A.T. KEARNEY

The Shifting Geography of Offshoring

The 2009 A.T. Kearney Global Services Location Index™

As the world continues to experience economic turmoil, the offshoring industry is not immune—especially as the industry's most important client, financial services, struggles to stay afloat. Findings in the 2009 A.T. Kearney Global Services Location Index™ reflect this unstable recessionary environment. While some established outsourcing hubs are fading—nine countries dropped nine or more positions in the Index—new rising stars are changing the outsourcing landscape.

The top three countries in the 2009 Global Services Location Index™ (GSLI) remain the same—India, China and Malaysia—but the world's volatile economic environment is reflected in the rest of the rankings. Not long ago Central and Eastern Europe emerged as one of the premier global hubs for offshoring, catering primarily to Western European clients. This year, however, the established leaders, including Poland, the Czech Republic and Hungary, have fallen as increasing costs erode their competitiveness. Meanwhile, countries in low-cost regions such as Southeast Asia and the Middle East make significant gains on this year's list, as the IT-enabled services industry grows and export figures improve *(see figure 1 on page 2)*.

The GSLI, first established in 2004, analyzes and ranks the top 50 countries worldwide as the best destinations for providing outsourcing activities, including IT services and support, contact centers, and back-office support. Each country's score is composed of a weighted combination of relative scores on 43 measurements, which are grouped into three categories: financial attractiveness, people skills and availability, and business environment *(see Appendix: About the Study on page 18)*.

This paper presents an overview of the 2009 findings in the GSLI, highlights the major strengths and weaknesses of each region, and offers recommendations for choosing the right locations around the globe to locate services during these turbulent times. Regardless of the economic conditions, making decisions that maximize the overarching benefits of offshoring is vital for success both in the short and long term.

Changes in the Offshoring Landscape

The offshoring industry has matured over the past decade. IDC, an IT market intelligence company, reports that outsourced offshoring alone has generated $30 billion in revenues and has grown by 25 percent over the past two years. This does not take into account captive centers in low-cost locations operated by companies from developed countries.

Figure 1

The 2009 A.T. Kearney Global Services Location Index™

Rank	Country	Financial attractiveness	People skills and availability	Business environment	Total score
1	India	3.13	2.48	1.30	6.91
2	China	2.59	2.33	1.37	6.29
3	Malaysia	2.76	1.24	1.97	5.98
4	Thailand	3.05	1.30	1.41	5.77
5	Indonesia	3.23	1.47	0.99	5.69
6	Egypt	3.07	1.20	1.37	5.64
7	Philippines	3.19	1.17	1.24	5.60
8	Chile	2.41	1.20	1.89	5.50
9	Jordan	2.99	0.91	1.59	5.49
10	Vietnam	3.21	1.02	1.24	5.47
11	Mexico	2.48	1.50	1.45	5.43
12	Brazil	2.18	1.83	1.37	5.39
13	Bulgaria	2.83	0.89	1.62	5.34
14	United States	0.47	2.71	2.15	5.33
15	Ghana	3.26	0.70	1.36	5.32
16	Sri Lanka	3.13	0.95	1.17	5.25
17	Tunisia	2.86	0.91	1.45	5.22
18	Estonia	2.06	0.93	2.20	5.19
19	Romania	2.63	0.91	1.58	5.12
20	Pakistan	3.12	1.08	0.91	5.11
21	Lithuania	2.31	0.81	1.99	5.11
22	Latvia	2.28	0.86	1.96	5.10
23	Costa Rica	2.67	0.89	1.50	5.07
24	Jamaica	2.77	0.79	1.49	5.06
25	Mauritius	2.32	0.95	1.77	5.04
26	Senegal	3.06	0.88	1.08	5.03
27	Argentina	2.47	1.34	1.21	5.02
28	Canada	0.54	2.10	2.38	5.02
29	United Arab Emirates	2.10	0.84	2.04	4.98
30	Morocco	2.62	0.93	1.42	4.97
31	United Kingdom	0.43	2.13	2.39	4.94
32	Czech Republic	1.74	1.14	2.07	4.94
33	Russia	2.39	1.45	1.08	4.92
34	Germany	0.42	2.10	2.40	4.91
35	Singapore	0.72	1.55	2.62	4.90
36	Uruguay	2.46	1.00	1.43	4.89
37	Hungary	1.95	1.01	1.92	4.88
38	Poland	1.82	1.22	1.73	4.77
39	South Africa	2.28	1.02	1.44	4.74
40	Slovakia	2.05	0.94	1.75	4.73
41	France	0.40	2.03	2.29	4.72
42	Ukraine	2.63	0.97	0.99	4.58
43	Panama	2.48	0.70	1.40	4.58
44	Turkey	2.01	1.23	1.29	4.54
45	Spain	0.57	1.90	2.00	4.47
46	New Zealand	1.12	1.18	2.15	4.45
47	Australia	0.42	1.62	2.22	4.26
48	Ireland	0.27	1.56	2.26	4.09
49	Israel	0.85	1.39	1.78	4.02
50	Portugal	1.00	1.00	1.97	3.98

Note: The weight distribution for the three categories is 40:30:30. Financial attractiveness is rated on a scale of 0 to 4, and the categories for people and skills availability, and business environment are on a scale of 0 to 3.

Source: A.T. Kearney

India is still the largest provider of offshore services, with the Philippines a distant second. Together the two countries account for 50 percent of the world's business process outsourcing (BPO) market. While the strong position of these two countries appears unthreatened for the time being, the competition is heating up, as Europe steps more prominently into the picture. North American companies, which still account for 70 percent of offshore outsourcing spending, were the first to send services offshore. However, European companies are catching up as their spending on offshoring has risen faster than their counterparts in North America. This shift on the demand side affects the overall industry footprint, resulting in more interest in European near-shore locations where English is not the dominant language, including locations in Central and Eastern Europe, and the Middle East and North Africa.

