The CIO Insight

Whiteboard

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The Global Outsourcing Report

Opportunities, Costs and Risks

Despite the supercharged politics surrounding the issue, outsourcing IT offshore has become a fact of life, and it's growing quickly. Why? Because despite the difficulties, offshoring can provide huge benefits in terms of productivity, prices, profits and wages—an irresistible combination in a highly competitive world. A natural evolution of how the global marketplace operates today, offshoring is on the way to becoming a mainstream business. And the future for outsourcing looks even brighter.

Still, offshore outsourcing brings with it a wide variation in costs from country to country, as well as significant risks—geopolitical, economic, legal, cultural, and IT infrastructure and competency—and companies making decisions about where to outsource must take these into account. The goal of this whiteboard is to provide a thorough country-by-country analysis of the current outsourcing market, and to point out where to find the best opportunities for a variety of services. The result is the Global Outsourcing Index, which rates each country on the basis of a combination of relative cost, risk, and market opportunity. And because the world is changing so fast, the whiteboard also looks at where offshoring opportunities can be found in the future.

The trend toward offshore outsourcing is a lot more complex than simply seeking skills and resources in the lowest-cost locations. The driving forces in the IT outsourcing market are quality and speed to market, not just cost of services.

A new wave of outsourcing is allowing companies to acquire reliable IT quickly, in order to deploy specialized services, and ramp down easily when these services are no longer needed.

At the same time, offshoring is pushing the world beyond the information economy and toward a global knowledge-based economy. Technology enables knowledge to be shared quickly throughout the developed and developing world, allowing a variety of regional specializations to arise.

The Top Three

	2005	2015
1	India	China
2	China	India
3	Costa Rica	U.S.A.

These trends are conspiring to bring further changes to the global outsourcing market in the next decade or so. First of all, consumer demand and spending power in the emerging economies is growing more quickly than expected. And as they grow in strength and stability, the risks of outsourcing can be spread further as companies have a wider variety of geographic locations to choose from.

In the future, many companies will not outsource to a particular country at all. Instead, they will turn to large multinational corporations with access to a variety of resources and expertise across the globe and the ability to spread risk. As these one-stop shops grow in size and skills, they will gain a significant competitive advantage over even the strongest individual outsourcing markets.

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TURN AND FOLD OUT TO VIEW WHITEBOARD

THE GLOBAL OUTSOURCING REPORT: Opportunities, Costs and Risks

HOW TO READ

The goal of this whiteboard is to provide the reader with a country-by-country guide to the worldwide outsourcing market, its opportunities, costs and risks. It was compiled from surveys and interviews with outsourcing, economics and business experts.

The 20 countries we analyzed are ranked along the top of the chart in their order of finish in the Global Outsourcing Index (GOI), which rates each country according to its competitiveness as an outsourcing destination. The index comprises three main factors:

Cost: Few companies would outsource at all if doing so didn't save them money. The cost factor, which includes compensation and wages, infrastructure cost, and tax and regulatory cost, makes up 30 percent of the GOI.

Risk: Every country possesses its own strengths and weaknesses, risks and rewards. The Overall Risk Rating, which makes up 54 percent of the GOI, aggregates a variety of risks every potential outsourcer must take into account:

Geopolitical risk (10% of GOI)
Includes stability of government, corruption, geopolitics, security.

Human capital risk (10%)
Includes quality of educational system, labor pool, number of new IT graduates.

IT competency risk (10%)
Includes project management skills, high-end skills and competence (custom code writing, system writing, R&D, business process experience).

Economic risk (6%)
Includes currency volatility, GDP growth.

Legal risk (6%)
Includes overall legislation, tax, intellectual property.

Cultural risk (6%)
Includes language compatibility, cultural affinities, innovation, adaptability.

IT infrastructure risk (6%)
Includes IT expenditure, quality of key access infrastructure.

Market Opportunity Rating: This number, which makes up 16 percent of the GOI, includes expert third-party analysis of each country, its global competitiveness and IT market share. The rating serves as a check on any imbalances elsewhere in the report.

