DUKE THE FUQUA SCHOOL OF BUSINESS

OFFSHORING RESEARCH NETWORK

IS THE GLOBAL OUTSOURCING INDUSTRY IN FOR A NO-HOLDS-BARRED COMPETITION?

2009 ORN SERVICE PROVIDER SURVEY REPORT

Is the global outsourcing industry in for a no-holds-barred competition?

Since its inception in 2004, Duke University's Offshoring Research Network (ORN) project has tracked and reported on the growth of global sourcing for business and information technology (IT) services. Central to these studies has been the observation of aggressive growth of outsourcing and offshoring demand and the shift from the dominant labor arbitrage tactic to a game-changing global sourcing strategy. The ORN 2007/08 annual buy-side survey report, *Offshoring Reaches the C-Suite*,[1] documented the importance of a global sourcing strategy for companies accessing capabilities and talent outside their home country. On the supply side of outsourcing service, the *ORN 2009 Service Provider Survey* documents the transformation taking place on the provider side. The outsourcing industry is being transformed as new entrants around the world rapidly emerge, as countries reshape their national policy to obtain a share of its value, and as incumbent providers attempt to defend their existing market and expand into new markets in order to keep up with the increasing demand and intensified competition.

[1] Heijiman, T., Lewin, A., Manning, S., Perm-Ajchariyawong, N. & Russell, J. (2008) Offshoring Reaches the C-Suite. Duke University & The Conference Board.

Survey profile

The *ORN Service Provider Survey*, initiated in 2007, aims to track service providers along the key dimensions of service offerings, offshore destinations, contract and client relationships, economics, and growth strategies. This survey complements the ORN global corporate client surveys on outsourcing and offshoring and covers large multinational, midsize, and small entrepreneurial service providers (see Chart 1). A closer look at the distribution of client size broken down by size of service provider, shown in Chart 2, reveals that large multinational providers are likely to engage in outsourcing deals with large companies while small service providers are more likely to serve smaller clients.

Survey respondents consist of 514 service providers from 50 countries across 6 continents (see Chart 3). The outsourcing industry has long been dominated by large multinational US and Indian-based service providers, but the *2009 ORN Service Provider Survey* reveals the emergence of service providers from other regions, especially developing countries in Latin America, Eastern Europe, and Asia. New entrants from these emerging regions can be expected to intensify competition among providers, especially for commoditized contact centers, business process outsourcing (BPO), and IT services.

CHART 1
Service provider by size

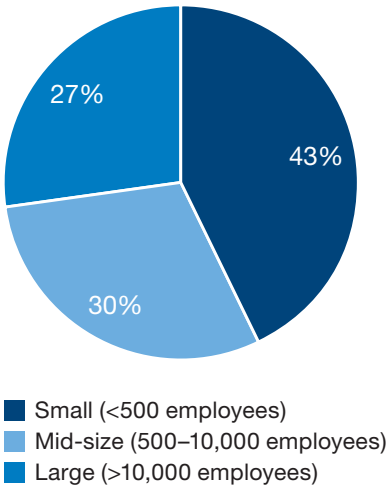
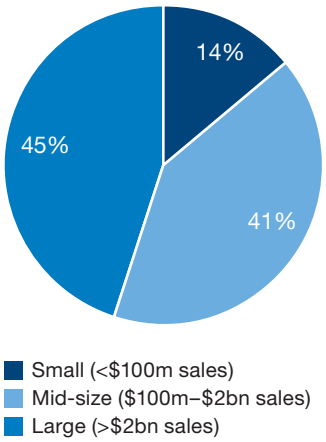
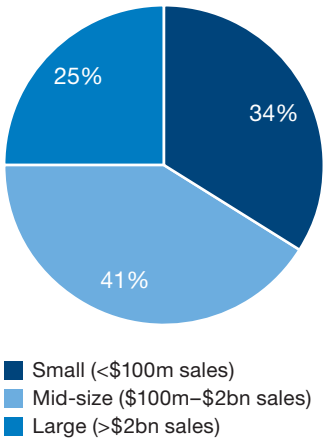


CHART 2
Distribution of client size broken down by size of provider

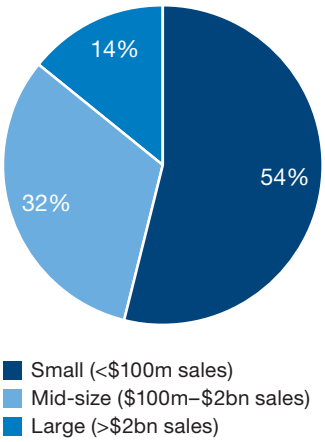
Clients served by large providers



Clients served by mid-size providers



Clients served by small providers



Source:

Duke University Offshoring Research Network 2007/08 Service Provider Survey
Duke University Offshoring Research Network 2009 Service Provider Survey

CHART 3
Distribution of service providers by HQ location (Total number of providers = 514)

Source:

Duke University Offshoring Research Network 2007/08 Service Provider Survey
Duke University Offshoring Research Network 2009 Service Provider Survey

The new game: Countries are bidding for share of the outsourcing market

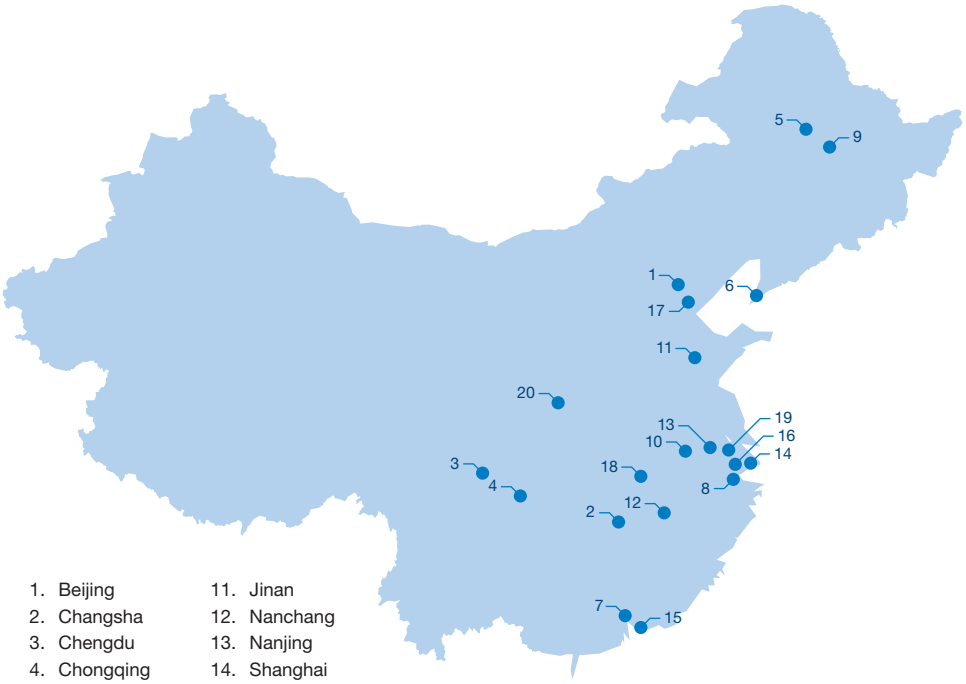
National policies for attracting outsourcing are impacting the market

Traditionally, a discussion about outsourcing and offshoring service has centered on issues concerning the demand for offshore outsourcing. Outside India, the development of an outsourcing industry and competition among service providers and countries has received little attention. However, growing competition among countries, cities, and providers has transformed the outsourcing industry into a global race for market share. India's success and pride as "the world's back office" has motivated other developing countries with a significantly underutilized university-educated population to replicate what India has done. It has reached national policy-making agendas as governments provide incentives to attract outsourcing business. China, for example, has mounted a vigorous challenge to India's software development outsourcing industry. More and more US and European companies are outsourcing software and IT services directly to Chinese service providers. Meanwhile, the Chinese government designated 20 cities as outsourcing hubs to attract more international investment and has provided them with tax breaks, labor hour systems, and employment subsidies (see Chart 4). China's outsourcing demonstration city, Hefei, for instance, has attracted some of the world's top businesses, including IBM, General Electric, Exxon Mobil Chemical, Motorola, and Mitsubishi Heavy Industries to its newly constructed technologic industrial development park. The Philippine government has declared IT-BPO a priority industry and has implemented policies (e.g., formation of economic zones and income-tax holidays) to boost foreign investment.