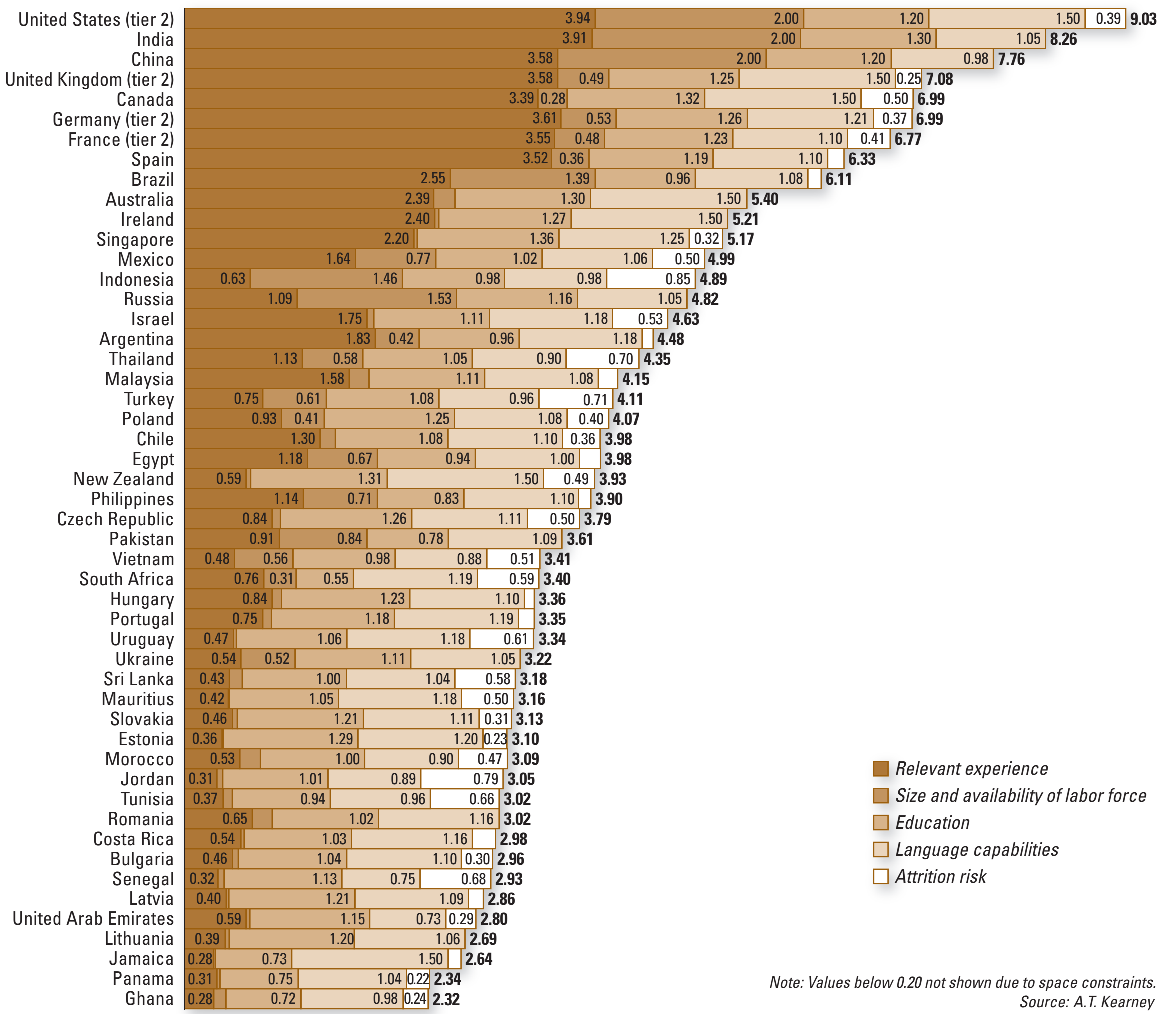
Another major trend is a move away from captive centers toward more outsourcing providers. As many captive centers failed to contain costs efficiently, more companies are opting to buy the services they need from outsourcing providers. For example, after many false starts, Citibank finally sold its Indian captive operations to Indian outsourcing provider Tata Consultancy Services (TCS) in October 2008. The deal included 12,000 employees and an agreement that TCS will provide the services that Citigroup produced in its captive centers. The sale made TCS the second-largest outsourcing company in India and Citigroup its largest client. Similarly, Philips sold three of its offshore BPO centers, which employ a total of 1,300 people, to Infosys in 2007 for $250 million. That agreement included a provision that Infosys would provide Philips with BPO services for the next seven years.

While cost remains a major factor in decisions about where to outsource, the quality of the labor pool is gaining importance. With this in mind governments around the world are investing in the human capital demanded by the offshoring industry. University curricula are being updated, postgraduation courses are being offered, and private educational institutions are offering training in key vocational skills. Companies are viewing the labor market more through a global lens, and in many cases offshoring decisions, especially in higher, value-added functions, are being driven by talent shortages at home as much as by cost-cutting. Companies with a focus on research and development (R&D) are increasing their global footprint to seek fresh talent in new markets, as their home locations cannot supply the needed talent. In this year's Index, an experienced labor force is key to success *(see figure 2 on page 4)*.

Regardless of the economic conditions, making **decisions that maximize the overarching benefits of offshoring** is vital for success both in the short and long term.

Figure 2
Companies want a quality workforce

People skills and availability scores



The Impact of the Economic Crisis

Although past figures indicate healthy growth in the offshoring sector, like all other sectors it is being hit by the economic crisis. The full effects of the crisis remain far from known, but early signs suggest that offshoring growth has already slowed. For example, the Indian software association NASSCOM has revised down its industry growth figures for 2009. The value of new offshoring deals signed worldwide during the three-month period between October 2008 and January 2009, as reported by research service Datamonitor, declined by 38 percent compared to the same period the previous year. Compensation has been

frozen among several outsourcing providers in India and attrition rates have dropped in half compared to the previous year—sure signs that the industry is slowing down.

A major factor driving this decline is the prominence of the financial services industry in offshoring. Forty percent of the activities in Indian service centers are driven by banks, and the meltdown of the banking sector worldwide thus hurts the offshoring sector disproportionally. Banks worldwide have shed 5 percent of their entire workforce during the financial crisis—a quarter-million people; in the United States, it's 8 percent. As the most important customer segment tries to fit into smaller shoes, offshoring providers will certainly suffer.

A different crisis-related issue could come from the various government bailout packages in many countries. Not only have they made banks dependent on government, but these bailouts have led to public resentment, as taxpayers' money is spent on restoring balance sheets. Much as corporate jets and Wall Street bonuses became a hot political issue in the United States, moving offshore to cut costs could become politically controversial. Whether or not offshoring is good corporate strategy, or if it benefits the national economy, will be less relevant than the news headlines. Lawmakers have already inserted provisions in some bailout packages that attempt to limit expansion of offshoring operations for banks receiving government support.

Nonetheless, we do not expect the offshoring trend to reverse anytime soon, not even in the financial sector. Although there will likely be a slowdown in the number of new moves offshore, the "onshoring" of current offshore operations in banking is still rare. Any such attempts will run counter to efforts to keep the banks afloat. Offshore operations are an integral part of the supply chains for most financial services companies. The process of removing offshoring from the equation would be very costly, not taking into account the longer-term loss of savings due to increased labor costs.

