



## Monetization of Captives Fueling the Outsourcing Marketplace: Aviva's Recent Sale of its Captive Illustrates Common Motivations, Benefits

By Sid Pai, Partner & Managing Director, TPI India  
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During the past two years, merger and acquisition (M&A) activity in the outsourcing marketplace has witnessed an interesting wave of transactions emanating from the sale of captive centers. Captive centers are free-standing shared services owned by a parent company, commonly in an offshore location. The most recent captive center transaction of note was the sale of the captive belonging to Aviva, the fifth largest insurance company in the world and the largest in the United Kingdom, to third-party service provider WNS.

Outsourcing industry participants have tracked the trend for the “monetization” of captives — parent companies selling their offshore captives to third party service providers — with considerable interest. The transaction sizes have ranged from fairly small to mega deals and, for the most part, have surfaced in the business process outsourcing (BPO) space.

### TPI's point of view on this trend is:

- Monetization, as an opportunity, is available to parent companies within a short window of about 18-24 months — limited, in no small measure, by the current credit crunch and recession. It is fuelled both by service providers' aspirations to grow to global scale or to specialize in a particular industry and by the need of parent organizations to raise cash in the current challenging global economic environment.
- Service providers' interest in such transactions has varied from courting captives for the purpose of scale or for acquiring industry-specific capabilities to buying a large book of committed business from the parent of the captive center.

- Service providers' propensity to acquire captive assets will continue to change over time, which will affect both the number of such transactions as well as the valuations that such centers command in the marketplace.
- Over time, a higher proportion of captive center monetization transactions will occur for more tactical than strategic reasons, thereby, shifting the balance of negotiation in favor of service providers. The underlying rationale for such a shift is the growing maturation of the third-party outsourcing industry in general and their coverage of specific industry segments (such as insurance or banking) in particular. The higher the degree of maturity of the third-party players, the lower their interest in buying for scale or credentials. Niche segment acquisitions will still be attractive to service providers, as long as they are nascent and evolving from an outsourcing perspective.

TPI's extensive 2007 benchmarking study of captive operations located in India, as well as our significant advisory experience of working closely with several such operations, reveal that parent companies need to be extremely sure of the strategic alignment and market competitiveness of their existing captive operations. In other words, our research revealed that captives should clearly either serve the purpose of an efficiency play (relative to similar third-party players) or a value play (core and strategic to the business not amenable to outsourcing) to the parent. Without such clarity in the captive organization's reason for being, there is going to be a loss of shareholder value by keeping such operations in-house over time.



Most recently, TPI advised Aviva on the monetization of its large-scale captive operations spanning India and Sri Lanka. Aviva originally set up its offshore captive operation in 2003 using “build-operate-and-transfer” (BOT) agreements, through which it worked with service providers to create its captive capability in India. The company proceeded to transfer some of its operations into in-house captive operations and was on course to eventually transition all its offshore operations into its in-house captive.

A review of Aviva’s strategy in late 2007 revealed that the company might be better served by not exercising its remaining options under the BOT agreements and, instead, “monetizing” its existing operations and entering into a long-term outsourcing contract for the provision of its “offshored” business processing. This strategic realignment eventually resulted in a watershed “captive monetization” transaction.

This was a complex transaction that entailed the transfer of almost 6,000 personnel from Aviva to WNS, the winning bidder, with an associated eight-year outsourcing contract valued at a total contract value of more than US\$1 billion. Additionally, the transaction resulted in a sale of US\$228 million paid by WNS to Aviva.

As the largest sale of captive capability in the history of BPO outsourcing, it certainly qualifies as a landmark transaction that offered strategic value to both Aviva and WNS. Apart from already benefiting from an upfront cash inflow from the sale consideration, Aviva anticipates considerable operational efficiency and cost predictability from the new outsourced arrangement, while WNS has beefed up its scale and credentials in the insurance industry to an unmatched level through this transaction.



**ABOUT THE AUTHOR:** Sid Pai, Partner & Managing Director, Global India, leads the firm's office in Bangalore. Sid provides TPI clients expert sourcing solutions for information technology (IT) processes and business process outsourcing (BPO) with a special focus on offshore operations. He possesses specialized industry expertise in the telecommunications and financial services sectors, and has had sector profit responsibility for significant service provider businesses across the globe in both these sectors.

Prior to TPI, Sid held senior executive roles with IBM and BearingPoint in the Americas, Asia Pacific and Europe.

Sid holds Master of Business Administration and Master of Science degrees from the University of Rochester, Rochester New York, and earned his undergraduate degree from Bangalore University.

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**Americas**

Nigel Walker  
Partner & Managing Director  
**+1 281 465 5763** or  
[nigel.walker@tpi.net](mailto:nigel.walker@tpi.net)

**EMEA**

Denise Colgan  
Marketing Manager  
**+44 (0) 1628 421862** or  
[denise.colgan@tpi.net](mailto:denise.colgan@tpi.net)

**Asia Pacific**

Arno Franz  
Partner & Managing Director, Asia Pacific  
**+61 (0) 2 9006 1610** or  
[arno.franz@tpi.net](mailto:arno.franz@tpi.net)



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