In the *2009 Service Provider Survey*, we observe several emerging countries—where wages are low, competencies are high, and foreign investment is encouraged—that are making increasingly sophisticated efforts to enter the market and take a share of this fast-growing industry. While incumbents such as India- and US-based service providers still attract a majority of business, the new entrants signal their intent by building up their capability in specific service offerings (see Chart 5). Interestingly, not every new player enters the market by eyeing the low-hanging fruit and working its way up to the high-end innovation and knowledge-related activities. Emerging countries with advantage on low labor costs are entering the highly commoditized market, but those with a pool of educated and skilled population seek to penetrate the high-end markets such as innovation and knowledge process outsourcing (KPO).

The distribution of service providers by headquarter region for each function suggests that apart from Indian and American providers' footprint in contact center service, Western European providers take a nontrivial proportion (16 percent) of share in this mature market. Back-office service and KPO markets, including finance and accounting, marketing and sales, and human resources, have been penetrated by Western European and Asian providers. Western European providers, particularly German providers, play on their strength and specialty in procurement outsourcing. Our survey results show that 21 percent of procurement outsourcing providers are based in Western Europe, with leading Indian service providers accounting for 20 percent of the overall market.

CHART 4
China's twenty service outsourcing demonstration cities

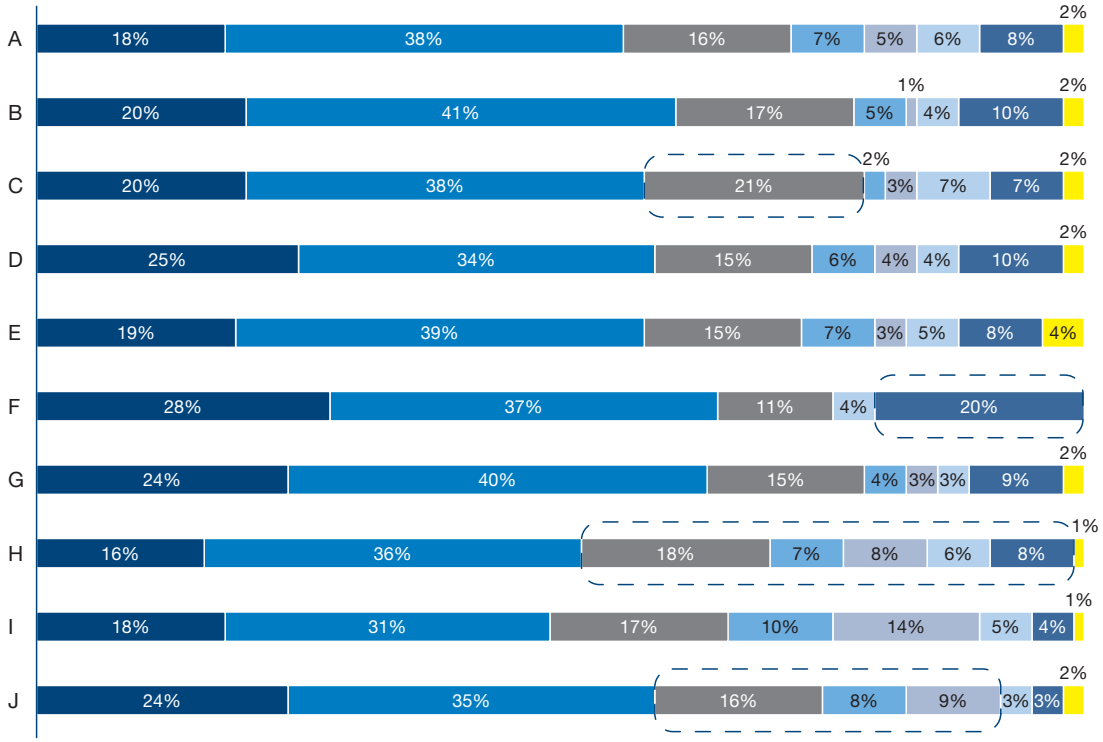


1. Beijing
2. Changsha
3. Chengdu
4. Chongqing
5. Daqing
6. Dalian
7. Guangzhou
8. Hangzhou
9. Harbin
10. Hefei
11. Jinan
12. Nanchang
13. Nanjing
14. Shanghai
15. Shenzhen
16. Suzhou
17. Tianjin
18. Wuhan
19. Wuxi
20. Xi'an

The ORN database indicates that Asian providers, dominated by The Philippines and Sri Lanka, provide 20 percent of legal process outsourcing (LPO), behind only US- and India-based providers. Although India has a well-established position in the LPO market, The Philippines' closer alignment to the US legal system attracts a number of LPO businesses from US companies. Other advantages such as cheaper labor, low cost of living, and a well-educated, English-speaking community are a plus for LPO in the Philippines.

As one would expect, Eastern Europe, Latin America, and China made their move into an outsourcing space by penetrating areas in which they have developed skills and capability, such as software development and IT service outsourcing. Armed with a notable technology-oriented education system and solid research and development foundation, Eastern European countries are positioned as an attractive IT and software development offshore and near-shore outsourcing destination for many Western European firms. Many of these companies are choosing to near-shore IT and software development to less-developed Eastern European countries rather than offshoring to Asian countries. Based on our survey findings, Eastern European providers account for 14 percent of software development providers, only slightly behind Western Europe- and India-based providers at 17 percent.

CHART 5
Distribution of service providers by HQ location for each function



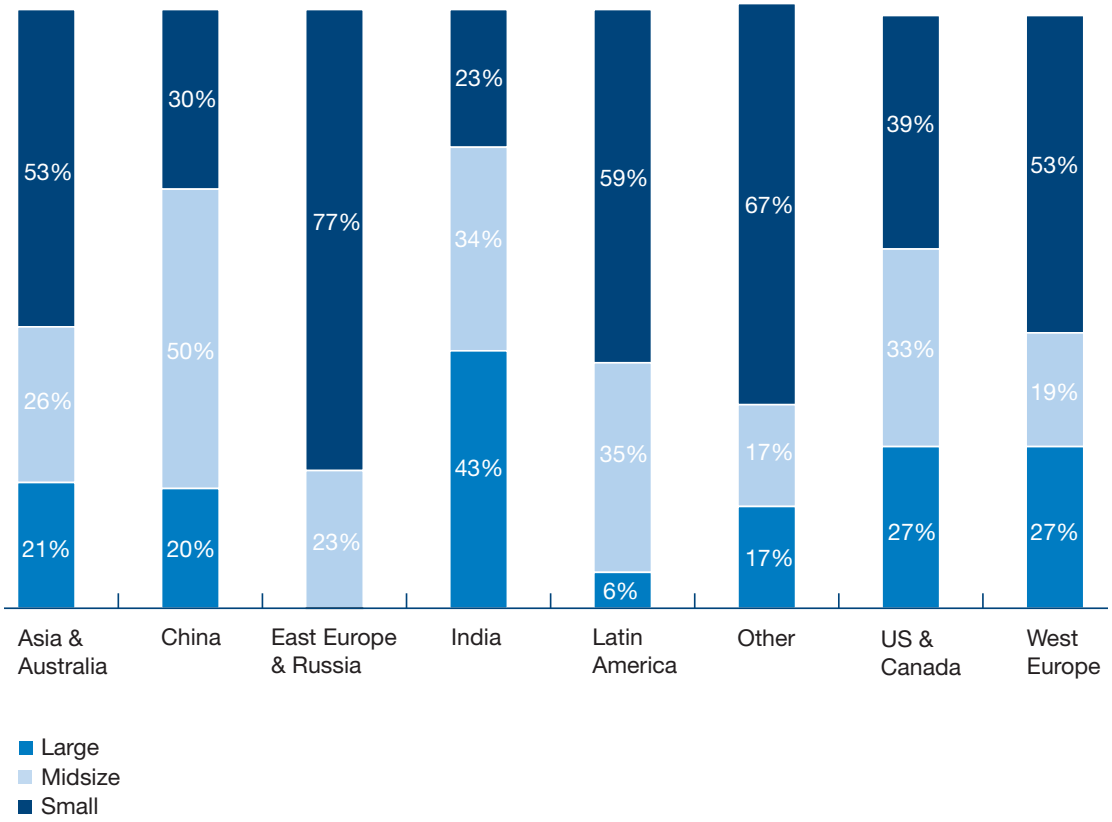
A. Call Centers
B. Finance & Accounting
C. Procurement
D. Marketing & Sales
E. Human Resources
F. Legal Services
G. Knowledge Services
H. Information Technology
I. Software Development
J. Innovation