New moves offshore have declined considerably, but the percentage of companies with staff in offshore locations may rise as companies lay off staff in onshore locations due to the recession. There are two reasons for this: cost and efficiency. It makes sense to look at high-cost areas first when seeking to contain costs. A prime example is IBM, which in March announced 5,000 job cuts in the United States, while simultaneously transferring many of the affected functions to India. The other reason is efficiency. Offshore centers have in most cases been set up in the past decade and are running on well-developed and standardized procedures. Onshore organizations, on the other hand, have decades of history and may not be fully aligned with operational requirements; thus, they may not be as efficient as offshore centers. Once the economy turns and companies start to grow again, it is likely that the percentage of staff offshore versus onshore will remain constant. We are witnessing a more global workforce as a result of the crisis.

The Findings: Familiar Names at the Top

While there is great volatility in the Index, the top three countries—India, China and Malaysia—have remained the same since the inception of the Index in 2004. While we often see an inverse correlation between costs on one hand, and business environment, and people skills and availability on the other, these three countries are regular outliers, in that they have better scores for the areas of people skills and availability, and business environment than their cost structure suggests *(see figure 3 on page 6).*

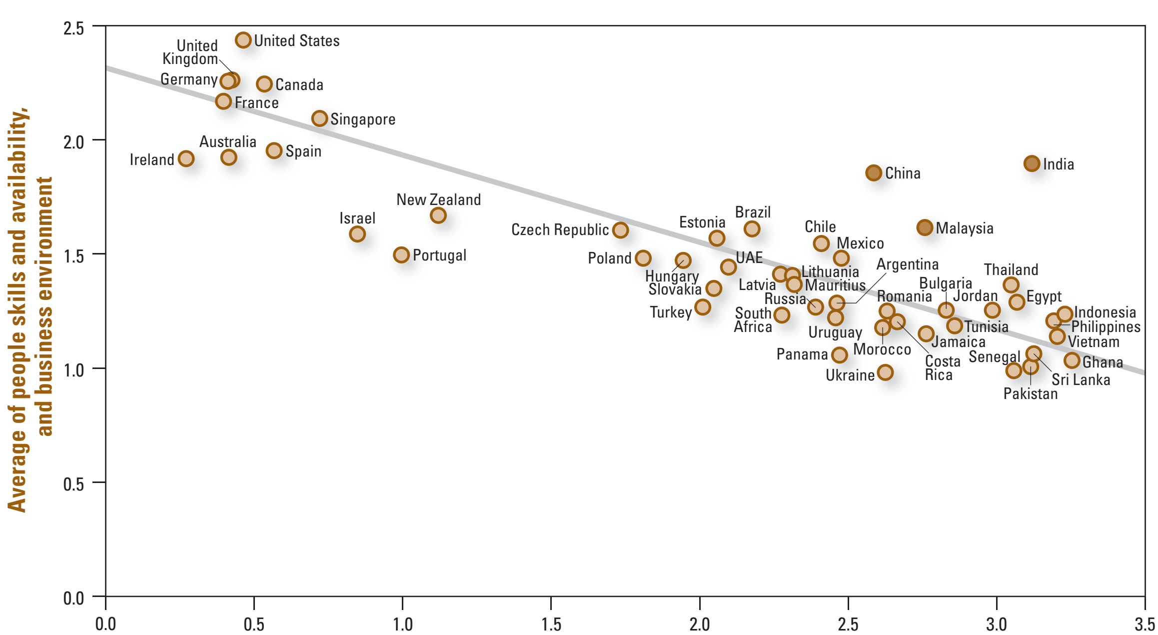
The compensation and other cost data used to build the Index reflect the situation in 2008 when the U.S. dollar was weak in relation to other global currencies (reaching $1.60 to the euro at its lowest point). The Index uses the dollar to measure costs, and compensation data is benchmarked to U.S. wage levels, so the dollar's weakness affects the rankings. This had little effect on the attractiveness of low-cost locations, where compensation costs still remain between a fifth and a tenth of U.S. compensation cost levels. However, medium-income countries experienced an accelerated drop in their relative competitiveness due to the exchange-rate shifts, since their compensation costs are only about half of the American equivalent. Countries whose currency is tied to the dollar—along with, of course, the United States—are the real winners in the Index rankings since 2007, as they have become more competitive against virtually all other countries.

It is important to remember, however, that currencies are volatile. In the first few months of 2009, the dollar is strengthening—to roughly $1.35 to the euro as of mid-May. The stronger dollar will benefit some countries and hurt others, but the main conclusions of our survey still hold, regardless of the changing exchange rates.

Generally speaking, many middle-income countries are suffering because they are converging toward the same cost levels as high-income countries, especially in professions that are part of a global service market. The classic response to rising costs is to increase productivity and value, and improve the business environment, including

