



WORKING PAPER SERIES

**March towards RPO(s)  
Research Process Outsourcing prospects in India**

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RPO (Research Process Outsourcing) has attracted much attention from business researchers over the last few years. It has been repeatedly propounded by evangelists that India would be a hotspot for contract research (in fields of pharma, bio-tech and Hi-tech) Hence, we took it upon ourselves to learn more about this prospect, with emphasis on high-tech, and stumbled upon some astounding facts, which we present in this white paper.

First we intend to dispel a few common myths, which we discovered, surrounding RPO(s).

**Myth 1:** Research can never be outsourced since it is central to the organization.

**Reality:** Partly true, basic research shall be never be outsourced but peripheral research or development shall be increasingly so. Development is defined as translation of research findings or other knowledge into new or improved product, process, or service [[www.gcsaa.org/mc/benefits/glossary.asp](http://www.gcsaa.org/mc/benefits/glossary.asp)].

Often basic research throws up a lot of new ideas but the organization often has resources to only fund the development of the one which it thinks is the “Killer Idea”. But with laws of probability at play, the second best idea could very well turn-out to be the block buster. It is then the second and possibly third best ideas that could be outsourced to be worked upon. Even if they are not a success, it reduces the cost of failure and diversifies risk.

**Myth 2:** Global Majors are not ready to outsource research.

**Reality:** Again partly true, research outsourcing needs much more comfort level and trust between the outsourcee and the outsourcer than currently required in traditional business models. But to get to a level of comfort demanded by RPO, it would require adequate investment; in terms of human resource and infrastructure.

The roadblock is the lack of business models which can factor in uncertainty and risk associated with research. The success of some Indian bio-tech firms in joint-collaborative research proves the point that RPO does become reality with proper investments and research specific business models.

**Myth 3:** Research is by definition unstructured, it cannot be put into process.

**Reality:** Basic research is unstructured as it is the search for the unknown, where as peripheral research is always towards an end. Hence it can be put into defined process and steps. The research processes described by Dorothy Leonard and Jeffrey F Rayport in their land mark article “Sparking Innovation through Empathic Design” could be a starting point. Another HBS article “Creating Breakthrough Products using the Lead User Process” by Eric Von Hippel, Stefan Thomke, and Mary Sonnack outlines similar ideas.

IT outsourcing happened only when the process were put in place in a un-hitherto ad-hoc activity (though with a clear purpose).

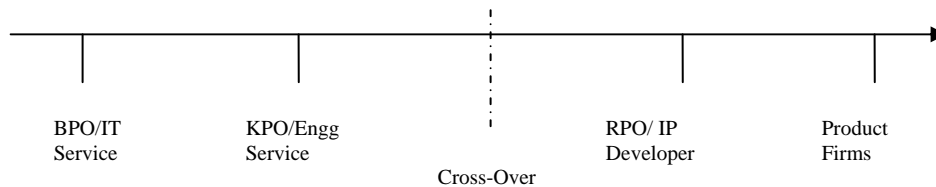
**Myth 4:** Present Indian business majors would be the first to move into RPO(s)

**Reality:** Upstarts would have an upper hand and once they have the correct business model it would take much less time to scale up to Indian majors (in terms of revenues). Large-sized incumbents would continue to face complacency and fatigue. Even in the Pharma industry, the new entrants have shown greater agility to scale up.

Profitability is much higher than the traditional business models and hence the entrants would achieve comparable bottom line on smaller revenues

We studied the outsourcing industry and found that there are basically four types of firms currently around.

Exhibit 1: Stages of the outsourcing industry



**BPO/IT Service** – Generic firms involving matured business process. Billing is based on the labor, time and materiel services provided.

**KPO/Engineering Service** – Involves knowledge driven business process. Billing is based on both labor and content. However the “content” per se is not so important in terms of criticality but on content. There is no notion of success and failure as long as the content meets certain standards set by the client. This is being hyped as the next growth area and is seeing a large number of existing firms shoring up their activities.

**RPO/IP Develop-** Involves highly knowledge intensive and loosely defined processes. Billing is on the basis of criticality of content + fixed-set cost. The outcome, if successful, often leads to IP creation. However the firm only earns royalty fees and the IP is for exclusive use by the outsourcing organization. Most firms who want to be future RPO(s) are in the cross-over stage. We have come across at least two firms in the high-tech space who are using this business model to venture into RPO. Needless to say, the revenues generated are minuscule compared to the overall revenues.

**Product Firms** – Internally defined processes which provide the firms a competitive edge. There is no billing and revenue is in sales of the products. The gestation period is often high and these firms are mostly non-existent in India.

