



Offshoring – where to next?

Op2i Analysis

September 2008



Setting the scene

- Offshoring is a widely understood concept, at least within the sourcing community - what is not so well understood are the top destinations for offshoring.
- Mention offshoring, and almost all will mention India, but should organisations wishing to offshore, only think about India?
- There is no question, India was the first destination, which viewed outsourcing as a sector on its own right and influenced government policy. India still leads when it comes to sheer volume, however many question whether the country is suffering from its own success:
 - Where there was an abundant labour supply, today there is a shortage in some areas
 - Where there was immense scope of labour arbitrage, today that has narrowed, as inflation takes grip
 - Companies benefited from the dollar exchange, today it is quite opposite
 - Where there was pro-outsourcing government incentives, these are slowly been eroded as government priorities shift
 - Where companies were eager to get business and went that extra step, today these same companies have an overflow of opportunities showing little loyalty to its old client base
- There are new destinations coming up, which may offer a better “deal” for offshorers
- These new destinations may also be superior in offering services where India was weak
- This perspectives delves into the top offshoring destinations
- We note that every organisation will have a different view of which factors are the most important for their needs, but we hope this perspective, helps sourcing managers determine which locations maybe right for their organisations



Wide discrepancy on analysts views of top countries - apart from the top position that is...

- Gartner (2008 view on top 30 ITO destinations)
 - Gartner used ten criteria that it determined important for organisations to consider when looking at a potential location for offshore or nearshore IT or business process services. They were: language, government support, labour pool, infrastructure, educational system, cost, political and economic environment, cultural compatibility, global and legal maturity, and data and intellectual property security and privacy.
- IDC (2007 view)
 - Predicting that China would overtake India in offshoring by 2011
 - its Global Delivery Index (GDI) compares 35 cities in the Asia-Pacific region as potential offshore delivery centers based on a set of criteria such as labor and rental costs, language skills and turnover rate.
 - Although the top ranked Chinese cities--Beijing, Shanghai and Dalian--trail their Indian counterparts in the GDI this year, they are expected to overtake the competition by 2011.
 - IDC attributed this to China's massive investments in areas favorable towards offshoring, such as infrastructure development, technical skills as well Internet connectivity.
- AT Kearney
 - India and China to dominate
 - India maintains a wide, albeit slightly shrinking, lead over China, confirming what industry surveys and visiting executives repeatedly find – for all the concern about overheating, wage inflation and service levels, India still offers an unbeatable mix of low costs, deep technical and language skills, mature vendors and supportive government policies



What factors make a country / city attractive?

1. Legal system (can you enforce the contract – what is the data and IP rights protection regime like?)
2. Skilled workforce (how educated is the labour market?)
3. Cultural alignment (do they think and work the same way?)
4. Political stability (is there a risk of security /sanctions/ change in policy stances?)
5. Economic stability (how solid is the economy, is there are risk to currency / taxes etc)
6. Government incentives (are there favourable government incentives to go there?)
7. Language (is English the predominant language? What about other languages that your customer may desire?)
8. Labour costs (what is the scope for labour arbitrage?)
9. Existing track record (how good is the outsourcing vendor market – can they be trusted?)
10. Proximity to home (what if there is a problem tomorrow, can you resolve remotely – how long does it take to get there?)
11. Infrastructure (all outsourcing requires robust communication links, good power supply and road and air links – how does the country/ city compare?)
12. Access to resources (no doubt, the offshorer will need local support at some stage – what is the availability of skilled business services and professionals – e.g. lawyers, consultants etc?)

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Which are more important than others – what's the ranking of these?

High (relatively)	Medium (relatively)	Low (relatively)
<ul style="list-style-type: none">1. Legal system2. Skilled workforce4. Political stability7. Language8. Labour costs	<ul style="list-style-type: none">3. Cultural alignment5. Economic stability6. Government incentives11. Infrastructure	<ul style="list-style-type: none">9. Existing track record10. Proximity12. Access to resources