Figure 3

India, China and Malaysia are the outliers in financial attractiveness

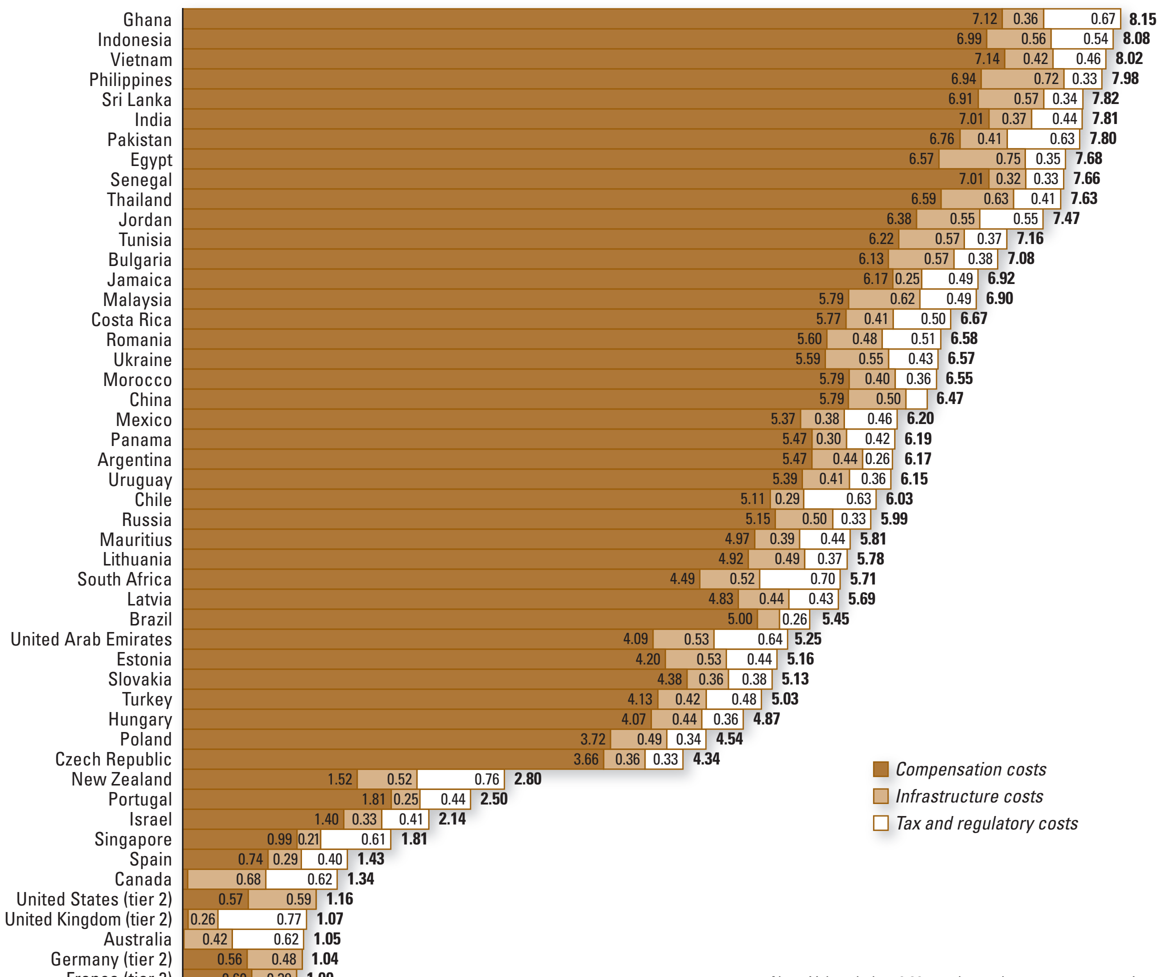


Source: A.T. Kearney

Figure 4

Traditional cost leaders stay the same

Financial attractiveness scores



Note: Values below 0.20 not shown due to space constraints.
Source: A.T. Kearney

infrastructure and intellectual property rights legislation. This helps increase competitiveness. Despite rising costs in these middle-income countries, there is still room to take advantage of labor arbitrage, as our analysis still reveals a clear divide between developed economies and emerging markets in terms of cost *(see figure 4)*.

India: Continued Growth

India remains the leader in the Index, which we expect will continue for the foreseeable future. In just one decade India has transformed and reinvented the outsourcing industry several times over, staying ahead of all trends. India started as a low-cost location that provided routine tasks for

American IT companies, and it still retains a competitive advantage in this area. At the same time, it has moved up the value chain. Today, virtually any offshoring service can be performed in India, and new areas are constantly being invented. These services include routine data entry, finance and accounting, customer-facing functions, and higher-end outsourcing such as knowledge management and legal processes.

While cost remains a major factor in decisions about where to outsource, the **quality of the labor pool is gaining importance.**

In addition, Indian outsourcing companies are beginning to expand across the world, with the largest companies becoming significant players in the United States and Europe. Their own offshore footprint is also rapidly expanding to dozens of other countries, which from the perspective of many other countries, makes India a country that is impossible to compete with head-on. The good news, however, is that India has in many ways ceased to be a competitor and has become an enabler for industry growth in other countries. As India-based outsourcing companies spread across the world, the country is an important player in expanding and pushing offshoring to new frontiers. The expansion has turned Bangalore, Hyderabad and Gurgaon into hubs of the global offshoring universe, with more spokes reaching out to increasingly diverse locations. For example, TCS operates global delivery centers in Argentina, Brazil, China, Hungary, Mexico, Singapore, the United States and Uruguay, in addition to its multiple centers in India. This trend benefits not only India, but it also creates opportunities for the new host countries. When Indian outsourcing vendors Infosys or Wipro set up shop in a new country, they tend to expand more aggressively than most Western multinational corporations, and they also bring with them the expertise to train large numbers of new staff quickly, which gives the local labor pool an immediate boost.

India's outsourcing industry has been shaken by an accounting scandal at Satyam, coupled with safety issues stemming from the 2008 attacks in Mumbai *(see sidebar: Is India Vulnerable?)*. Yet, India will likely remain the unmistakable leader for years to come.

East Asia: Climbing Up in the Rankings

China shares many characteristics with India. Both countries have a large, well-educated workforce with significant labor cost arbitrage opportunities compared to the United States or Japan. However, China still lags far behind India in industry size. A lack of language capabilities, concerns around intellectual property protection and an economy geared toward manufacturing are keeping China from developing into a global offshoring behemoth such as India. For now, China is an important player in the Asia-Pacific offshoring industry, notably with Japanese companies as

its major customers. This may change, however, as the Chinese government recognizes an opportunity and is launching an ambitious plan to support and grow the offshoring industry. China may be able to capitalize on new concerns regarding security in India following the Mumbai terrorist attacks and the Satyam accounting scandal.

Several more Southeast Asian countries figure prominently in the top of the Index, occupying the 3rd, 4th, 5th, 7th and 10th spots. For the fourth year in a row, **Malaysia** is ranked 3rd in the Index. Its strong performance reveals good fundamentals—a safe business environment and high-quality human capital at an affordable price,

Is India Vulnerable?

There is no debate around India's leading position in offshoring, yet, recent events have highlighted that even India is vulnerable. Currency movements, terrorism and a major corporate scandal have made some executives uneasy with India.

Currency movements. Starting in late 2006, the rupee began strengthening against the dollar, trading at 37 rupees per dollar in 2007 as opposed to 47 rupees in 2006. The across-the-board cost increase of almost 30 percent, in dollar terms, created much concern and questions about the sustainability of the Indian offshoring industry. Starting in 2008 the trend reversed when the rupee returned to normal levels—a trend reinforced by the economic crisis as investors flee to safer currencies and the rupee trades at record lows. Although this is good news for the Indian offshoring industry, the currency developments in 2007 show how fast a cost advantage can erode. India will remain cost-competitive for U.S. companies, but its advantage may come under attack from cheaper locations.

Terrorism. While terrorism has been a fact of life in India for a long time, the attacks in Mumbai in November 2008 drove home the risks of operating in India, especially for Western companies. Western interests were deliberately attacked, raising fears that corporate interests could be next on the target list. Though the overall risk may or may not have changed in India, the perception and risk equation in the minds of executives has changed. Continued cross-border tension with Pakistan has not helped. The search for alternative locations to complement the Indian centers has accelerated and there is an opportunity for countries with lower exposure to terrorism, such as China, to capture market share.