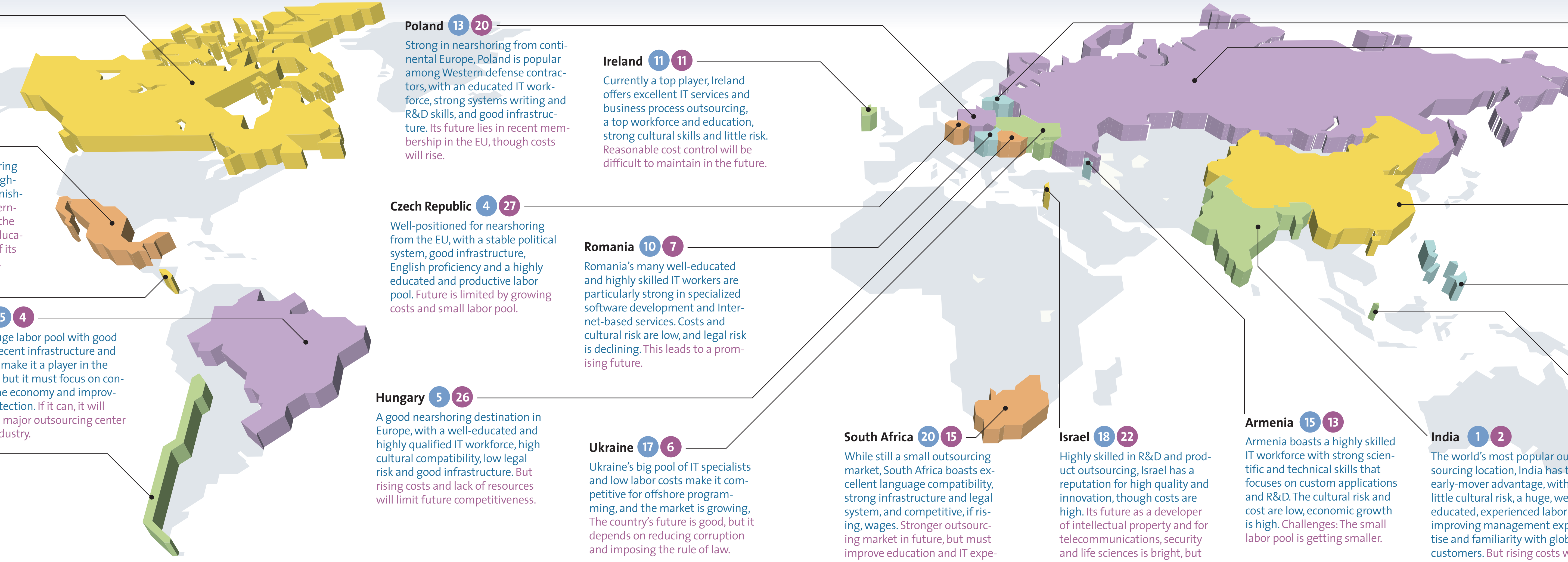
Finally, the map itself includes brief descriptions of the strengths, weaknesses and future prospects of each country in the GOI.

Rating: 1 2 3 4 5

Cost, risk and market opportunity are rated on a scale of 1 to 5, where 1 is the least risk and 5 is the greatest.

Notes: For a list of the experts who contributed to this whiteboard, please see page 97. For the complete report, log onto www.cioinsight.com/whiteboard and click on the Global Outsourcing Report.

Global Outsourcing Rank	1	2	3	4	5	6	6	6	9	10	11	11	13	13	15	15	17	18	19	20
Global Outsourcing Index (GOI)	2.02	2.16	2.24	2.26	2.28	2.40	2.40	2.40	2.42	2.46	2.50	2.50	2.56	2.56	2.58	2.58	2.74	2.76	2.78	2.86
Country	India	China	Costa Rica	Czech Republic	Hungary	Canada	Latvia	Russia	Chile	Romania	Ireland	Singapore	Philippines	Poland	Armenia	Brazil	Ukraine	Israel	Mexico	South Africa
Cost	$$	$	$$	$$$	$$$	$$$$$	$$$	$$	$$$	$$	$$$$$	$$$$$	$$	$$$	$	$$$	$$	$$$$$	$$	$$$$
Geopolitical risk	3	3	2	1	1	1	2	3	2	2	1	1	3	2	3	2	3	3	2	3
Human capital risk	1	1	2	2	2	1	2	1	3	2	2	2	1	2	3	2	2	2	3	3
IT competency risk	2	4	3	2	2	1	2	2	3	2	1	1	4	2	3	2	3	1	5	2
Economic risk	1	1	2	3	3	2	3	2	2	3	2	3	3	3	2	2	2	3	3	2
Legal risk	3	5	3	2	2	1	2	5	2	5	1	1	4	3	4	4	5	1	3	2
Cultural risk	1	4	2	2	2	1	2	3	2	2	1	1	1	2	2	3	3	1	2	1
IT infrastructure risk	4	3	2	2	2	1	2	2	2	3	1	1	3	2	4	3	2	1	3	3
Overall Risk Rating	2.1	2.9	2.3	1.9	1.9	1.1	2.1	2.4	2.4	2.6	1.3	1.4	2.7	2.2	3.0	2.4	2.8	1.8	3.1	2.4
Market Opportunity Rating	1.8	1.8	2.5	2.0	2.1	1.9	2.3	3.0	1.5	3.0	1.9	1.5	3.1	2.9	4.1	2.3	3.9	1.9	3.3	2.4
Future Outsourcing Rank	2	1	30	27	26	10	28	5	14	7	11	29	9	20	13	4	6	22	19	15



Canada 6 10
A low-risk, high-cost world leader in IT outsourcing, specializing in call centers and BPO. Canada will remain competitive thanks to specialized high-level R&D and BPO services. But it will have to work hard on lowering cost structures.

Mexico 19 19
Mexico is a strong nearshoring destination for low-level, high-volume IT projects and Spanish-language BPO. But the government needs to strengthen the economy and improve IT education and the competency of its labor pool to keep growing.

Costa Rica 3 30
Ideal for outsourcing from the U.S., with low costs, good infrastructure and a well-educated, if small, labor pool. But its small size and lack of resources will cause a precipitous drop in competitiveness in the future.