- Asia

- India and China have seen double-digit growth rates have fuelled wage inflation, with average compensation costs rising between 20-30%, however, cost escalations have been matched by corresponding increases in skill supply and quality indicators.
- India maintains a strong-lead in terms of language skills and vendor maturity, together with an enviable track record and strong albeit slow legal system.
- China leads on infrastructure development and growth in education, but its legal system lacks transparency and it suffers from the obvious language skills.
- Singapore some 20 years ago a leading outsourcing destination has been overtaken by lower-cost countries now competing to establish themselves as service centers.
- Philippines is getting exponential business in the case of call centers, largely as firms relocate these from India to the Philippines. It also has language skills unmatched in the region and a very good cultural alignment with the West. It also offers one of the lowest wage locations and offers low cost telecom.
- Malaysia's economic stability, its diverse language skills and the investment the government has made, in the Multimedia Super Corridor and Cyberjaya, to establish the country as a regional IT hub, are driving the region as a outsourcing destination.
- Thailand, Indonesia and Vietnam have also seen significant declines in telecom costs, while slower growth rates have moderated wage inflation. However they lack the language skills, scale and labour arbitrage afforded by India. Thailand and Indonesia will likely remain challenged by lesser English language capabilities and concerns over their economic and political stability.
- Sri Lanka and Pakistan, although offer many of the same advantages as India, suffer from their relatively smaller population-base and obvious concerns over internal security.
- Australia and New Zealand offer attractive destinations in terms of language, cultural alignment, legal systems and infrastructure, but lack the scale and costs structures that others in the region can provide



- South Americas

- Spurred on by India's success, governments throughout the region have recognised the potential of the export services sector, particularly in the context of providing near-shore support to North America and Iberia.
- Brazil has begun to leverage the traditional strengths of its indigenous IT sector, rapidly expanding university enrollment and quality certifications, together with the scale it can offer.
- Chile, Mexico and Argentina have seen significant sector growth and some increases in graduation rates.
- Chile continues to benefit from the best business environment and tax structure in the region
- Mexico leverages its proximity to the US
- Argentina offers relatively lower costs.
- Costa Rica was a traditional leader in the region but has been overtaken by the heavyweights moving in.



- Europe
 - Czech Republic, Hungary, and Poland the leaders in the region are now losing ground to emerging locations, such as Bulgaria and Romania. Continued improvement in the business environment in the Czech Republic and Hungary can not offset deterioration in cost competitiveness.
 - The Baltic States, Estonia, Latvia and Lithuania still lack the infrastructure of its European neighbours, and suffer from the relatively small size.
 - Russia the new kid on the block offers strong technical skills, but lacks the infrastructure, language skills and cultural alignment that some of the newer EU members or prospective members offer.
 - UK and Ireland score relatively highly and would be leaders were it not for their high labour costs. Both countries offer stable political and economic environments with strong legal systems, excellent infrastructure and access to good resources, albeit smaller in population size than the Asian counterparts



- Africa and the Middle East

- Middle Eastern and African countries are increasing their visibility as remote services locations.
- Egypt, Jordan and the United Arab Emirates are all trying to establish themselves as outsourcing hubs. The former attracting a number of Asian vendors to the region as they run short of skilled and cost effective labour from the home markets.
 - » Egypt has become a prime location for Information Technology (IT) and call center outsourcing.
 - » Egypt's Smart Village has been the preferred destination for call centers and exported IT services in Egypt. The Village currently hosts some 12,000 employees working for more than 100 multinational companies — most of them in outsourcing — who have massive call centers serving English and non-English speaking clients around the world. From providing cell phone services and customer support (Vodafone call center) to R&D centers (Orange Business Services) that work autonomously to provide solutions to the IT and Telecom sectors, Smart Village is well-equipped for anyone seeking to enter Egypt's outsourcing market. Smart Village expects to host 80,000 employees by 2014, which is more than six times the current number over the coming six years.
 - » Xceed has been Telecom Egypt's call center arm since 2003 and is considered to be the biggest call center in the local market.
 - » Wipro joins Satyam as the second Indian company to find conditions there suitable for its outsourcing operation.
 - » With a 20% growth rate in Egypt's IT and call center sector in 2007, outsourcing has already played its part in contributing to the local economy's growth, up by 7% last year.
- Mauritius a leader in the African region offers good infrastructure, political, economic and business climate, but lacks scale.
- Morocco and Tunisia reflect growing interest in locations with the ability to serve francophone markets.
- Ghana maintains its position as a low-cost English language location in Africa, while South Africa is fast becoming the India of the African world.