India
US & Canada
West Europe
China
East Europe & Russia
Latin America
Asia & Australia
Other

Source:

Source: Duke University Offshoring Research Network 2007/08 Service Provider Survey
Duke University Offshoring Research Network 2009 Service Provider Survey

CHART 6
Percent of providers by size in each HQ location



Source:

Duke University Offshoring Research Network 2007/08 Service Provider Survey
Duke University Offshoring Research Network 2009 Service Provider Survey

Increasing trend of consolidation of outsourcing industry

Our analysis of service provider size across regions (see Chart 6) shows that India's mature outsourcing industry is dominated by large service providers with more than 10,000 employees: Large providers account for 43 percent of the overall market in India. In contrast, a majority of service providers in new emerging regions, such as China and Eastern Europe, are small (with fewer than 500 employees) or midsize providers (with 500—10,000 employees). This pattern showing up in the ORN survey largely is supported by an increasingly common phenomenon of outsourcing industry consolidation, suggesting that India's outsourcing industry as a whole is well into the maturity phase of its life cycle.

TABLE 1
Examples of consolidation in outsourcing service industry

Date	Buyer	Seller	Acquired Function	Size of Deal
January 25, 2008	Affiliated Computer Services (ACS)	Syan Holding Limited	IT	$60 million
February 29, 2008	NCO Group	Outsourcing Solutions	BPO	$325 million
April 29, 2008	3i Infotech	Regulus Group		$80 million
May 13, 2008	Hewlett-Packard	Electronic Data System (EDS)	Remittance and Document Processing Services	$13.9 billion
June 10, 2008		Oberon Associates	BPO, IT Application and IT Infrastructure Management	$170 million
July 1, 2008	Quatrro	Media	Biometric System Engineering, IT and Data Management	Undisclosed
July 16, 2008	Allied Digital Services	En Pointe Global Services	BPO	$30 million
July 16, 2008	HCL Technologies	Liberata Financial Services	IT Infrastructure Management and Remote Management Services	Undisclosed
July 16, 2008	WNS	Business Application Associates (BizAps)	BPO	$19 million
July 25, 2008	Capgemini	Getronics PinkRoccade	SAP Solutions for Finance and Accounting	€255 million
August 6, 2008	Essar/Aegis Communications	PeopleSupport	Business Application Services	$250 million
August 26, 2008	HCL Technologies	Control Point Solutions	BPO	$20.8 million
September 19, 2008	Wipro	Gallagher Financial Systems	Telecom Expense Management	Undisclosed (sources estimate at $6 million)
October 4, 2008	Xchanging PLC	Solutions	Mortgage Solutions	£83 million
November 4, 2008		NVS Installation AB	BPO and IT	€235 million
November 10, 2008	EBIX	Confirmnet Corporation	Insurance BPO	$10-11 million
November 22, 2008	Serco Group	Infovision	BPO	$75 million
November 24, 2008	HCL Technologies	Axon Group	SAP Consultancy Services	£441 million

During the past year when the financial crisis put pressure on the economy, the outsourcing industry witnessed an increase in mergers and acquisitions (M&A) and IPO activity, especially among midsize and small service providers. For example, Hewlett-Packard's deal to buy Electronic Data System (EDS) in May 2008 forced other players such as Infosys, Wipro, and Tata Consultancy Services (TCS) to look for acquisitions. In October 2008, TCS bought Citigroup Global Services Limited (CGSL), an India-headquartered offshore BPO branch of Citigroup. Table 1 summarizes examples of consolidation deals taking place during 2008. As global service outsourcing industrial structure and market distribution pattern is facing a major adjustment, service providers from emerging regions, predominantly China, Eastern Europe, Russia, and Latin America, are becoming more influential.

Clients pressure providers to cut cost and renegotiate existing contracts

Renewed emphasis on cost savings and enhancing efficiency

Cost savings long have been the main focus of early adopters of outsourcing and offshoring. However, as companies began to adopt corporatewide strategies for outsourcing and offshoring decisions at the BU and function level, managers' attention has shifted from focusing exclusively on labor arbitrage to viewing outsourcing as part of their firm's strategy to access qualified personnel, improve speed to market, manage risk, and optimize processes. In the 2009 survey, we observe that the economic crisis has reemphasized the importance of cost savings and improving efficiency via outsourcing, but access to qualified personnel is still the third most important strategic driver (see Chart 7). More than 70 percent of service providers indicate that labor and other cost savings, as well as enhancing efficiency through business process redesign, are important reasons for their client to outsource.

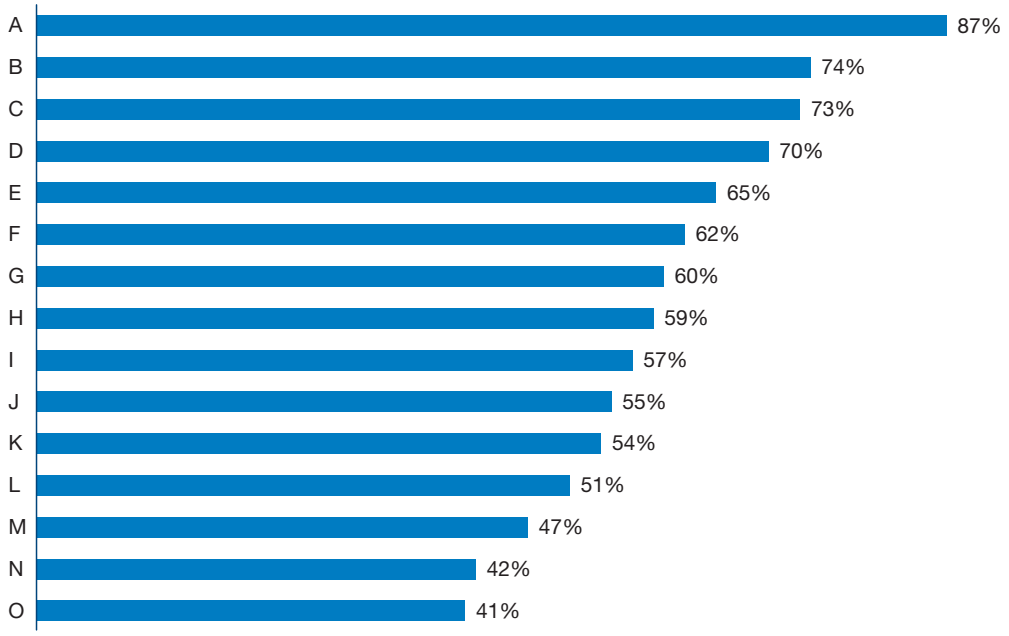
A strong interest in cost reduction also shows up in service provider selection decisions: 52 percent of service providers indicate low cost of service delivery as one of the five most important selection criteria. To ensure the realization of expected cost savings, a majority of companies include expected savings as part of the explicit contract terms. More than 60 percent of service providers identify cost savings as one of the five most important contract items, a 42 percent increase over the 2007 survey.

