

# Offshore Insights

## Market Report Series

[www.neoIT.com](http://www.neoIT.com)

### RESEARCH SUMMARY:

## Services Globalization<sup>SM</sup> Trends 2007

### The Business Transformation Lever Companies Can No Longer Ignore

**B**usiness transformation is breaking the limits of geography, and is going across the seas and shores. Year 2007, neoIT predicts, will see companies significantly scale up global services operations to accelerate transformation. The focus will be on leveraging it to enter new segments, gain speed to market, enable process standardization and significantly lower costs.

An overall growth of 25-30% will translate into emergence of new offshore and nearshore locations with hard-to-ignore players, M&As, scaling up of capabilities and subject-specific expertise...all reflect the fairly confident transition of closer-to-the-core functions to global players or locations.

neoIT tracks players, agreements, and directions of the services globalization industry and in this research brief brings you the trends that will have an impact in 2007.

---

Year 2007, neoIT predicts, will see companies significantly scale up global services operations to accelerate transformation.

---

## Buyer Trends

Buyers are becoming more sophisticated as their experience with services globalization expands. Some key buyer trends that we will see in 2007 are:

### 1. **Demanding "Client of Choice" status:**

As services globalization gains momentum, service providers have to manage relationships with a larger number of clients. Seasoned buyers of services are now demanding a "client of choice" status from service providers, to ensure greater attention, increased responsiveness and high service levels. With a large number of agreements up for renegotiation, neoIT predicts this trend to have a major impact, especially for enterprises keen to explore optimizing the number of service providers. Mature buyers will move from multi-sourcing to fewer service providers.

2. **Closing in on "Core":** Continuing with the trend seen in 2006, enterprises shall globalize more of their functions which are closer to the "core". Enterprises have seen a reduction in costs as well as reduction in risk of innovation by taking the services globalization route. Now they are looking at deriving similar advantages by globalizing higher-impact services. The growth in globalization of engineering design, legal services, animation, financial planning & business analysis, and tax planning are evidence of this trend. neoIT expects this to continue at an accelerated pace through 2007.

3. **Evaluate requirements first:** It comes as no surprise that buyers will become more savvy and sophisticated in their need for global services. Many of the early adopters of global services that moved to low-cost jurisdictions will now understand the 'total

cost' of their move and start tweaking their strategies. Buyers will start to focus on establishing their requirements first, and not stating preferences regarding countries.

For example, buyers do not want to 'go offshore' per se, instead, they want to go to the country that meets their requirements (which may relate to cost, intellectual property rights, etc.)

### 4. **Services Globalization "M&As" as the way to increase business impact:**

Globalizing some of the functions through outsourcing or captive operations is just one part of the story for many enterprises. The other part is about buying out companies to gain offshore facilities, rather than having to build competency and facilities from scratch. This enables them to jump-start high-end work, while the commoditized work goes to the local service providers.

### 5. **Portfolio management of services globalization:**

As buyers have an increased portfolio of services operations in global locations, the need to better manage risk becomes paramount. The concept of portfolio management as applied to one's investments will take hold. Buyers will look to other geographies as a means to better manage operational and financial risks for their services globalization efforts.

### 6. **Pent-up demand through renewals:**

A significant value of outsourced agreements are coming up for renewal in 2007 (some estimate that the number may be closer to \$100 Billion). As buyers look to renew these agreements, they will explore transition of many of these activities to offshore locations. This will drive increased business to offshore based service providers and put pressure on global players to be more pro-active in managing this change.

7. **Change Management Process:** With unprecedented growth in globalization, the focus now needs to be on implementing effective change management at the buyer's end. As significant risk is attached to the change management process, we see internal communication strategies as the key tool for the initial transfer phase of outsourcing. Buyers will need to create this capability in their Program Governance Office or access it from external consultants.
8. **Connecting Services Globalization to Competitive Advantage:** 2007 will be the year when organizations on a broad scale will realize that it's not just about cutting costs, but rather services globalization is truly about achieving competitive advantage. As a result companies will be more strategic about how they leverage global talent and also how they organize internally to manage their distributed workforce.
2. **Global players continuing to scale up:** Large players with extensive global presence, such as IBM, Accenture, HP, EDS and Unisys are scaling up dramatically in locations such as China and India. All have plans to add thousands of people to their offshore resources. This is also driven by the fact that there is growing onshore presence of Service providers who are now able to deliver seamless hybrid onshore-offshore services at a lower cost. Companies looking at offshore service providers can now also consider these US- and UK-based providers along with the local providers of a particular country.
3. **Increased M&A activity:** With scale being key to landing bigger, better agreements, relatively smaller Service providers are now actively looking for opportunities to be acquired or to form partnerships. MphasiS' agreement with EDS last March is a good example of a trend we see picking up in 2007. This agreement extends EDS' reach in India while giving MphasiS access to major clients. Such agreements will work both ways: eastern companies will acquire western outfits to gain a global footprint and venture into services that demand a significant onshore presence. Companies based in the West will take a keen interest in setups in the East to stay competitive as well as explore eastern markets, which are now, not only cost effective delivery locations but also rapidly emerging markets by themselves.
4. **Increase in leading service providers' rates/Decrease in margins:** In 2007, leading Tier 1 offshore based ITO and BPO service providers are likely to increase their rates. With the growing demand for skilled resources, rise in wages, and increased overheads incurred in

### Service Provider Trends

Service providers are re-inventing their business strategies in the face of growing competition. This competition is not just from traditional rivals, but from other areas such as business consulting and captive operations. Here's how we see the service provider landscape shaping up in 2007:

1. **Acquisitions of domain specialists:** In 2007, we shall see an increased focus among service providers on developing industry-specific subject matter expertise. The year will see enhanced M & A activity by service providers seeking to add deep expertise in specific vertical industry and horizontal domain areas to their portfolio of services. The result will be a broad based move up in the value chain for many service providers.

maintaining quality or ensuring tight security, rates are expected to go up by 2-3%. This will still be very competitive against global players.