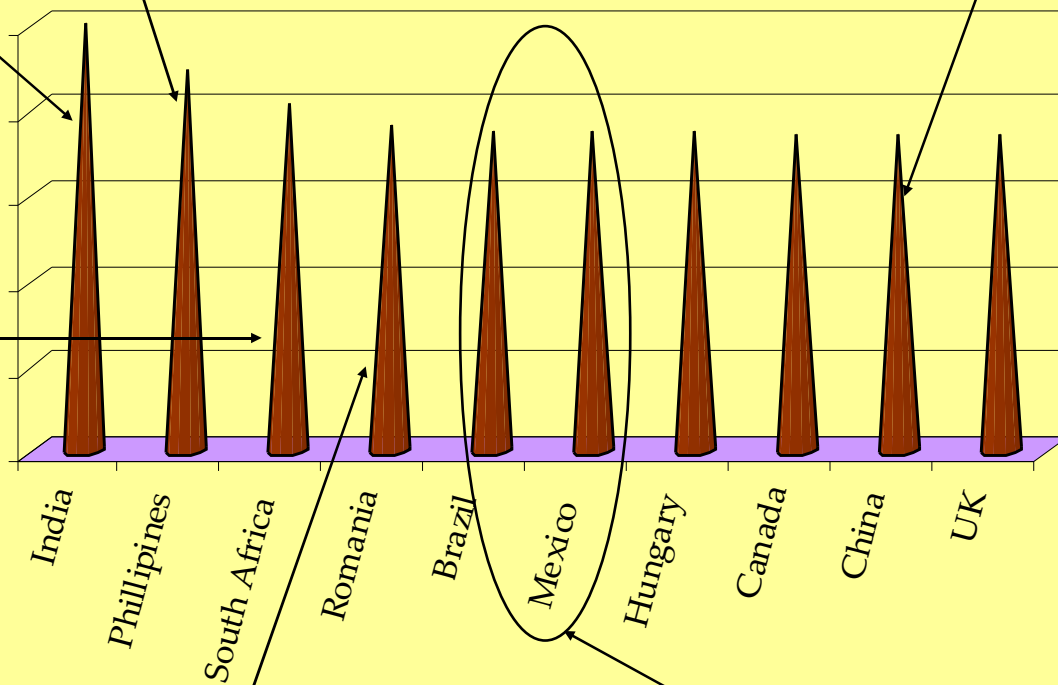
Op2i top offshoring rankings

The indisputable leader
In ITO and BPO

Becoming a hot destination for call centres

China, contrary to other analysts, has
some way to go

Top Offshore Destinations



South Africa
serving both
domestic
African and
Western
firms

Romania becoming nearshore
destination for European firms

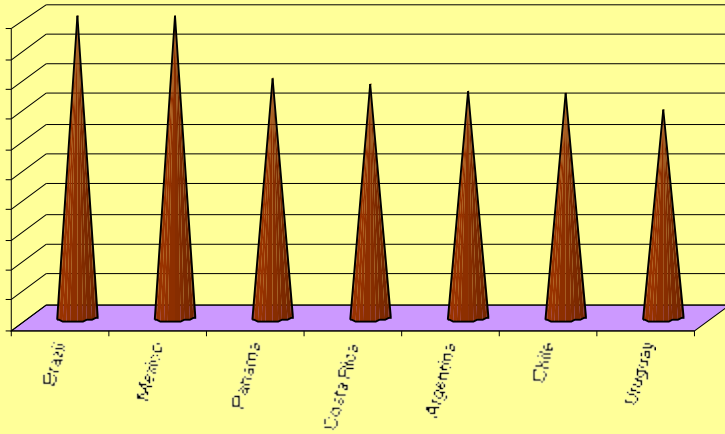
Serving domestic the USA market

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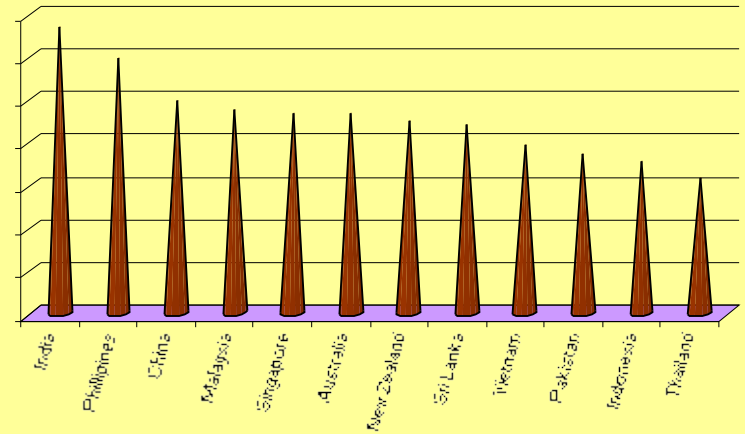