Increasing pressure on profit margins

In the current economic climate, service providers are focusing on accommodating their client demands while defending their market position from new competitors by offering price concessions, intensifying their focus on internal operational efficiencies, and adopting new operating models. Survey findings indicate that pressure on margins is the most important threat (see Chart 8) to service providers, especially for large and midsize providers, followed by the challenge of retaining talent and achieving quality expectation. More than 65 percent of large and midsize service providers rate pressure on margin among their most important risks compared with 46 percent for small service providers. This is partially explained by the fact that large providers have a much bigger share of large BPO, information technology outsourcing (ITO), and contact center contracts, while the more nimble, smaller providers are able to realize higher margins because of their focus on KPO and innovation services and lower overhead. As a result of the economic crisis, more service providers are entering the market, often with indirect support

CHART 7

Percent of providers rating drivers as "important" or "very important" reasons for their clients to outsource



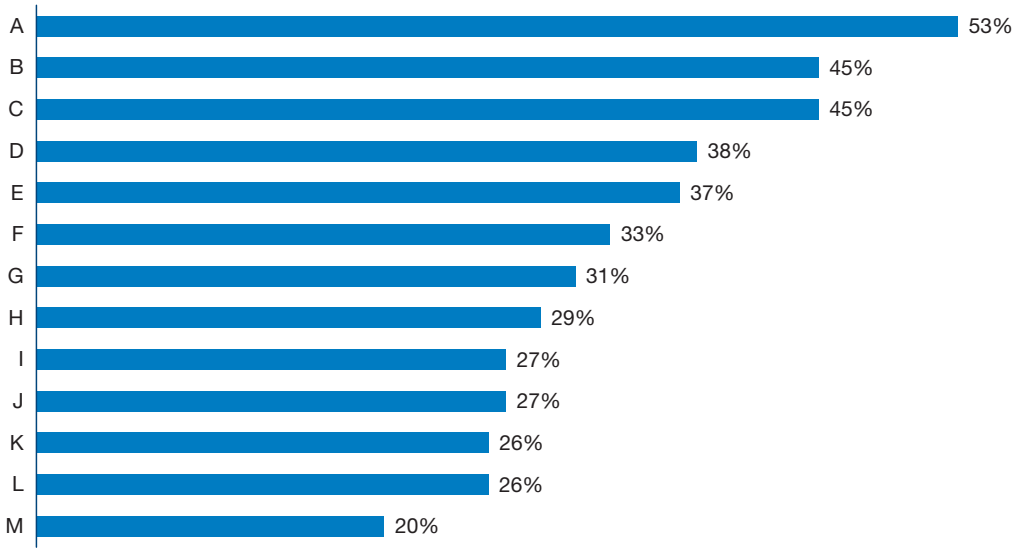
A. Labor cost savings
B. Other cost savings
C. Access to qualified personnel offshore
D. Enhancing efficiency through business process redesign
E. Competitive pressure
F. Growth strategy
G. Need to improve service levels
H. Increase organizational flexibility
I. Increasing speed to market
J. Exploit location-specific advantages
K. Part of a larger global strategy
L. Enhance capacity for innovation
M. Domestic shortage of qualified personnel
N. Accepted industry practice
O. Accessing new markets for products and services

Source:

Duke University Offshoring Research Network 2007/08 Service Provider Survey
Duke University Offshoring Research Network 2009 Service Provider Survey

from their governments. As this phenomenon fuels price competition, large service providers seek volume to achieve economies of scale. Rather than a pure organic growth approach, alternatives include acquiring their competition or their clients' captive operations. The market recently has seen significant examples of both strategies.

CHART 8
Percent of providers indicating factor as one of six most important risks



A. Pressure on margin
B. Retaining talents
C. Satisfying quality expectations
D. Currency fluctuation on dollar denominated contracts
E. Increased difficulty in finding qualified personnel
F. Achieving expected cost savings
G. Availability of personnel with management skills
H. Competitors poaching clients
I. Client inability to manage relationship
J. Wage inflation
K. High employee turnover
L. Threat of new competitor from another country *(16% of India-based providers see this as an important risk)*
M. Proprietary information held back by clients

Source:

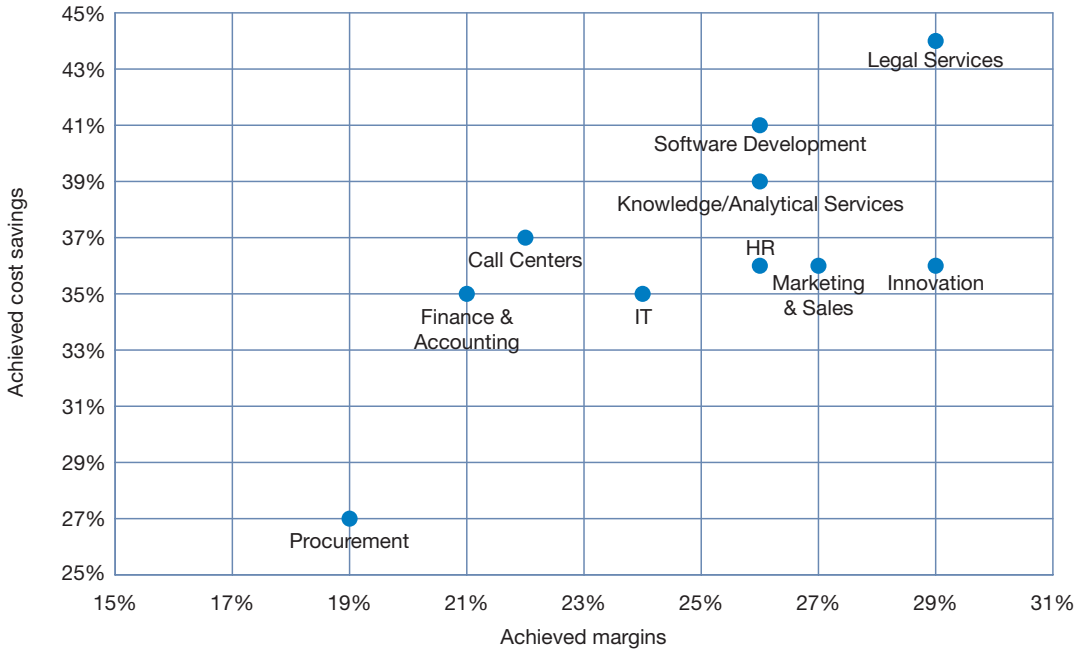
Duke University Offshoring Research Network 2007/08 Service Provider Survey
Duke University Offshoring Research Network 2009 Service Provider Survey

Service offering margins are shown in Chart 9. LPO has only recently emerged as a new opportunity for outsourcing offshore and, perhaps not surprisingly, realizes the highest profit margins for service providers as well as the highest cost savings for companies. The attractive economic benefit of LPO may explain the high number of service providers entering the market and of companies exploring opportunities to outsource their most routine legal activities over the past few years. In the United States, legal services outsourcing also has been stimulated by two important events. The Federal Rules of Civil Procedure concerning Electronic Discovery in 2006 has changed the relationship between law firms and their corporate clients. Later, in September 2008, the American Bar Association issued an ethical opinion endorsing the outsourcing of legal services: US attorneys are responsible for the supervision of offshoring services and for making sure that offshored

work meets the US standard. In India alone, the LPO industry is growing faster than 40 percent per annum[2] with more than 110 LPO service providers as of 2008.[3] Interestingly, the presence of a rapidly growing number of LPO providers has not yet unleashed price competition as economic theory would predict. Together, an emergence of outsourced legal services and the recent economic events have set profound changes in companies' perception of the legal industry, once regarded as a sensitive and privileged activity that needed to be kept in-house.

Outsourcing of innovation processes generates similarly high margins for service providers and very significant cost savings for companies. Due to a high degree of required customization and context-specific characteristic of innovation projects, service providers are able to realize higher margins. However, in a mature, commoditized service market, such as contact center or application development, intense price competition and declining profit margins are unavoidable. For instance, participating service providers report an average margin of 23 percent for contact center, 24 percent for IT services, and 21 percent for finance and accounting (while companies realize savings of 35 percent).