The roadblocks and challenges in the march towards RPO(s)

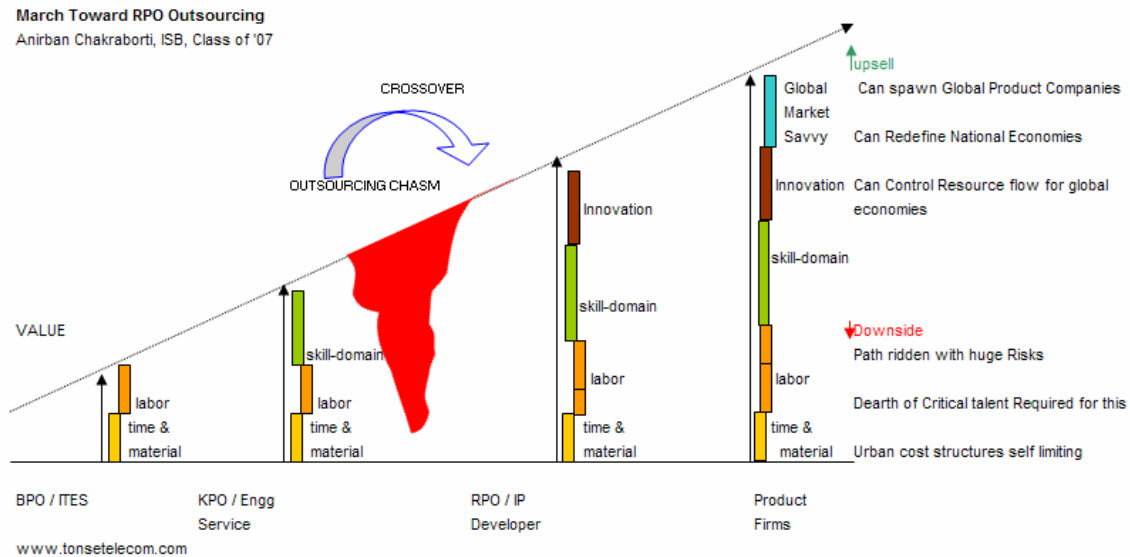
1. RPO(s) would require different mindset and not necessarily different skills. Since innovation would play a major role in the success of the firm, it would require risk appetite.
2. RPO(s) would require a different business model which factors in the risk spread, reward probability and value of the reward. Currently very few firms have that kind of model. The idea is not have one size fits all model but the ability to create one with the changing business environment.
3. RPO(s) would need managers to have business acumen and exercise market judgment to swerve the direction of a project in coordination with the client. The managers need to plan long terms strategies and opportunities for co-creation of value. Sadly, India Inc has severe shortage of these kinds of managers and there are no efforts to build such competencies.
4. The comfort level and trust with the outsourcing organization has to be far higher than that required for a generic KPO.

In spite of all the challenges, there are more positives which outweigh the negatives. They are –

1. India is the base of highly skilled professionals who can undertake such ventures.
2. Cost Arbitrage – For the skills needed in a RPO, we are still 1/5<sup>th</sup> the cost.
3. Not easily replicable as it requires skill-sets not easily found elsewhere. Hence the customer exit barriers are high.
4. Ability to scale up fast and cheap in India which is a unique competitive advantage. Recently a Pharma global major contract required a bio-tech to recruit 200 chemists in a week's time. This number is close to the number of chemists graduating from top European universities in any given year.
5. Move from captive centers (which are essentially cost centers) to joint ventures (which are profit centers) is a favorable trend. We came across a few mid-sized European and American organizations that don't have or are not willing to commit enough resources for a captive center and hence have set-up joint R&D collaboration. What we have observed is that the cost pressures are equally on all firms but the responses are governed by the size of the organization.

6. A few successes in generating Intellectual Property shall earn enough royalty revenue to cover failures.

Exhibit 2: Summary Diagram



### *Our Predictions*

Our interactions and discussion with numerous bio-tech and technologies firms, in various stages of lifecycle, have let us to conclude that pure RPO(s) are still two years away. However, more and more KPO(s) would be at the cross-over stage. In fact new KPO(s) are incorporating RPO aspects in their business model. This approach is necessary not only to hedge the risk of failure with the steady cash flow of KPO but also ensure long-term competitive advantage. BPO(s) would face challenges of existence as transactions cost spiral upwards. The KPO industry would leap-frog into RPO and wouldn't go through the life-cycle that BPO underwent.

Unfortunately, India would not see many product firms as ROI (Return on Investment) is higher in RPO(s) than in pure product firms. Our study showed that Indian firms feel that the rewards in final customer marketing are not worth the global marketing and sales efforts. However they shall invest in acquiring capabilities which help in customer-focused product development.

### *Closing Thoughts*

1. Would the venture capitalists fund RPO ventures?
2. Would India Inc develop the marketing ability to understand the global customer which is so necessary for a successful innovation?

3. Would India Inc be able to develop a risk appetite and work out mature business models which shall make RPO(s) the next success story?

***Research Methodology***

To arrive at the conclusions which have been presented in the white paper, we decided on a sample space of bio-tech, hi-tech, IT firms and also captive centers of Fortune 10 companies operating in India. We distributed questionnaires and followed up with personal interviews. We also extensively searched public domain information and looked at similar trends in Taiwan, Korea and China.

Out of all contacted, only one IT major refused to participate, citing resource constraints.

***Contact Information:***

We invite suggestions, comments and brickbats. Please contact at

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