Op2i ranking by region

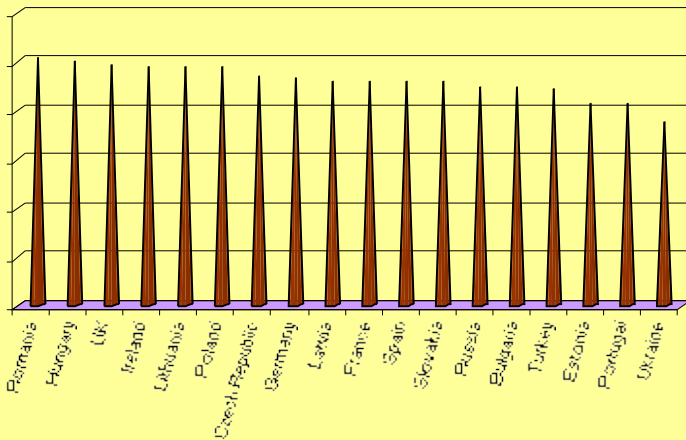
Top South Americas Offshore Destinations



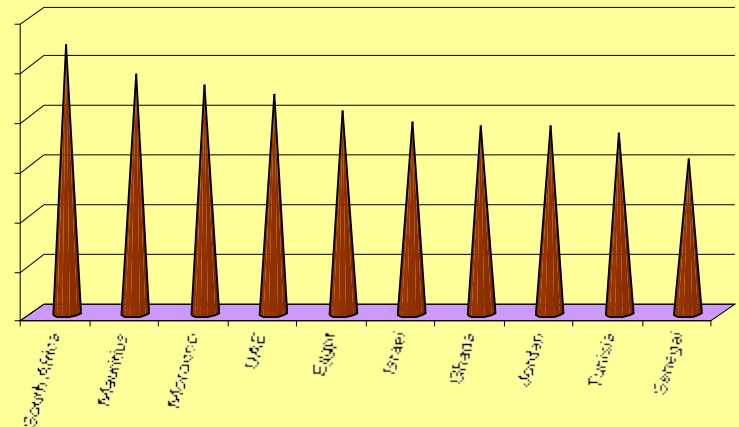
Top Asia Offshore Destinations



Top European Offshore Destinations