CHART 9
Comparison of profit margins achieved by service providers and estimate of cost savings achieved by function



Source:

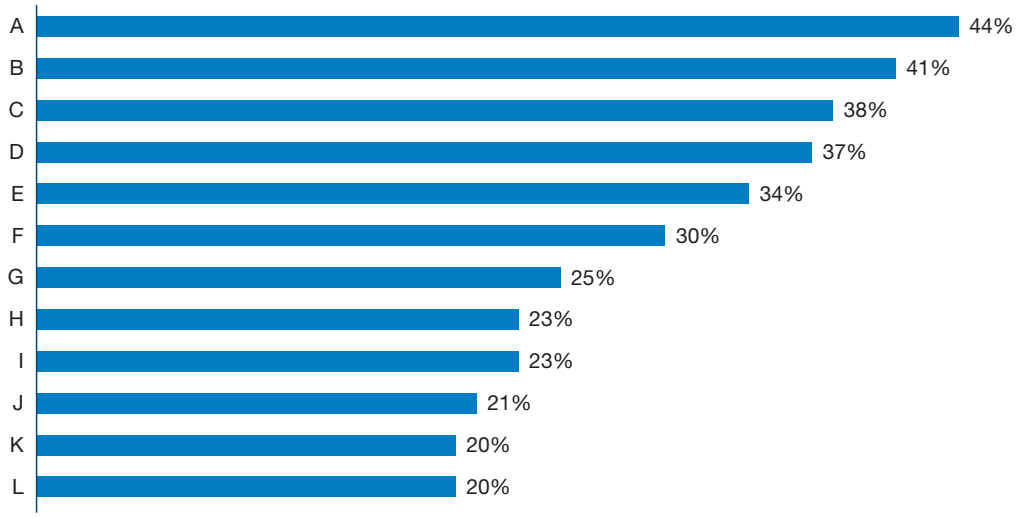
Duke University Offshoring Research Network 2007/08 Service Provider Survey
Duke University Offshoring Research Network 2009 Service Provider Survey

[2] Source: EFY News Network
[3] Source: Prism Legal "Outsourced Legal Services—Introduction and Explanation"

Building enduring outsourcing relationships

Apart from revenue growth driven by securing new clients, service providers are also focused on renewing their existing contracts. The results from the 2009 survey show that, on average, 70 percent of deals were renewed at the expiration of the first contract compared with 72 percent in the 2007 survey, reflecting many clients' reluctance to go through the pain of transitioning to a new provider. According to the 2009 survey respondents, the failure to meet clients' expectations is a key reason when contracts are terminated (see Chart 10): More than 40 percent of service providers indicate clients' unrealistic expectations and lack of clear outsourcing strategy as one of the most important reasons for contract termination. Increasing M&A activity during the past year also helps to explain why we observe a slight decline in contract renewal rates: Post-M&A reorganization and integration efforts often result in rationalizing the number of service providers leading to some contract terminations.

CHART 10
Percent of providers indicating reasons for contract terminations



A. Client's expectations are unrealistic
B. Client has no clear outsourcing strategy
C. Service no longer needed
D. Client underestimates scope of project
E. Service quality is not achieved
F. Client lacks skills/resources to implement and manage relationship
G. Management-level turnover on client side
H. Change in target operating model
I. Lack of buy-in by client's middle management
J. Poor planning in work transfer
K. Conflicts due to unanticipated work (change orders)
L. Cost savings are not achieved

Source:

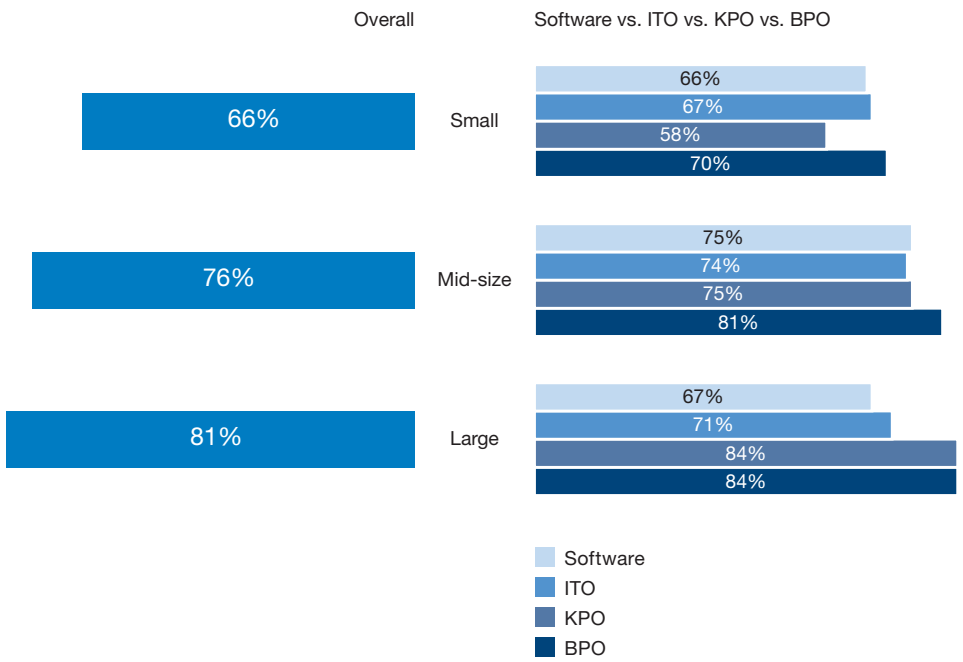
Duke University Offshoring Research Network 2007/08 Service Provider Survey
Duke University Offshoring Research Network 2009 Service Provider Survey

Generally, BPO and ITO[4] deals, which often involve a high degree of standardization and large investment, are at an advantage when it comes to contract longevity in comparison with KPO deals, which involve shorter duration, project-based work carried out by highly skilled staff (e.g., research and development, product design, and engineering services). Interestingly, the analysis of renewal rates by service provider size reveals that large service providers tend to have a higher renewal rate compared with smaller-size providers (see Chart 11): 81 percent of large service providers' contracts are renewed compared with 66 percent of small providers,' supporting the view that transition costs can be an important consideration in contract termination. The survey also reveals that smaller service providers have a 58 percent renewal rate for their KPO contracts while the KPO deals of large providers, which are likely to incur higher transition costs, have a significantly higher contract renewal rate of 84 percent.

The tension between satisfying demand for near-shore delivery centers and declining margins

Among the recent trends in outsourcing and offshoring, near-shoring has gained momentum among companies currently offshoring and those considering it. Media reports point to a substantial number of companies making changes or planning to bring their offshoring closer to their home country. The emergence of new service providers in near-shore

CHART 11
Percent of deals that are renewed at the expiration of the first contract by provider size



Source:

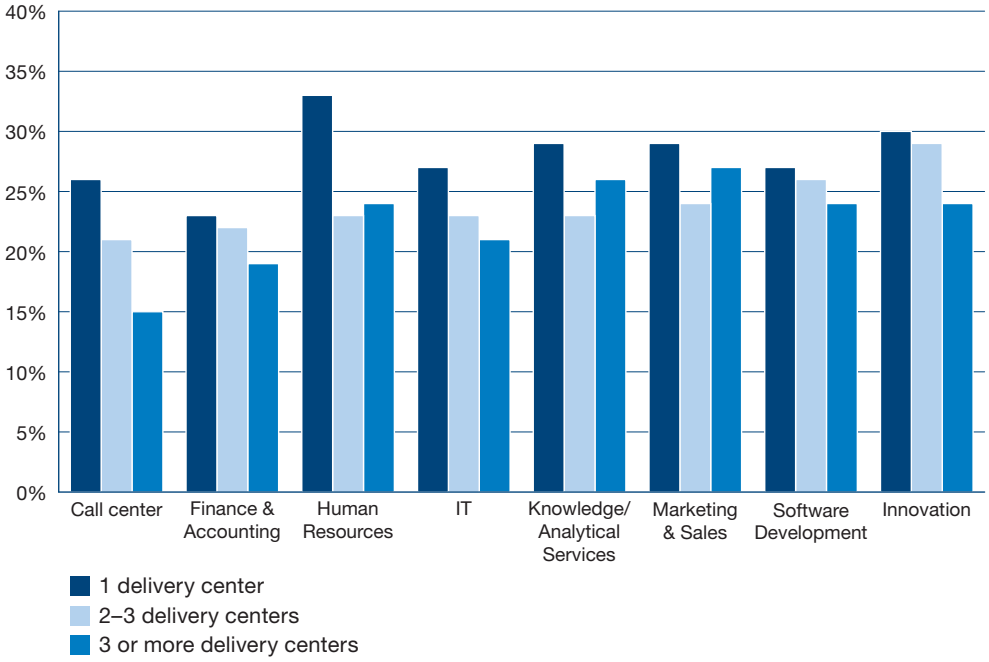
Duke University Offshoring Research Network 2007/08 Service Provider Survey
Duke University Offshoring Research Network 2009 Service Provider Survey

[4] Business Process Outsourcing (BPO) includes contact center, human resources, finance & accounting, marketing & sales and procurement. ITO includes information technology service.

locations and the toll of time zone differences and geographical distance in offshoring likely have influenced this trend. Incumbent service providers are under pressure to establish delivery centers in multiple locations in order to serve an increasing demand for near-shore location.

