



The Two Billion Dollar (and some more) Giant: Implications of TCS's Insurance BPO deal with Friends Life

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On November 9, 2011, Tata Consultancy Services (TCS) announced that its UK subsidiary, Diligenta, signed one of its biggest deals ever – a huge US\$2.2 billion contract with Friends Life, a UK-based life and pensions insurer. The deal, which will be effective from March 2012, will be spread over 15 years and will transfer administration of 3.2 million policies from Friends Life to Diligenta. TCS also announced that under the terms of the deal, Diligenta will take up responsibility for Friends Life's closed books line of business, together with much of its corporate benefits business. A significant number of the policies will be turned over to TCS's insurance platform – BaNCS. Around 1,900 Friends Life employees will also transition to Diligenta as part of the deal.

Why the Deal Came to Be Signed

While the size of the deal is definitely eye popping, the deal per se is not very surprising to the followers of Friends Life in particular and the Insurance BPO market in general.

Friends Life is the UK operating arm of Resolution plc. It was created in March 2011 when Resolution acquired the life businesses of Axa and Bupa, bringing together operations of all the three companies under the Friends Life banner. In August, Friends Life separated its open and closed book businesses, creating the UK Heritage business to handle the operations of the closed book division. This was a clear indication that Friends Life wanted to treat the two businesses separately and focus on new business acquisition through open policies, without really burdening itself with the operational complexities of its closed books arm. The current deal seems to be a part of this arrangement, where Friends Life clearly endeavors to reduce administrative costs, operational burden, and yet maintain high service standards for clients by turning over the administration of the portfolio to Diligenta.

The deal is also interesting from the point of view of the outsourcing experience that the buyer, its parent company, or its constituent companies, had. In 2008, before Resolution group took over Friends Life in its previous avatar as Friends Provident, the erstwhile Friends Provident outsourced £200 million worth of IT and infrastructure services to IBM. In 2009, AXA Sun Life (one of the companies that merged to form Friends Life in 2011) signed a 15 year, US\$800 million contract with Capita covering 3.2 million policies with Capita. Therefore, it was also reasonable to expect this deal to happen from the point of view of the

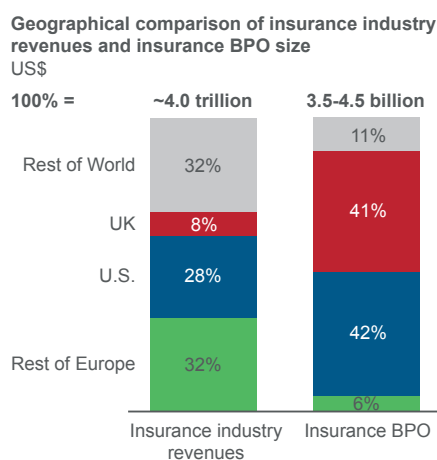
organizational maturity for outsourcing – Friends Life has people who have experience of working in an outsourcing environment and realize the benefits that outsourcing can bring.

Given that insurance BPO is one of the most mature business practices in the UK also helped Friends Life take this step with confidence. Everest Group's research shows that while UK insurance market is only a quarter of the U.S. market, the insurance BPO size is comparable (see **Exhibit 1**). In fact, within the closed book life and pension segment, the UK market is significantly more mature than other markets including the U.S. market.

EXHIBIT 1

Comparison of insurance industry size and contribution to global insurance outsourcing by region in 2010 (US\$)

Source: Everest Group analysis



Why This Deal Is Significant

There are a number of reasons why this deal is significant.

- **Size of the deal.** The deal size itself (US\$2.2 billion spread over a service term of 15 years) is the largest within insurance BPO and amongst the largest within the overall BPO market. This is the second largest deal ever for TCS, which signed its only other larger deal as the US\$2.5 billion acquisition and continuing service agreement with Citibank to acquire its India captive in 2008. The other insurance BPO deals which are comparable to this one, but smaller, are the ones signed by Capita with Prudential plc (worth US\$1.45 billion running over 15 years) and Resolution Life Group (worth US\$1.1 billion running over 12 years).
- **Indian-heritage providers' increased success in mega deals.** This deal signifies the increasing pursuit and success of Indian-heritage providers in mega outsourcing deals. Indian-heritage providers have clearly moved beyond their earlier penetrate and radiate strategy of first starting a deal small and then growing it as the relationship developed over time. With 1,900 employees of Friends Life now moving to Diligenta, the deal also signified the increasing willingness of Indian-heritage service providers to do re-badging of employees when appropriate.

- **Industry-specific BPO coming to the fore.** While horizontal BPO areas such as F&A, HR, and procurement are quite mature now, buyers are increasingly looking at industry-specific functions for BPO. After all, industry-specific areas are a large chunk of a company's operational cost base, and so BPO has greater potential to impact this cost base more significantly.
- **Harbinger of IT+BPO convergence.** As organizations look to derive greater transformational value, the role of technology in BPO gains more importance. This deal is a reflection of the same. Beyond BPO, TCS will not only provide IT services and infrastructure services, but will also move a significant portion of the policies to its BaNCS technology platform.