Brazil 15 4
Brazil's huge labor pool with good IT skills, decent infrastructure and low costs make it a player in the Americas, but it must focus on controlling the economy and improving IP protection. If it can, it will become a major outsourcing center for U.S. industry.

Chile 9 14
Very competitive Spanish-speaking offshoring services, with a stable economy, high level of education, low costs and good infrastructure. While growth is limited by scarce manpower and rising costs, Chile will remain an attractive outsourcing market.

Poland 13 20
Strong in nearshoring from continental Europe, Poland is popular among Western defense contractors, with an educated IT workforce, strong systems writing and R&D skills, and good infrastructure. Its future lies in recent membership in the EU, though costs will rise.

Ireland 11 11
Currently a top player, Ireland offers excellent IT services and business process outsourcing, a top workforce and education, strong cultural skills and little risk. Reasonable cost control will be difficult to maintain in the future.

Czech Republic 4 27
Well-positioned for nearshoring from the EU, with a stable political system, good infrastructure, English proficiency and a highly educated and productive labor pool. Future is limited by growing costs and small labor pool.

Romania 10 7
Romania's many well-educated and highly skilled IT workers are particularly strong in specialized software development and Internet-based services. Costs and cultural risk are low, and legal risk is declining. This leads to a promising future.

Hungary 5 26
A good nearshoring destination in Europe, with a well-educated and highly qualified IT workforce, high cultural compatibility, low legal risk and good infrastructure. But rising costs and lack of resources will limit future competitiveness.

Ukraine 17 6
Ukraine's big pool of IT specialists and low labor costs make it competitive for offshore programming, and the market is growing. The country's future is good, but it depends on reducing corruption and imposing the rule of law.

South Africa 20 15
While still a small outsourcing market, South Africa boasts excellent language compatibility, strong infrastructure and legal system, and competitive, if rising, wages. Stronger outsourcing market in future, but must improve education and IT experience and skills.

Israel 18 22
Highly skilled in R&D and product outsourcing, Israel has a reputation for high quality and innovation, though costs are high. Its future as a developer of intellectual property and for telecommunications, security and life sciences is bright, but expensive.

Armenia 15 13
Armenia boasts a highly skilled IT workforce with strong scientific and technical skills that focuses on custom applications and R&D. The cultural risk and cost are low, economic growth is high. Challenges: The small labor pool is getting smaller.

India 1 2
The world's most popular outsourcing location, India has the early-mover advantage, with little cultural risk, a huge, well-educated, experienced labor pool, improving management expertise and familiarity with global customers. But rising costs will limit future competitiveness.

Russia 6 5
Russian IT offshoring is growing, with a focus on niche software companies. The country boasts a highly skilled, creative workforce; drawbacks include poor government support and poor enforcement of IP. Will focus successfully on creative solutions and R&D services in the future.

Latvia 6 28
Excellent outsourcing destination: good infrastructure and skills, highly educated labor pool with strong software development skills. But costs are growing, thanks to EU integration and limited labor pool; will likely remain a minor player, together with Estonia and Lithuania.

China 2 1
China's software and services offshoring is still in its infancy. It lags behind India in work experience and project management skills, and legal risk is high, with piracy rampant. But it's catching up fast, and its sheer size will push it to No. 1.

Singapore 11 29
A successful high-end niche player, with excellent infrastructure, good technical talent, strong education and a pro-business environment. But it is costly, and becoming more so. That will limit growth to specialized outsourcing in fields like microtechnology and biotechnology.

Philippines 13 9
The Philippines offers a well-educated labor pool and low-risk offshoring, with strong BPO, close cultural compatibility and good infrastructure. Less political insurgency and better IP protection, combined with low cost, will make the future bright.

Outsourcing in the Future

The Future Outsourcing Rank compares each country by its competitive position in the overall outsourcing market as it will look in ten years, based on such factors as population growth, GDP growth, labor supply and IT expertise. As the bottom row of the country listings shows, China will rise to No. 1, while India will drop to No. 2. The U.S. will enter the list at No. 3, thanks to competitively priced high-value offerings. Countries such as Israel and Singapore will become much less competitive because they won't be able to slow rising costs, while others, such as Costa Rica, will struggle to remain competitive because they'll be unable to maintain the population growth and skilled workforces necessary to remain attractive. Here is a ranking of the countries not currently included in the Global Outsourcing Index that should rise to the top 30 over the next ten years:

- 3 U.S.A.
- 8 Belarus
- 12 Malaysia
- 16 Thailand
- 17 Vietnam
- 18 Moldova
- 21 Bulgaria
- 23 Pakistan
- 24 Kazakhstan
- 25 Albania

The Rise of the Multinationals

The Global Outsourcing Report only ranks countries active in outsourcing now and in the future. Among the major trends over the next ten years, however, is the growth of multinational outsourcers—large corporations with the capacity to go anywhere in the world for the skills their clients need. In ten years, they will actually become the second most attractive outsourcing option, after China, not just because of their wide-ranging outsourcing options, but because they will be better able to spread the costs and risks of outsourcing, relieving many corporations of the need to make country-by-country decisions.

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