Corporate scandals. Adding to the worries, the confidence in India took a hit following the unveiling of a large-scale accounting fraud at Satyam. Much like the Enron debacle shook confidence in corporate America, the Satyam scandal has put the spotlight on Indian corporate governance practices. Given the reliance on Indian outsourcing partners, India will have to reestablish trust in its regulatory environment to prevent such scandals from happening again.

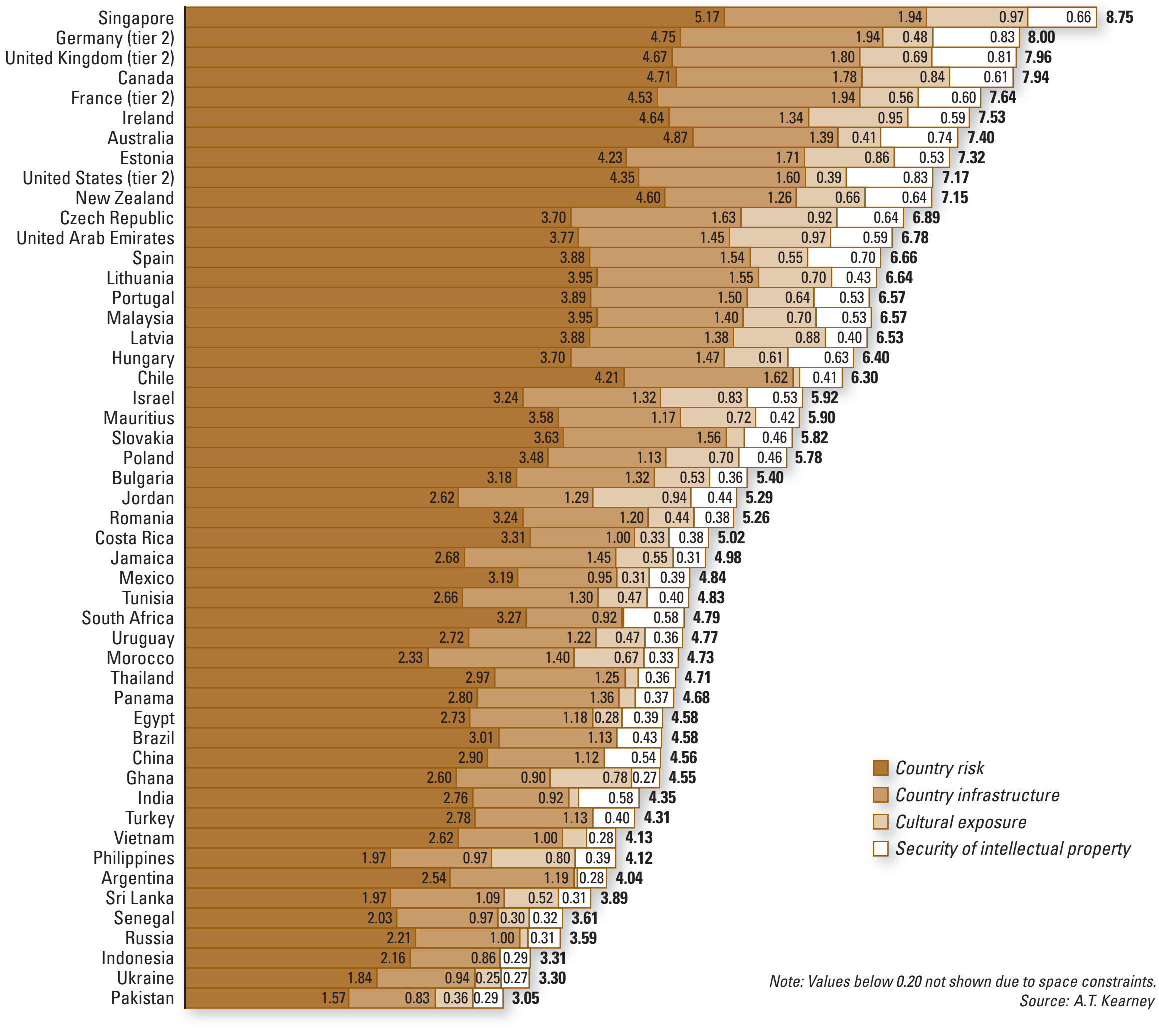
In addition, there have been recent examples of companies abandoning India, returning customer service functions to domestic locations. The world's largest airline, Delta Airlines, announced in April 2009 that it would close its contact centers in India and return these functions to the United States in an effort to improve customer service. Similar centers in Jamaica and South Africa are not affected by the decision. Delta competitor United Airlines announced in February 2009 the relocation of its customer-facing functions from India to Chicago and Hawaii. In a similar move, Dell is now offering a premium technical-support subscription, which guarantees American customers they can talk to customer service representatives in the United States as opposed to India.

Still, India remains indispensible in offshoring and no country or combination of countries can replace it—at least not yet. Nonetheless, these events illustrate India's vulnerabilities and the challenges to staying on top.

Figure 5

Singapore leads in business environment

Business environment scores



and strong government support. The **Philippines** is the second-largest offshoring destination in the world, capturing around 15 percent of the global market, and its leading position is reflected in its 7th position in the Index. It has been home to many contact centers, especially those geared toward the U.S. market, for the past 10 years, but it is now increasingly moving into IT and nonvoice BPO services.

Sri Lanka and **Pakistan** both climb the ranks this year, assisted by low costs in a world with otherwise rising costs. While Pakistan is held back by the continued political instability and country risk (it ranks as the riskiest country in the Index),

Sri Lanka has started to take off as an offshoring destination, steadily expanding since HSBC established a base there in 2005. The risks associated with a civil war and relatively weak English-speaking capabilities (as compared with India) are still obstacles for Sri Lanka. However, its advantages—including its proximity to India and a supply of chartered accountants trained on the same accounting standards used in the United Kingdom—allow the country to function as a backup to Indian centers.

Thailand and **Indonesia** share many similar characteristics with the Philippines but the English skills in the Philippines account for the dramatic difference in industry size. However, as part of the takeover of Philips' captive offshoring operations, Infosys gained a foothold in Thailand, hailing the move as the addition of "another low-cost location that is not plagued with attrition and wage hyperinflation." Given the strong fundamentals of these countries, it is our view that the offshoring industry in Thailand and Indonesia could offer companies a large pool of largely untapped talent at a low cost. Thailand and Indonesia could be in a position to compete for business that is currently going to the Philippines.