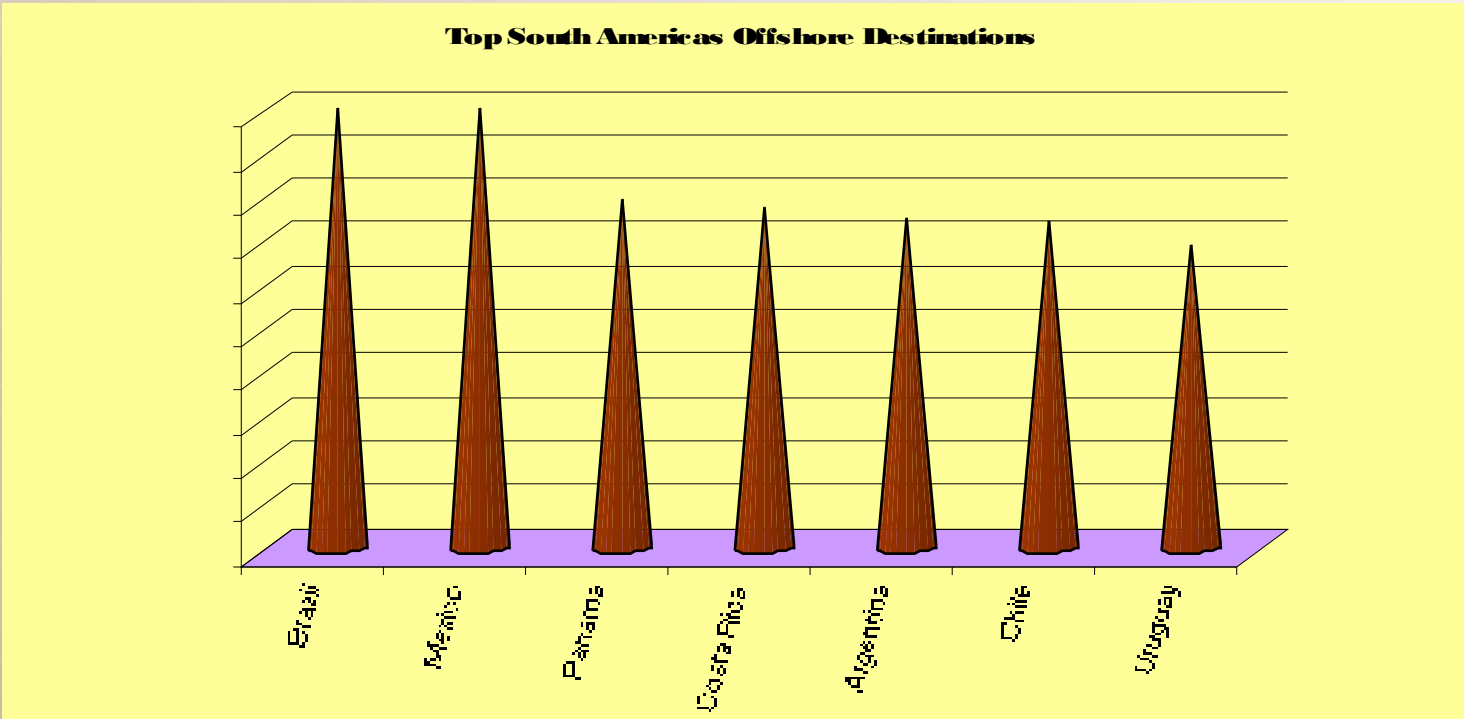
Top Africa /ME Offshore Destinations



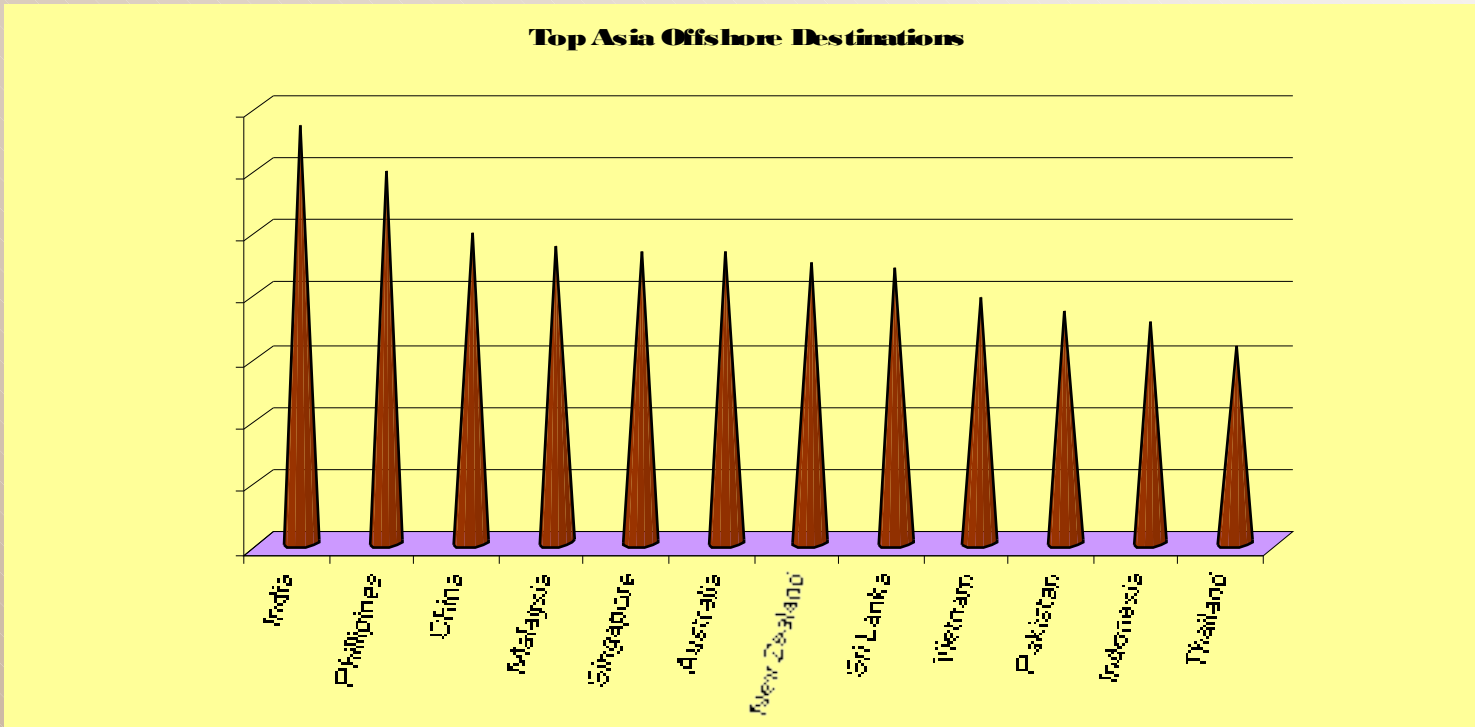
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Op2i South Americas ranking