Unfortunately for service providers, the 2009 survey findings indicate that average profit margins generally decline as service providers expand their scale—defined as the number of a provider's delivery centers in different locations (see Chart 12). This suggests an inherent conflict between clients' demand for near-shore delivery centers and large, global providers' overall efficiency. Setting up an operation in multiple locations helps providers distribute their risk of relying on one major operating location and accommodates their clients' near-shore demand. However, it requires a large investment and a focus on capacity management and utilization, especially for asset-intensive services requiring technology infrastructure, such as contact center and IT services. Overhead and transaction costs arising from coordinating and managing multiple locations also add to operating costs and drive down profit margins. This suggests that large global providers will experience underexploited economies to scale. However, the exception is North American-based providers, which achieve high margins and deliver the highest cost savings. Through in-depth experience and a large international footprint, these providers have developed superior client account management models and superior organizational capabilities to exploit the benefits of custom software development projects (see Chart 13).

CHART 12
Margins achieved in particular functions by number of delivery centers



Source:

Duke University Offshoring Research Network 2007/08 Service Provider Survey
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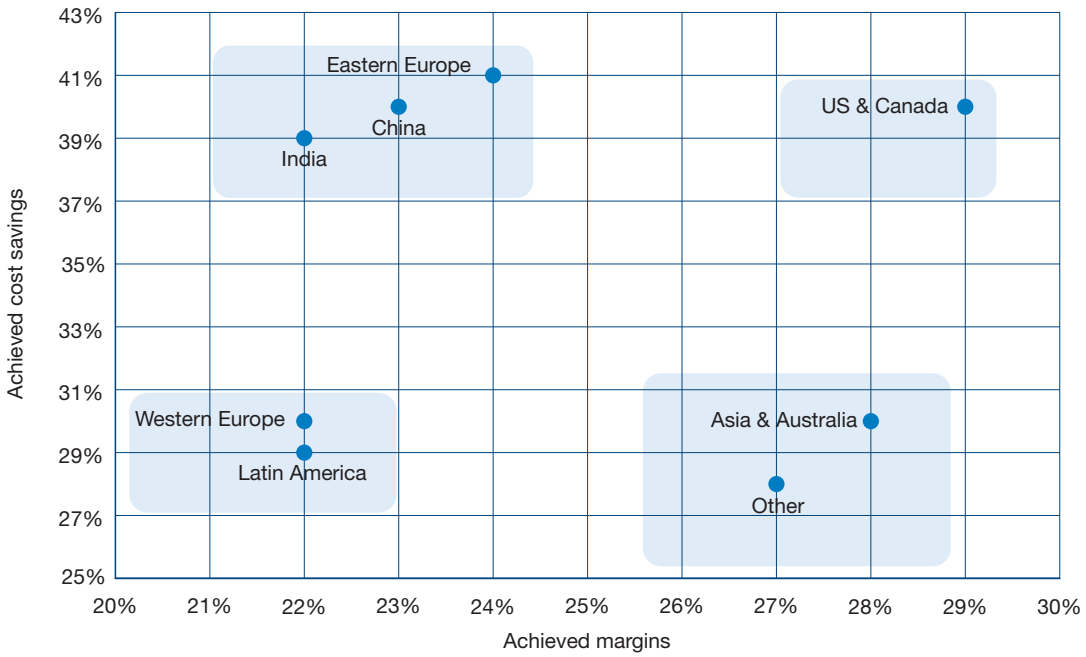
CHART 13
Profit margins achieved by service providers and estimate of cost savings achieved by service providers' HQ region



Source:

Duke University Offshoring Research Network 2007/08 Service Provider Survey
Duke University Offshoring Research Network 2009 Service Provider Survey

Many service providers are also looking into expanding the scope of their service offerings, hoping to realize gains from economies of scope, to broaden their client relationships, and to diversify. Surprisingly, our survey results show that the number of service offerings and profit margins have an inverted U-shaped relationship (see Chart 14). In fact, economies of scope, or the positive effect of synergy among different service offerings, tend to level off and, consequently, decline as providers continue to increase the scope of their services beyond an optimal point.

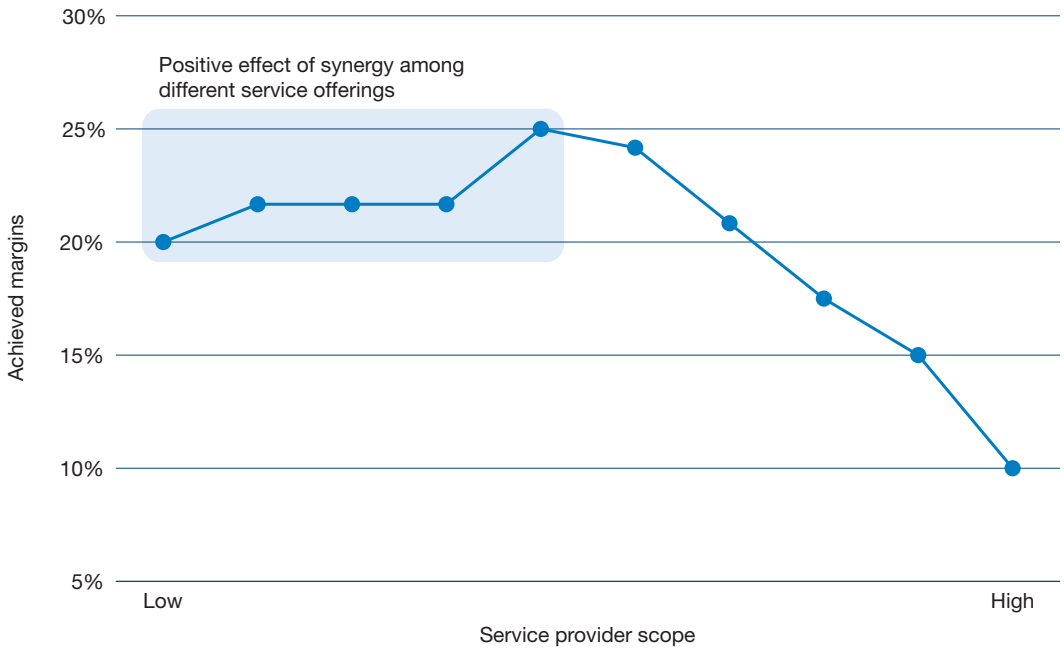
The diseconomies of scale and scope of service offerings found in our survey results lead us to conclude that most large service providers have neglected to invest in organizational capabilities, such as client account management or coordination capabilities that match their build-up of scale and scope. In fact, we believe that full service providers are at advantage for realizing synergy among their service offerings but, more importantly, they need to develop organizational capability to synchronously manage, rationalize the portfolio, and coordinate among diverse services.

Expansion of global services

Growing scale of existing providers and new entrants

The ORN survey captures the growth in the outsourcing industry both in terms of providers' plans for new service offerings, as well as plans for expansion of existing service offerings. According to the survey participants, the outsourcing industry is continuing its rapid growth in spite of the difficult economic environment. A large number of providers indicate their aggressive plans to initiate new software development and IT services (see Chart 15) in the next 18–36 months. In addition, the number of service providers planning to offer new finance and accounting, human resources, and innovation services has more than doubled relative to the 2007/08 survey responses. Plans for new software development and innovation services are dominated by small niche service providers, given the high potential margins. Thirty-three percent of small providers indicate their initiative to offer new innovation service, and 51 percent have a plan to offer new software development service, suggesting a desire of new entrants to move up the value chain.