How This Deal Will Impact TCS

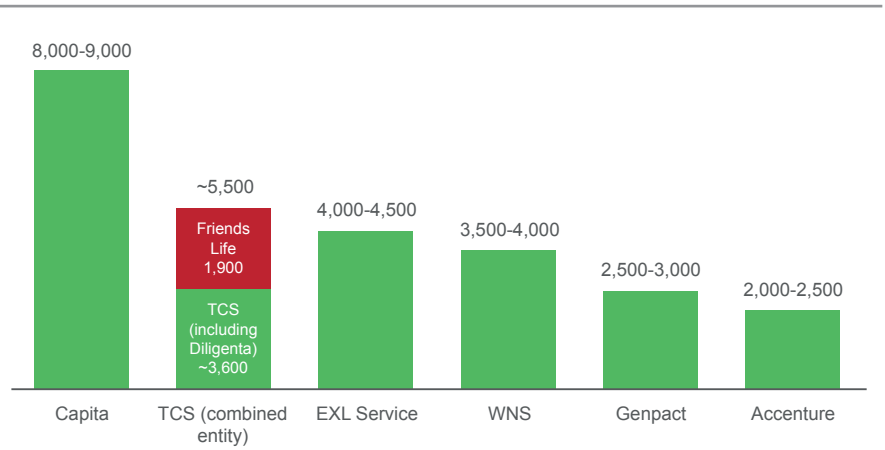
This deal is a significant win for Diligenta, as well as TCS as a whole.

- **Catapults TCS to the position of second largest provider in the Insurance BPO space.** The deal has a significant impact on the scale of TCS's insurance BPO business. Before this deal, Diligenta had only 1,800 employees onshore in the UK. With this development, that number goes to 3,700, making TCS the second biggest insurance BPO service provider in terms of onshore FTE presence in the UK. This deal also makes TCS the second biggest Insurance BPO service provider globally, with 5,000+ FTEs, leapfrogging over competition such as EXL Service, WNS, and Genpact (see **Exhibit 2**). TCS also consolidates its leadership position in the Life & Pensions (L&P) segment of insurance BPO.
- **Boost to the top line but potential drag on the bottom line in the short-run.** The deal will provide a significant boost in revenues to Diligenta and TCS, with a US\$147 million surge on a per annum basis. However, the margins from large deals generally take a fair amount of time (two-three years) before they turn green, and the margins from this deal too will take some time to start contributing to the TCS (and Diligenta) bottom line. Also, considering that the deal will have a significant concentration of onshore resources and FTEs (including 3,700 FTEs in the UK after Friends Life employees move to Diligenta), it may end up being a drag on TCS margins in the short-run as TCS has a much higher offshore focus in its sourcing mix. It remains to be seen how many of these newly acquired FTEs will ultimately end up being offshored by TCS over the medium- to long-term.

EXHIBIT 2

Service provider scale in insurance BPO – top six providers in terms of number of FTEs in industry-specific insurance BPO

Source: Everest Group analysis



- **Unlikely to sign another large Insurance BPO deal in the near future.** The transition time, effort, and resources required for this deal are immense. This might therefore hamper the ability of TCS to pursue new opportunities as it ties up their resources, at least in the short term. We, therefore, do not expect TCS to sign another large insurance BPO deal in the near future.

Developments to Watch Going Forward

- **Transition.** The transition phase of a deal this large is going to be fairly complex. The integration of operations, including the transition of insurance policies to a new technology platform, will need to be closely watched to determine how efficiently and quickly it proceeds. On a long term basis, TCS' ability to deploy Friends Life operations and resources to other clients is also going to be important.
- **Adoption beyond UK.** While UK is already a mature market for insurance BPO in general and closed book in particular, we expect global service providers to target other geographies to tap opportunities.
- **Platform strategy of other service providers.** This deal underscores the importance of technology platform and IT capabilities to succeed in large deals. It will create peer pressure on other insurance BPO service providers that don't have a platform to create one. Additionally, service providers with silo-based IT and BPO capabilities will increasingly push to create a combined offering. This will create opportunities for more IT+BPO-led deals in the closed books segment in life insurance.

About Everest Group

Everest Group is an advisor to business leaders on next generation global services with a worldwide reputation for helping Global 1000 firms dramatically improve their performance by optimizing their back- and middle-office business services. With a fact-based approach driving outcomes, Everest Group counsels organizations with complex challenges related to the use and delivery of global services in their pursuits to balance short-term needs with long-term goals. Through its practical consulting, original research and industry resource services, Everest Group helps clients maximize value from delivery strategies, talent and sourcing models, technologies and management approaches. Established in 1991, Everest Group serves users of global services, providers of services, country organizations, and private equity firms, in six continents across all industry categories. For more information, please visit www.everestgrp.com and research.everestgrp.com.

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