Vietnam is a country to watch as it climbs the rankings nine spots into 10th place. This change reflects an increasingly busy offshoring industry, especially focused on IT. Japanese companies have outsourced IT services work to Vietnam for several years. Japan's preferences for Vietnamese IT providers prompted Russia's Luxoft, an IT outsourcer, to open a center in Ho Chi Minh City, with the explicit purpose of targeting the Japanese outsourcing market. Singapore has the best business environment score in the Index, well ahead of second-place Germany *(see figure 5)*. It is home to business continuity and disaster recovery sites for IBM and Hewlett-Packard, among other companies.

Central and Eastern Europe: A Sharp Drop

Among the most dramatic changes in this year's Index is the decline in rankings of the established Central and Eastern European (CEE) countries that were global leaders just a few years ago. The

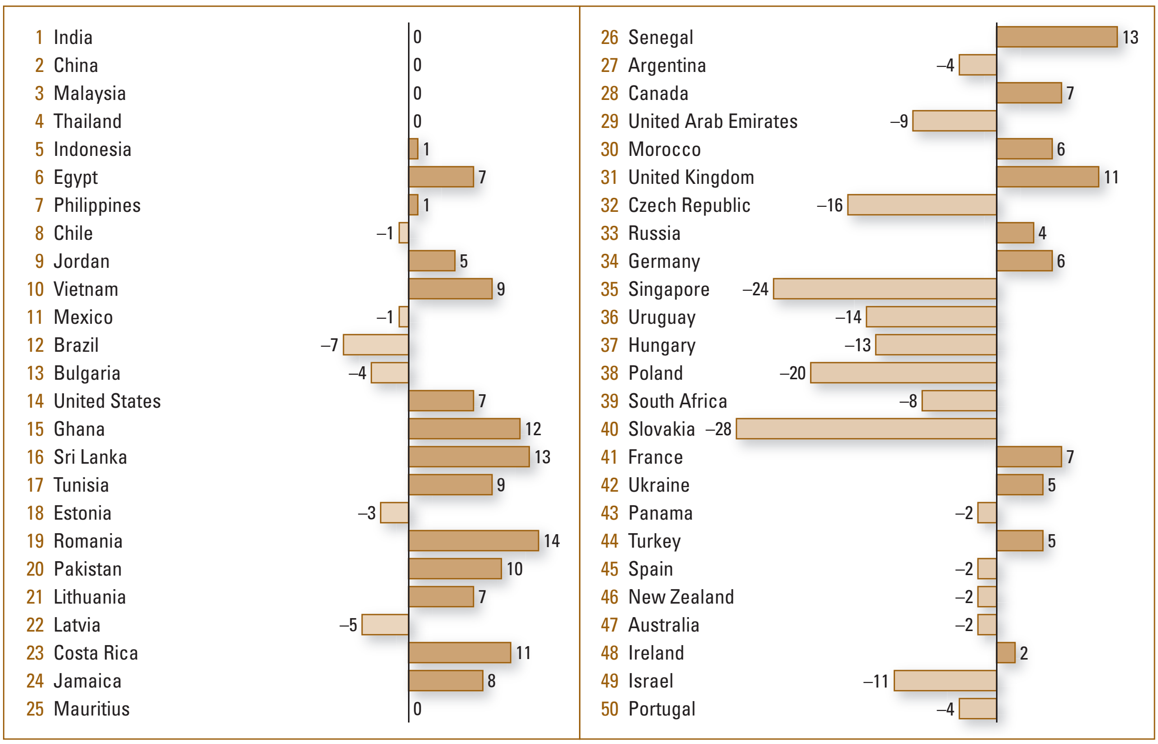
Regional Offshoring on the Rise

While offshoring is often understood as a phenomenon in which companies in developed countries outsource work to low-cost countries, the global offshoring landscape is far more complex than that. Just as it makes sense for advanced economies in North America and Europe to trade business services with lower-cost countries, it also makes sense for low-cost countries to offshore to each other.

In the Middle East, Egypt has supplied skilled migrant labor to the countries in the Gulf region for decades. As improved telecommunications allows for remote delivery, some of these skilled laborers can deliver their services without leaving their home country. Saudi software companies, including Saudisoft, Harf and Sakhr, and Kuwaiti ITS, established their IT development centers in Cairo. Local Egyptian systems integrators sell more services in the Gulf markets, supplying much of the development work from their home offices.

Mauritius is a service exporter to Europe. Now, several local Mauritius companies that provide BPO services to France have opened up their own offshore centers in nearby Madagascar. By doing so, these companies augment their service offerings by hiring French-speaking workers at significantly lower costs.

Figure 6
Changes in Index rankings (2007 to 2009)



Source: A.T. Kearney

Czech Republic was 4th in the 2004 Index and now ranks 32nd. **Hungary, Slovakia** and **Poland** experienced similar falls in their rankings *(see figure 6).* The main reasons for the falls are rapid increases in costs, driven partly by currency appreciation against the dollar and wage inflation, which hampers these countries' competitiveness in lower-end BPO activities. The glimmer of good news is that the price increase has been less dramatic for customers that operate in euros—the majority of the CEE customer base.

The winners in Europe are **Bulgaria** and **Romania,** which continue to stay comfortably in the upper half of the Index, at 13th and 19th, respectively. Members of the European Union but with a lower cost profile than most other member states, they are the new offshoring stars in Europe. Bulgaria provides a great example for creating niche capabilities—for example, when Outsource Partners International established a BPO center to cater to the global shipping industry, they selected the Bulgarian port city of Varna, where they could find the relevant expertise. In Romania, Swedish telecom company Ericsson established a global delivery center, exclusively employing engineers.

At the same time, the Baltic countries are also emerging as alternatives to the Central European countries. **Lithuania** made great advances in the Index this year and now ranks 21st. It specializes in contact centers serving the European market,

providing services in English, German, Russian, Polish and the Scandinavian languages. Today 3,000 people are employed in the sector. **Russia** has lost some of its attractiveness due to the increasingly volatile political environment and rapidly escalating costs, particularly in Moscow and St. Petersburg.