CHART 14:
Positive effect of synergy among different service offerings



Source:

Duke University Offshoring Research Network 2007/08 Service Provider Survey
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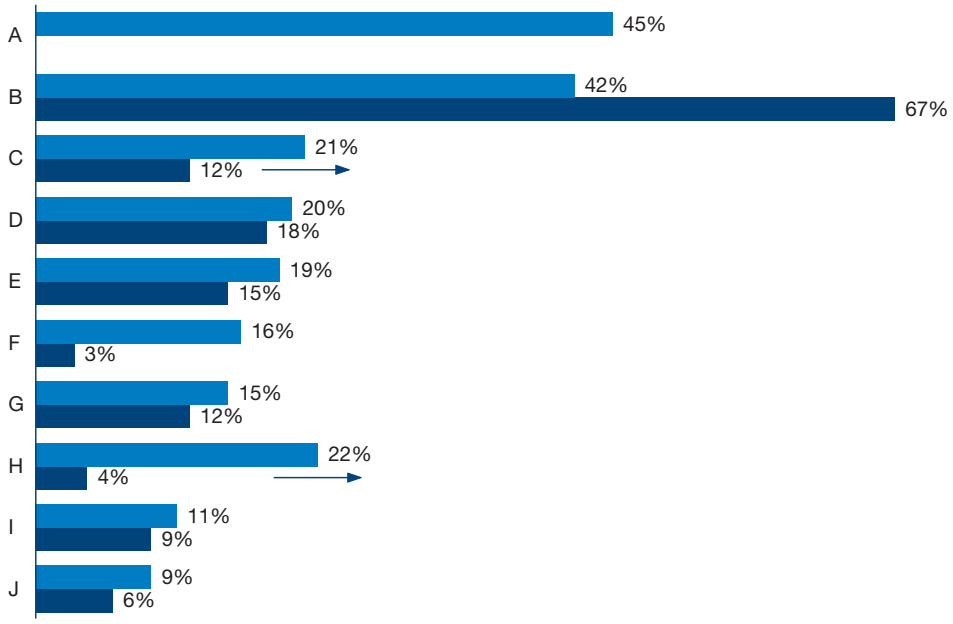
CHART 15
Percent of providers planning to offer NEW service in the next 18-36 months



A. Software Development†
B. IT
C. Finance & Accounting
D. Call Centers
E. Knowledge/Analytical Services
F. Human Resources
G. Marketing & Sales
H. Innovation
I. Legal Services
J. Procurement

2009
2007/08

† Software Development was included in Information Technology for 2007/08 survey

Source:

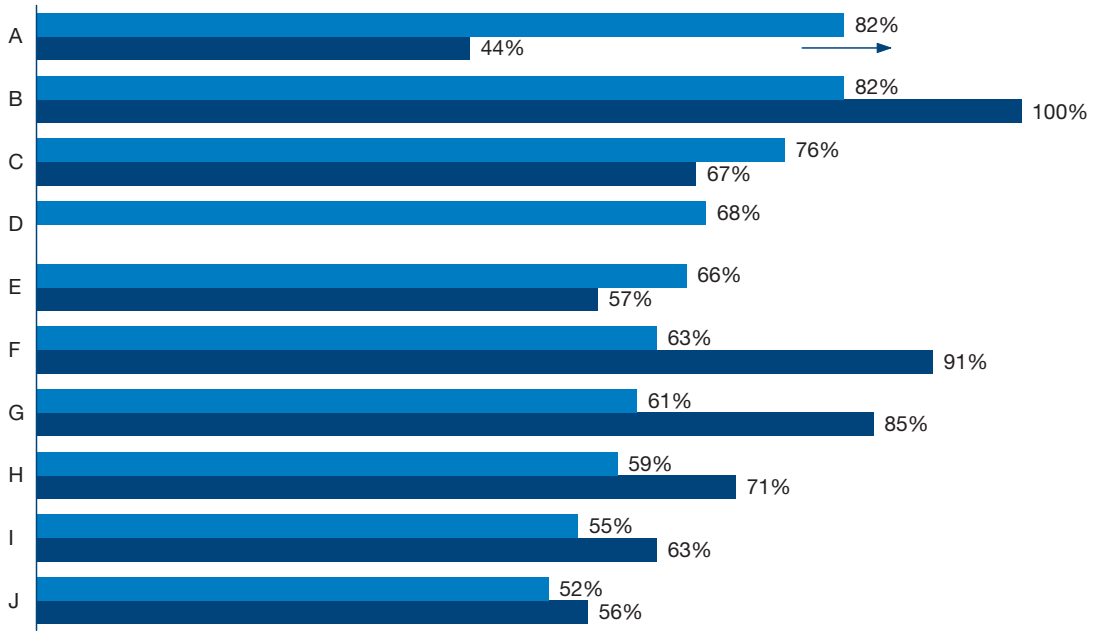
Duke University Offshoring Research Network 2009 Service Provider Survey

Our survey findings also reveal that, in addition to new service offerings, 62 percent of service providers are planning to expand the scale of their existing services. The percentage of providers planning to do so in the next 18–36 months is illustrated in Chart 16. Although only 9 percent of providers indicate their plan to offer new procurement services (see Chart 15), more than 80 percent of providers are planning to expand their existing procurement service (see Chart 16). This suggests that the expected growth in procurement outsourcing is pushed by existing providers rather than new players entering the market. However, when compared with companies' plans, there is a significant discrepancy between the two. Our data indicate that a misalignment exists between client demand for procurement outsourcing and the service providers' internal forecasts: Most likely actual procurement and end-to-end process optimization projects will be much smaller

than providers expect. Similarly, more than 80 percent of LPO service providers are planning to expand the scale of their legal service offering compared with 11 percent of new providers entering LPO market. The data from the ORN buy-side surveys also suggest that LPO is another offering where supply is ahead of demand. Software development and knowledge/analytical services are expected to continue their growth in 2010, as more than 65 percent of service providers are planning to expand their scale of these services. However, the expansion in scale of contact center and IT services tends to slow down, compared with the 2007/08 survey.

CHART 16

Percent of providers planning to expand the scale of EXISTING services in the next 18-36 months



A. Procurement
B. Legal Services
C. Finance & Accounting
D. Software Development†
E. Knowledge/Analytical Services
F. IT
G. Call Centers
H. Marketing & Sales
I. Human Resources
J. Innovation