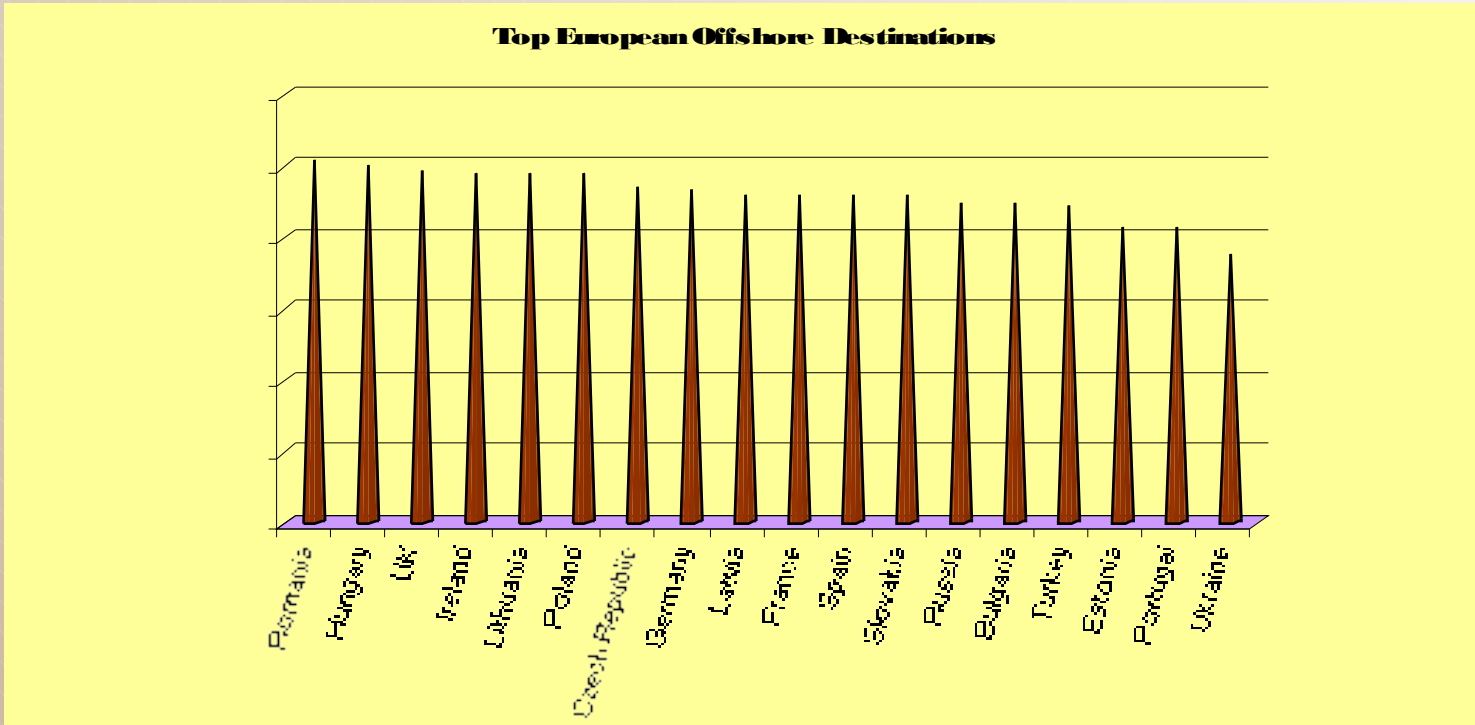


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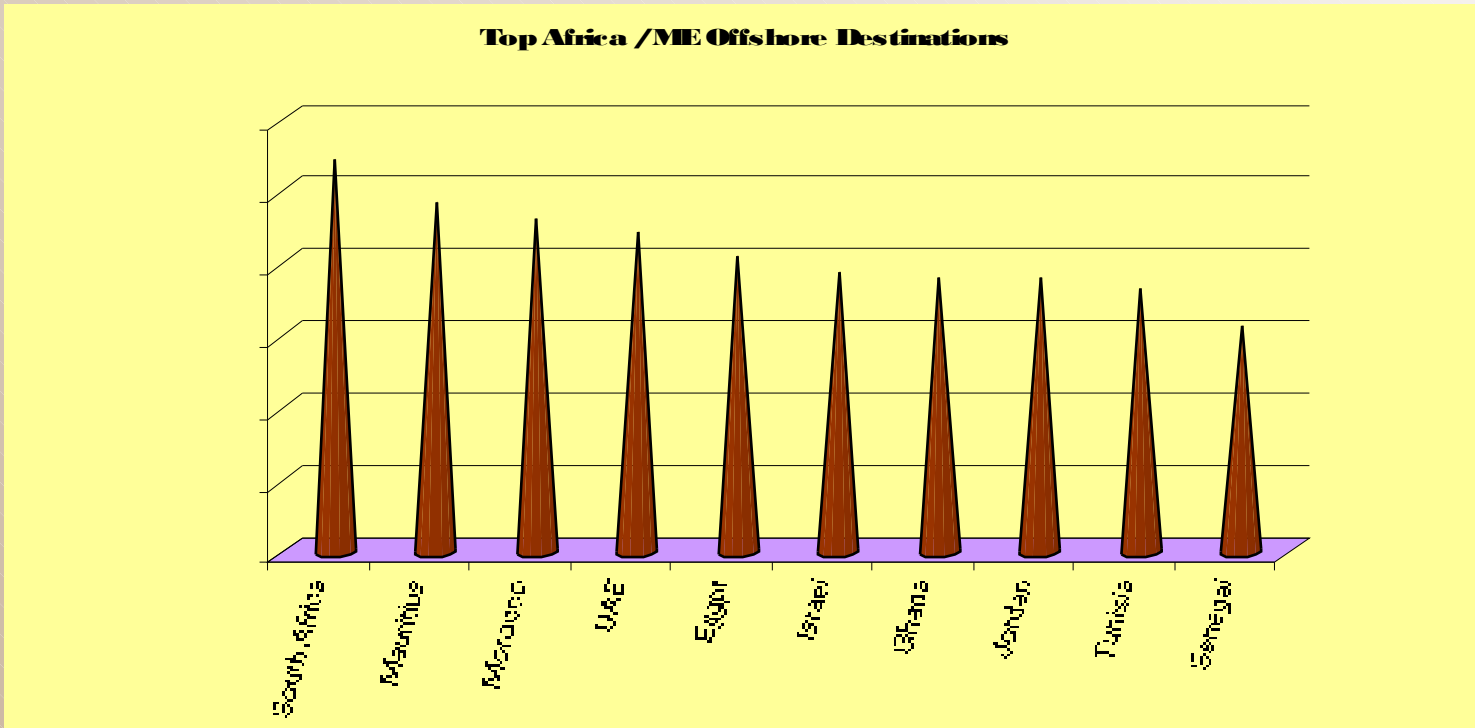
Op2i European ranking



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Op2i Africa / Middle East rankings



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Should we be thinking about top cities, rather than countries in the future?