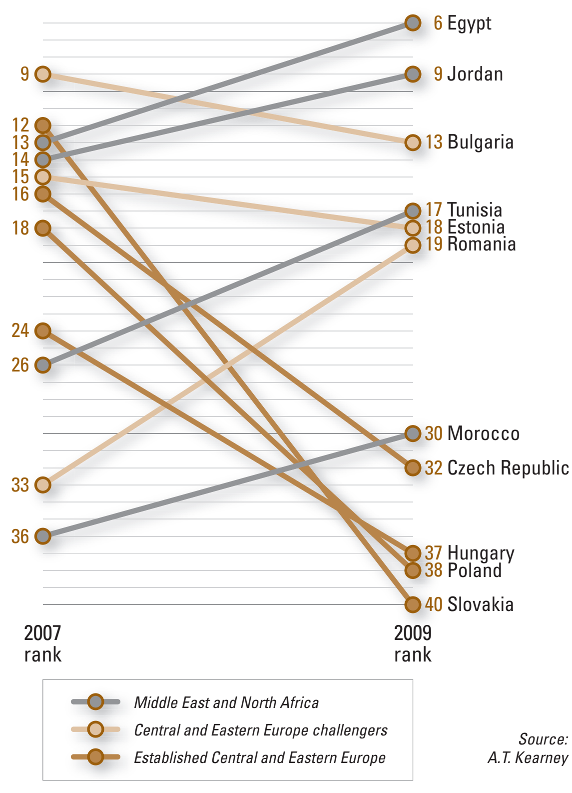
Middle East and North Africa: Hot Destinations

The Middle East and North Africa (MENA) region is emerging as a hot offshoring destination for the world. Home to large, well-educated populations, with low costs and proximity to Europe, the area has the potential to redraw the offshoring map and in the process bring much-needed opportunities *(see figure 7)*.

In 2004, the only Middle Eastern countries considered in the Index were Israel and Turkey—now, five more MENA countries make the list. Egypt, which debuted in the 2005 Index at 12th place, is now 6th. American IT giants IBM and EDS have had operations in Egypt for some time, but now Wipro and Infosys are aggressively expanding into Cairo, taking advantage of the availability of low-cost, qualified people. Egypt is also a service provider for companies in other Middle Eastern countries *(see sidebar: Regional Outsourcing on the Rise on page 11)*. Jordan, at 9th place, is another top performer, as it has solid capabilities in IT and is home to numerous successful outsourcing companies that compete internationally. It also has one of the region's most favorable business environments. The currencies of Jordan and Egypt are closely linked to the dollar, and their competitiveness is strengthened by a weak dollar.

The **United Arab Emirates** (29th place) is a major regional hub for IT services and headquarters functions, and the government-sponsored Dubai Internet City is further facilitating the IT industry. In North Africa, Tunisia and Morocco, ranking 17th and 30th, respectively, have long been destinations for French offshoring services. Morocco is the clear leader in French language offshoring, with approximately half the francophone market. The country has 25,000 jobs in the sector. The government is a strong backer of the industry and has invested heavily in the sector to support sustained growth. Dell, the U.S.-based computer maker, is providing services to its French customers from a contact center in Casablanca, and Spanish Telefónica has a near-shore center in the north of Morocco, just a short distance from Spain across the Strait of Gibraltar.

Figure 7
Middle East and North Africa gain popularity



Source: A.T. Kearney

Sub-Saharan Africa: Growing Markets

Despite the smallest labor force in the Index, the island nation of **Mauritius** ranks favorably at 25th overall thanks to strong people skills and a favorable business environment. Located east of Madagascar, Mauritius has created a favorable business climate. According to the World Bank's Doing Business report, it is the 24th most attractive business environment globally. HR outsourcing company Ceridian has several hundred positions serving the francophone market in the CyberTower, the government-sponsored technology park. Accenture and Infosys also use Mauritius for their global delivery functions.

South Africa is the largest offshore destination in Africa by far, operating a successful contact center cluster in Cape Town along with several R&D operations around its aerospace hub in Pretoria. This year, South Africa dropped to 39th place in the rankings after it lost points in all three categories; the deterioration in infrastructure was the most striking drop among individual metrics. In **Ghana,** 50 companies are members in the national IT association GASSCOM, including U.S.-based IT services company ACS, which employs 1,800 people in Ghana.

Latin America and the Caribbean: Capitalizing on Proximity

The top three countries in Latin America, Chile, Brazil and Mexico, are still doing well. This year, **Chile** is the Latin American leader, ranking 8th in the Index. Its political stability and favorable business environment are key differentiators, and it is in the process of joining the Organisation for Economic Co-operation and Development (OECD), a symbolic entry into the club of advanced economies. Its main strengths are in the high-value-added area, which has boosted IT services companies such as Oracle and TCS, and knowledge process outsourcing (KPO) activities in IT and biotech. For example, KPO provider Evalueserve serves U.S. banks with investment research and financial analytics out of the coastal city of Valparaiso.

In **Brazil**, the software organization Brasscom is promoting the country's strong domestic base of IT companies to overseas clients. Brazil is still showing strong performance in the Index at the number 12 spot and it will continue to be an important player in the offshore space. Red tape continues to be a concern, particularly the services and export taxes that inhibit growth for the offshore industry.

> Countries whose currency is tied to the weakening dollar—along with, of course, the United States—are the real winners in the Index rankings, as they have become more competitive against virtually all other countries.

Mexico, holding steady in 11th place, is increasingly viewed by American companies as a complement to Indian operations. The devaluation of the peso has helped to hold up the ranking, even while companies are wary of the security situation. Similar to the American manufacturing industry, the services sector considers Mexico's proximity and accessibility an advantage. Mexico's size also allows multiple cities to be offshoring hubs, giving the labor market greater depth than in countries relying only on one national center. Its large labor pool is developing English language skills, not to mention its ability to serve the growing U.S. Hispanic consumer market.

Argentina, at 27th place, has enjoyed a favorable cost environment since the devaluation of the peso in 2001, but inflation is slowly eroding its competitiveness, which means the country will have to rely on higher-end functions to compete with other locations. **Uruguay,** in 36th place, occupies a niche in the financial services outsourcing market thanks to the strong banking sector in Montevideo and the availability of trained professionals.

Jamaica is an offshoring leader in the Caribbean due largely to its English-speaking population, government incentives for the industry and proximity to clients in the United States. The country now has more than 15,000 outsourcing employees. Its 24th place ranking indicates the increasing popularity of the Caribbean islands as offshore destinations. One spot ahead of Jamaica is **Costa Rica,** an established player that is still adding new investors, including online retailer Amazon, which opened a contact center in Heredia in 2008. Several other Latin American countries that are not yet in the Index are also developing attractive offshoring markets *(see sidebar: New Players on the Offshore Field).*

Developed Countries: More Onshoring?

