai. Speaking at the launch, Edge Zarrella, Global Head of IT Advisory within KPMG’s Advisory practice, and a partner in the Australian member firm, said: “Just a few years ago, talk of KPO seemed far-fetched, especially as businesses were still struggling to come to terms with what the earlier forms of outsourcing could do for them. Now, depending on who you believe, it is set to be worth between US\$10billion and US\$17billion in just two years’ time. Our research suggests that KPO in the financial sector alone could be worth US\$5billion by that time. KPO may still only represent a small percentage of the total outsourcing market but, with the financial sector demonstrating just what it can be used for, I think that all of these numbers are set to increase exponentially.”

To better explain KPO, Zarrella cites the hypothetical example of a Wall St equities research firm which is faced with spending US\$250,000 to cover a specific stock when the most it can hope to achieve in revenues from that research is US\$200,000. However, if that research can be outsourced to a KPO provider at a cost of US\$100,000, the operation suddenly returns to profitability. As well as the profit uplift, more of the home office analyst’s time is freed up and can be put to use on even more high-value activities.

With this in mind, the KPMG paper claims that the concepts which were just pipedreams a few years ago could now be very real outsourcing options – and they now represent the third iteration of outsourcing. Outsourcing began with IT Outsourcing (ITO) in the 1980s, when strategies were put in place for third parties to manage IT systems’ maintenance, development and application. In the 1990s, this was followed by Business Process Outsourcing (BPO) which focused on relatively elementary and standardized processes.

Pradeep Udhas, Global Head of KPMG's Sourcing Advisory practice, pointed out: "One of the most surprising aspects of KPO is that it focuses on the high-end activities which were traditionally considered part of a company's competitive advantage. In this regard, this marks a major stepping stone for the outsourcing industry; moving from being at the periphery of the enterprise to the very heart of it. Now it's there, the possibilities are endless."

Endless they may be but – as with any fledgling enterprise – teething problems still abound. Foremost on the horizon, considering the geographical concentration of KPO providers in India, is the weakening of the U.S. dollar against the Indian rupee which is reducing the Indian industry's competitiveness. Of more long-term concern however may be the apparent shortcomings in the KPO providers' legal and compliance departments – which could place valuable intellectual property at risk – and the escalating battle for talent. Due to the highly specialist skills which it offers, there is not the same enormous talent pool available to KPO providers as is the case for BPO or ITO. Therefore, KPO providers may quickly need to adopt recruitment and retention strategies which reflect its qualification and skill set requirements.

If – or when – KPO does realize its full potential, Edge Zarrella reckons that India is unlikely to be the sole player. He explained: "India is by far the dominant force in this area but other countries like Canada, Australia, Singapore, South Africa and parts of the U.K. are now competing for a piece of the action. The current weakness of the dollar against the rupee may help them in this regard but the key factor in locating KPO operations will still be the availability of appropriately qualified and experienced professional staff. Without those talented people, KPO simply cannot exist. Such people – in appropriate locations – will become extremely sought after."

Central and Eastern Europe, and in particular Hungary, is also expected to be a sought-after location for KPO providers. Mark Bownas, partner at KPMG in Hungary and EMA Head of KPMG's Sourcing Advisory Practice said, "Over the past few years, we have seen Budapest establish itself as a regional centre for Business Process Outsourcing (BPO) activities, due to the availability of a highly skilled, multilingual workforce. Those companies with established BPO centers are now starting to replace or supplement the more basic processes with the type of higher value-added roles described in the report. We view this as a positive trend, which will further enhance Budapest's attractiveness as a location for knowledge based services.

KPMG is a global network of professional firms providing Audit, Tax and Advisory services. We operate in 145 countries and have 123,000 people working in member firms around the world. The independent member firms of the KPMG network are affiliated with KPMG International, a Swiss cooperative. Each KPMG firm is a legally distinct and separate entity and describes itself as such.

KPMG in Hungary employs 530 people - KPMG Hungary Ltd. offers audit services, while KPMG Advisory Ltd. offers comprehensive advisory services to Hungarian and multinational companies, government bodies and foreign investors.

© 2008 KPMG Advisory Ltd., a Hungarian limited liability company and a member firm of the KPMG network of independent member firms affiliated with KPMG International, a Swiss cooperative. All rights reserved.