2009
2007/08

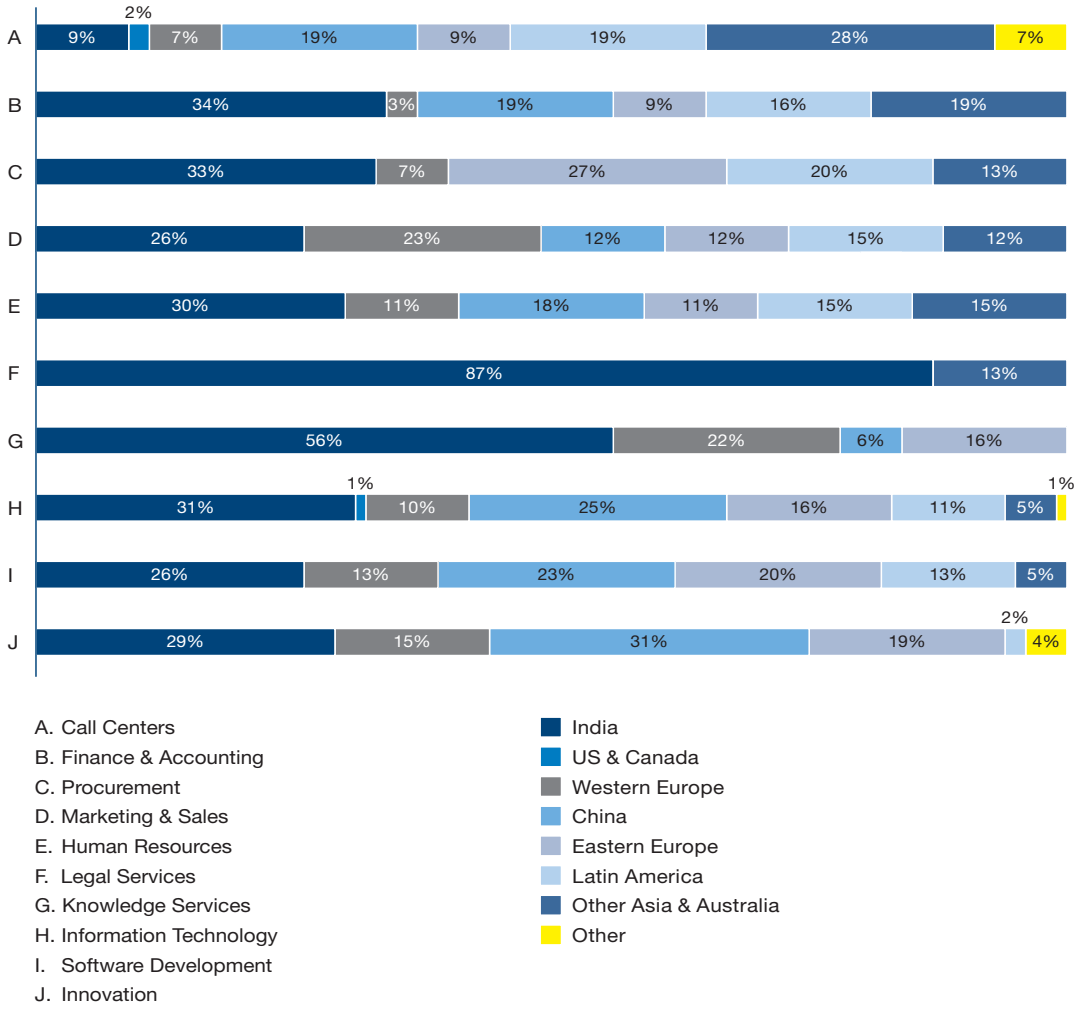
† Software Development was included in Information Technology for 2007/08 survey

Source:

Duke University Offshoring Research Network 2009 Service Provider Survey

The growth in finance and accounting services is accelerating at a rapid rate (compared with plans in 2007) with 76 percent of service providers planning to expand the scale of their existing finance and accounting offering. The most common targets of finance and accounting outsourcing today are transactional processes such as accounts payable, collections, fixed assets, and reconciliations, but we observe the dynamics of finance and accounting outsourcing are increasingly extending into key processes such as project accounting, tax, and business analysis. It is essential in finance and accounting outsourcing that service providers have a stronger technology backbone to be able to optimize and integrate a firm's discrete applications across platforms and versions, and we are seeing an increase in the bundling of finance and accounting outsourcing with ERP consolidations

CHART 17
Percent of providers naming regions as growing destinations in particular services



Source:

Duke University Offshoring Research Network 2009 Service Provider Survey

and support contracts. This required capability favors large service providers that are capable of interfacing their BPO and ITO offerings. Increasingly, we expect to see companies outsourcing their finance and accounting activities to service providers that have the expertise in integrating clients' ERP capabilities across different geographies within the client company and are able to provide tangible business benefits from consolidating multiple custom software development projects.

Rising outsourcing destinations

Although India remains the market leader, other emerging countries have their sight set on the outsourcing crown. Unfortunately, most Indian providers seem to be unaware of the mounting competition. The 2009 ORN survey results show the emergence of multiple outsourcing industry centers with regional centers of gravity in the emerging markets of China, Latin America, and Eastern Europe. When asking service providers participating in the survey to name growing destinations for each service (see Chart 17), we observe high growth of contact center outsourcing, (expansion into nonvoice, complex, and higher-value activities), into Latin America, China, and other Asian countries (e.g., Philippines). Through follow-up, in-depth interviews with leading contact center providers, we speculate the emerging growth in nonvoice services, which remove the language disadvantage of providers in non-English speaking countries and offer a more competitive environment. The survey results also suggest that service providers anticipate China and Eastern Europe continuing to grow as an attractive destination for technology- and knowledge-related outsourcing, including software development, IT, and innovation services.

India is no longer the only outsourcing hot spot. An emergence of capabilities and talent pools in new geographic regions, as well as national governments pushing hard to grab more offshoring business, is driving the industry to become even more global. The dramatic increase in the number of emerging outsourcing destinations is forcing the incumbents to expand their operations across regions, which in turn requires providers to manage more complex operations in parts of the world where they may not have experience. The increased level of globalization in the outsourcing industry is evident in Table 2, which illustrates the list of most popular delivery center cities identified by the ORN survey participants. American multinational providers such as Accenture, HP, and IBM are growing their delivery centers in these emerging regions to defend their market position. Indian providers such as Infosys, Wipro, and TCS are looking to acquire other players or captive units, and they are opening new delivery centers in emerging regions (e.g., China, Eastern Europe, and Latin America) to accommodate customers wherever they may be. In their attempt to expand globally, a number of service providers are struggling to develop the capability to manage their fast-growing business with multiple operations across countries.

TABLE 2
Global Outsourcing Cities by Service Offerings

Location	Contact Center	Financing & Accounting	Human Resources	Procurement	Marketing & Sales	Legal Services
India	Bangalore Chennai Mumbai Pune Noida	Bangalore Pune Chennai Mumbai Gurgaon	Pune Bangalore Hyderabad Mumbai	Pune Bangalore Chennai Delhi Noida	Bangalore Pune Chennai Gurgaon Nashik	Chennai Gurgaon Pune Bangalore Noida
China	Shanghai Beijing Dalian	Shanghai Beijing Dalian	Shanghai Beijing Guangzhou	Shenzhen Beijing Dalian Shanghai Hong Kong	Dalian Shanghai Shenzhen	
Other Asia Pacific	Manila Cebu Makati	Manila Makati Sydney	Manila Taipei Singapore		Manila Kuala Lumpur Taipei	Manila Colombo Laguna
Eastern Europe (Including Russia)	Sofia Budapest	Warsaw	Minsk Sofia		Minsk	Prague
Western Europe	Madrid Barcelona La Coruna	London Madrid	Munich Zurich	Munich	Frankfurt Munich	London
Latin America	Bogota Lima Buenos Aires Cordoba Sao Paulo	Bogota Santiago Barranquilla Cali Mexico City	Bogota Buenos Aires	Buenos Aires Sao Paulo Bogota	Bogota Sofia	Bogota Medellin

We conclude that it is the capability to manage globally distributed operations that is critical for service providers to succeed in this increasingly competitive outsourcing market. Just like other businesses struggling to survive in today's turbulent economic environment, outsourcing service providers' success relies largely on their capabilities to continually develop, deploy, and optimize their resources in pursuit of long-term economic return and global competitive advantage. The essence lies in the ability to acquire distinctive resources (e.g., possess and retain skilled personnel); the ability to allocate, deploy, and manage such resources (e.g., assemble, integrate, and exploit distinctive resources and skill, capacity management); and the ability to enhance and develop new capabilities (e.g., dynamic learning and building up new capabilities).

Key Insights

- Many outsourcing providers that see the market ramping are making investments in new services and hiring.

- Many service providers that are expanding their scope and scale are struggling with profitability and how to manage client demands for broader services from a smaller number of providers. This should be a consideration for clients that are deciding to go with a best-of-breed provider versus a large-scale, tier 1 provider.

- Many service providers outside of North America scramble to achieve the margins reached by their competitors based in North America and are trying to transform their operating models.

- Indian providers are notably unconcerned by the emerging global entrants. (Only 16 percent of participants surveyed see them as a threat). This is particularly surprising, given it is driving down prices and margins. How will they respond since achieving economies of scope and scale has been an issue?

- New service provider entrants are penetrating at the low end, in commoditized services (e.g., application development), as well as the high end (e.g., legal, research and development, and industry-specific process). This is squeezing the margins of the incumbents and driving down their potential for higher margins gained by those higher-value services. How will they respond (e.g., mergers and acquisitions, etc.)?

- Supply and demand clashes for some of the services offered. For example, service providers have been pushing and building capabilities around procurement outsourcing for several years, but the client demand does not seem to be there. Is it an issue of value proposition or how the services have been marketed?

- Legal services' outsourcing growth has been and is likely to be strong, particularly in India. How are clients thinking this through from a value and risk perspective?

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