5. **Global expansion of locations:** In 2007, expect to see service providers open up additional development and business processing centers in Asia and Europe. Reasons for will be language requirements other than English or to cater to nearshore markets. Expect to see increased operations particularly in China and Eastern Europe. This will also be enabled through strategic acquisitions or partnerships. But moving to new geographic areas takes time & is with some inherent risks so we can expect to see increased mergers & acquisitions activity that is driven by this need for global service delivery capabilities.
6. **Consulting arms:** To help clients increase their scope of outsourcing and scale up faster, more and more services firms will build or acquire consulting arms in 2007.
7. **The power of analytics:** This year will see a continuing trend of adding a layer of analytics to day-to-day BPO functions, creating significant value for clients. BPO service providers are making significant investments – both through acquisitions and through organic growth - in the area of analytics. The early results indicate that clients are thrilled with the increased visibility and inputs for key decisions as well as the cost reduction associated with becoming more productive. As service providers become more adept and clients learn to ask for the service we see a united move up the value chain for both parties.

## Location Trends

1. **Indian Tier 1 cities reign supreme:** Despite concerns of wage inflation, attrition and infrastructure issues, we expect the Indian Tier 1 cities (NCR, Bangalore, Chennai, Hyderabad and Mumbai) to grow at a continued pace in attracting offshore delivery work, through 2007. Though costs and attrition have risen, these cities still offer very attractive labor costs for both scale-intensive and skill-intensive services. Senior executives at client organizations are very comfortable with these cities as they have built a global brand for service delivery. Availability of good support systems, excellent managerial talent and a good expatriate standard of living all play a role in the continued attractiveness of these cities.
2. **Rapidly emerging European market:** The European market for global services will grow at a fast rate this year, as some European enterprises have "proved the concept" and set an example for their peers. With increasing maturity in nearshore delivery capabilities, European-language speaking countries like Hungary, Czech Republic, Russia, Poland, Bulgaria and Romania shall support this trend. With almost all major East European delivery locations under the EU, it has become easier from a regulatory standpoint to get service delivery from these countries. European enterprises shall also offshore services to India, Philippines and China and other lower-cost locations, depending on the language and culture-dependence of the particular service.

3. **Russia and Philippines will continue their growth as an outsourcing location:** Year 2007 will see Russia emerge as a strong contender in the IT outsourcing market. It is currently the 3rd largest IT outsourcing supply market, behind India and China. Russian IT companies specialize in high-end software and embedded software product development, which acts as a differentiator from lower-priced offerings from Indian companies. We expect the Russian ITO industry to grow at 40-45% in 2007.

The Philippines is providing excellent English language skills and that plays a key role in business process outsourcing. It competes very strongly with India in voice based processes. It's financial and accounting skills

are also at par. Also, Indian IT and BP companies have started setting up operations in the Philippines because of 2 major reasons: clients want to de-risk and want second English location, and attrition/shortages of staff in India are starting to impact projects. The ease in English and cultural affinity with the U.S. are making it easier for tier-2 clients to attempt setting up captive centers in the Philippines. What may be the critical catalyst at this crucial juncture is aggressive regulatory incentives in the Philippines for captive-center operations. Philippines will continue to benefit in 2007 from the focus on portfolio management as buyers expand their services globalization efforts.

In summary, Year 2007, neoIT predicts, will see companies significantly scale up global services operations to accelerate transformation. The focus will be on leveraging it to enter new segments, gain speed to market, enable process standardization and significantly lower costs. We notice that increasingly, service provider trends are driven by buyer trends...supply catering to demand. As buyers become more sophisticated, service providers need to meet those needs. Overall, neoIT expects to see the service provider landscape having broader capabilities and becoming more global in terms of service delivery locations.

Let the good times roll!!!

More information about the offshore outsourcing industry can be found within neoIT's research center at [www.neoOffshore.com](http://www.neoOffshore.com). For more details about neoIT's offshore advisory and management services, please contact:

**Juliana Gidwani**

Marketing Manager  
San Ramon, California  
[juliana@neoIT.com](mailto:juliana@neoIT.com)  
925-355-0557  
[www.neoIT.com](http://www.neoIT.com)

*No part of this report may be reprinted/reproduced without prior permission from neoIT.*



## neoIT Global Offices

### neoIT Global Headquarters

2603 Camino Ramon  
Ste. 200  
San Ramon, CA 94583  
Telephone: 925.355.0557  
Facsimile: 925.355.0558

### Asia Headquarters

Phoenix Towers, 5<sup>th</sup> Floor  
No 16 & 16/1, Museum Road  
Bangalore 560 025, India  
Telephone: +91 80 4018 2000  
Facsimile: +91 80 4018 2010

### neoIT Philippines

8/F Pacific Star Building  
Senator Gil Puyat Ave. cor Makati Ave.  
Makati City, Metro Manila, 1200, Philippines  
Telephone: +63 (2) 811-5519  
Facsimile: +63 (2) 811-5545

## Editors

**Atul Vashistha**  
CEO

**Eugene M. Kublanov**  
Managing Director & COO