Since the onset of offshoring, there has been considerable debate about its impact on importing countries. Many believe that offshoring is a race to the bottom, with employment and wage levels in

New Players on the Offshore Field

While the same 50 countries from the 2007 Index are in this year's Index, we are keeping an eye on new countries entering the offshoring playing field, and we expect some of them to enter future rankings. For example, there has been considerable activity in Latin America, where countries such as Guatemala and El Salvador are starting to focus on attracting U.S. near-shore dollars. In South America, Colombia is attracting offshoring investments, and the sector has been identified as a focus area in the government's future growth initiative.

Several Caribbean islands are hoping to become niche players; the Dominican Republic and Barbados already have centers up and running. In South Asia, Bangladesh is creating the necessary framework to accommodate the offshoring industry. More surprisingly, Bhutan, which until recently was closed to the world, is actively planning to capture Indian IT company investments. Indian software association NASSCOM's decision to hold an executive meeting in the kingdom in late 2008 was an early public relations success. In Kenya, KenCall is leading a nascent industry with clients in both the United States and the United Kingdom. Other African countries can also emerge as successful candidates in this space in the future.

developed countries suffering, especially in occupations exposed to international competition. The current economic crisis will no doubt create more concerns.

However, research indicates that developed countries and their companies have gained from offshoring. New research also indicates that professionals in developed countries have not seen their positions deteriorate as a result of offshoring. A study by Bradford Jensen and Lori Kletzer at the Institute for International Economics reveals that both employment and wages in tradable services occupations have not only increased between 1996 and 2006—but also increased *faster* than wages in nontradable service occupations.[2] While specific offshoring moves may have an impact on individuals, there is a good case that the globalization of trade in services has been on the whole positive for professionals in both exporting and importing countries. This is worth keeping in mind as calls for protectionism grow stronger.

In just one decade **India has transformed and reinvented the outsourcing industry** several times over, staying ahead of all trends.

For the third year in a row, we are including in the Index tier-2 locations in France, Germany, the United Kingdom and the United States. These countries have set up operations in lower-cost locations to perform domestic remote delivery functions. The cities used to represent tier-2 locations are based on regional cost data: Marseilles in France; Leipzig in Germany; Belfast in the United Kingdom; and San Antonio in the United States.

The **United States** dramatically improves its ranking in this year's Index thanks to the weakening dollar. Fourteenth overall, the United States is also the leader in the people skills and availability category, not surprisingly given its large and educated labor force working in the world's largest ITO and BPO industry sector. Although the dollar has regained strength in 2009, there is increased interest in onshoring in the United States, as the economic crisis has rendered offshoring politically sensitive and, at the same time, rising unemployment rates increase the number of available workers. U.S. tier-3 locations are becoming a new option for voice and nonvoice BPO services, as the costs in the U.S. hinterlands are lower than they are in the major cities. Regional development agencies in U.S. states are catching on to this trend and marketing their regions as "at home" offshore destinations.

The **United Kingdom, Germany** and **France** have all risen slightly in the rankings (31st, 34th and 41st, respectively), due more to other countries falling in the ranks than their own improvements. However, crisis-related political considerations and the availability of qualified labor may create an

[2] *Jensen, Bradford & Lori Kletzer,* "Fear" and Offshoring: The Scope and Potential Impact of Imports and Exports of Services, *Peterson Institute for International Economics Policy Brief, January 2008.*

onshoring movement in Europe similar to that of the United States, or at least delay further moves from domestic to offshore locations.

Rapidly Changing Offshoring Environments

The geography of offshoring is changing fast. Countries that were safe bets a few years ago and still attract large investments in the industry may already have peaked and be in decline as future destinations. Relatively unknown locations today may be important destinations tomorrow. The number of countries competing for the offshoring business steadily expands and the different niche markets that countries serve multiply. Location decisions are not as straightforward as they used to be.

In addition, the economic crisis is creating further volatility as it reshapes the offshoring landscape. In the short term, the recent decline in growth will continue, and the crisis will likely shake up the current offshoring geography as countries deal with the volatility with varying degrees of success. Over the longer term, the crisis might actually trigger the further globalization of services.

The volatility in the wake of the crisis and geopolitical risk mean that risk management will take on a new importance to protect supply chains from interruption. The offshoring landscape will reveal new opportunities as countries develop new competitive advantages. Companies on the lookout for new sources of talent should perform thorough location assessments so as not to miss under-the-radar locations in a broad range of countries.

Even as the world enters a new era of risk, the opportunities are larger than ever. As the global labor pool becomes more accessible, and the number of countries courting investors grows, the rewards will go to those companies first to identify them.

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Appendix: About the Study

The 50 countries included in this year's Global Services Location Index were selected on the basis of corporate input, current remote services activity, and government initiatives to promote the sector. They were evaluated against 43 measurements across three major categories: financial attractiveness, people skills and availability, and business environment *(see figure)*.

The metrics used to evaluate location attractiveness were determined from responses to A.T. Kearney and other industry surveys, and knowledge obtained in client engagements over the past five years. The relative weights of each metric are based on their importance to the location decision, again derived from client experience and industry surveys. Because cost advantage is typically the primary driver behind location decisions, financial factors constitute 40 percent of the total weight in the Index. The two remaining categories—people skills and availability, and business environment—each constitute 30 percent of the total weight.

Index metrics

Category	Subcategories	Metrics
Financial attractiveness (40%)	Compensation costs	• Average wages • Median compensation costs for relevant positions (call-center representatives, BPO analysts, IT programmers and local operations managers)
	Infrastructure costs	• Rental costs • Commercial electricity rates • International telecom costs • Travel to major customer destinations (New York, London and Tokyo)
	Tax and regulatory costs	• Relative tax burden • Corruption perception • Currency appreciation or depreciation
People skills and availability (30%)	Remote services sector experience and quality ratings	• Size of existing IT and BPO sectors • Contact center and IT center quality certifications • Quality ratings of management schools and IT training
	Labor force availability	• Total workforce • University-educated workforce • Workforce flexibility
	Education and language	• Scores on standardized education and language tests
	Attrition risk	• Relative IT and BPO sector growth and unemployment rates
Business environment (30%)	Country environment	• Investor and analyst ratings of overall business and political environment • A.T. Kearney Foreign Direct Investment Confidence Index™ • Security risk • Regulatory burden and employment rigidity • Government support for the information and communications technology (ICT) sector
	Infrastructure	• Overall infrastructure quality • Quality of telecom, Internet and electricity infrastructure
	Cultural exposure	• Personal interaction score from A.T. Kearney Globalization Index™
	Security of intellectual property (IP)	• Investor ratings of IP protection and ICT laws • Software piracy rates • Information security certifications

Source: A.T. Kearney

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