Offshoring cities

- The choice of outsourcing cities is based on a combination of both country specific factors and regional / city factors – the latter are clearly more important in larger countries and may not be relevant or smaller countries.
- Generic factors which offshorers look for include labour arbitrage, availability of proper infrastructure and lower country risk.
- It is these generic factors that have made Indian cities hot destinations for offshoring.
- Availability of a fairly large and qualified pool of workers is imperative to the success of these Indian cities over the rest of the world.
- Clearly infrastructure availability varies by city and combined with the availability of skilled labour, and in particular the availability of middle and senior level management is an important determinant of a good outsourcing city.
- A city's success eventually leads to its down fall – this is the case with cities like Bangalore. Its immense success has seen wage inflation and staff retention being a major issue. Real estate prices have gone through the roof and the availability of skilled resources is becoming a problem. The very things that made the city a success and now in reversal.
- However times are changing and the 'one size fits all' approach has lost its relevance.
- With offshoring emerging as a major business process and companies offshoring both core and value-added processes, and cities competing for that piece of the pie, cities will need to differentiate themselves and we will eventually see cities positioning themselves as specialists outsourcers whether this is call centres, like manila, IT development like Bangalore, creative and media, like Chennai, Delhi and Mumbai in market research and financial services etc



Analysis of top 10 Indian cities

- 1. Chennai was the poor cousin of Bangalore and Hyderabad during the initial years of the IT boom in India. Today it is the lead outsourcing destination due to the low cost advantage, improving infrastructure, international connectivity, availability of land, skilled manpower and lower attrition rates compared to Bangalore and Hyderabad.
- 2. Hyderabad continues to woo investors by focusing on improving its urban infrastructure. The Governments, both past and present, have been very clear in their focus and support to the IT industry. The city has been among the most favored destinations due to the infrastructural improvements and the planned growth phased in by the governments in the twin cities.
- 3. Bangalore is the technology hub of India. It is increasingly becoming a global melting pot of cultures. The original garden and pub city of India has a comfortable climate compared to the other Indian cities that are happening in terms of outsourcing. However, the city's infrastructure is inadequate to meet the demands of the exploding population. There is a growing feeling that other cities will overtake Bangalore if it continues to suffer due to political bickering, skyrocketing real estate prices and poor urban planning.
- 4. National Capital Region (NCR) includes Delhi and its surrounding suburbs. Delhi is expensive and not as popular for outsourcing. It is the suburbs, Gurgaon and Noida that have become important outsourcing destinations due to their proximity to the capital. They continue to be a major draw due to improving transport connectivity with Delhi, good international linkage and availability of skilled manpower.
- 5. Pune is Maharashtra's response to Bangalore. Its proximity to India's financial capital, Mumbai and availability of trained manpower has led to the development of a thriving hi-tech outsourcing industry in this erstwhile retirement and education haven. Apart from other infrastructure components, the city is focusing on township projects to improve housing facilities.



Analysis of top 10 Indian cities

- 6. Chandigarh and Mohali are twin cities. Chandigarh is one of the few planned and good cities of India. Mohali is its twin. Together, they have the space as well as the intellectual and financial capability to become India's best outsourcing destinations. It does not yet have an international airport, but is well connected to New Delhi by road and rail.
- 7. Kolkata, the capital city of the state of West Bengal is high in intellect and has an advantage in terms of low costs. However, the city is famous for its traffic snarls and trade union shut downs.
- 8. Mysore is one of India's smaller cities, which have joined the outsourcing bandwagon. Its proximity to Bangalore and presence of companies like Infosys and Wipro has helped the cause. It is emerging as a preferred choice over Bangalore as India's silicon city is now congested, expensive and has higher than average attrition rates.
- 9. Thiruvananthapuram in Kerala is well known for some of the leading science & technology research organisations in India. The city has the infrastructure and skilled workforce to attract IT investments. It is early days yet and remains to be seen whether Thiruvananthapuram can woo investors away from Bangalore, Hyderabad and Chennai.
- 10. Coimbatore is the emerging engineering outsourcing hub located in the state of Tamil Nadu. The government of Tamil Nadu is keen on developing Coimbatore as a major IT destination in the state. Coimbatore's strength is its rich engineering tradition and young graduating engineers to meet the manpower demands of the growing industry.



This Perspective has been written by Bharat Vagadia, CEO Op2i - a business improvement firm specialising in outsourcing.

Services offered include: advisory, training, project management, governance and arbitration services throughout the outsourcing lifecycle.

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The views expressed in this Perspective reflect only the views of its author and not the NOA.

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