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1.0 Executive Summary

After the technology bust of early 2000, corporations worldwide faced the challenge of arresting the decline in margins. To protect margins, enhance cash flows and to fund future growth, large multinational corporations turned to Shared Services and Outsourcing (SSO), with many companies aggressively emulating success stories such as General Electric’s captive shared services operations in India. Falling infrastructure costs, proven business models, hunt for economies of skill, and fast evolving maturity of service providers from low cost locations; only helped to accelerate the growth in SSO, especially for offshoring. With the global economy recovering, these SSO operations have played a significant role in boosting the profits for companies across several verticals to record levels.

Frost & Sullivan has estimated the SSO market for 2006 at approximately US$ 930 billion and projected to grow to US$ 1,430 billion by 2009, growing at a CAGR of 15%. Offshoring, which constituted a miniscule part of the total pie, is expected to grow at double the rate for overall SSO. The key drivers for SSO have continued to be cost benefits through standardization, leveraging of scale benefits, and cost arbitrage in countries like India and China. Other benefits include ability to free up of precious management time to allow them to focus on core competencies; ability to drive business innovation even in non-core areas; and reap benefits from standardization and resulting efficiencies. These factors have forced large corporations to explore further expansion of their current SSO operations or setting up new centers. On the other hand, concerns with SSO such as threat of loss of control and compromising confidentiality; potential reduction in service quality levels; risk of breach of intellectual property and shortage of skilled people through high attrition resulting in escalating costs, etc.; have forced some companies to reconsider against ramping up their SSO operations. Restrictive government regulations and political backlash in “send” countries have also forced some companies to adopt a more cautionary approach towards SSO.
While the Finance and Insurance vertical together with Technology continues to remain the largest verticals for SSO, constituting over 50% of the total spend on SSO, other verticals have developed effective operating models for SSO for functions such as IT services, finance and accounting, HR services, customer support and call center. Sectors like healthcare have gone to the extent of outsourcing core R&D functions while telecom companies in countries like India have outsourced network management, a function considered core for telecom operators. While the captive model and the third party model have become dominant, increasing instances of hybrid models involving equity participation, joint ventures and project funding, are being witnessed.

Most governments in top SSO locations offer various incentives to attract capital; however, structural factors like low labor costs and abundant supply of relevant skill have ensured that India remains as the prominent top of the mind location for SSO. But with high attrition rates and rising wage levels, India is facing threat from China which is emerging fast as an attractive location for IT, R&D and procurement services. Eastern European countries have been able to capitalize on their proximity to Western European countries, while Malaysia and Singapore have continued to grow. Frost & Sullivan’s study reveals that across the seven verticals, India remains the top location for SSO, followed by China, Ireland, Singapore, Malaysia, Mexico, Czech Republic, Poland, Philippines and Canada. New locations are emerging for specialized functions (Russia for high end software development) or for particular verticals (Dubai for BFSI).

This report leverages upon primary inputs from Fortune 500 and Forbes 2000 companies to benchmark the top locations for SSO for seven different industry verticals globally. This provide a strategic and empirical perspectives on the current and future state of the SSO landscape including key drivers and constraints, spending trends, location selection criteria and top of the mind locations for seven verticals.
2.0 Introduction

2.1 Objectives

The objectives of the study is to profile leading global companies from the Fortune 500 and Forbes 2000 list and to understand their Shared Services or Outsourcing (SSO) patterns currently and in the future. This includes but not limited to:

- Key Determinants
- Key Trends
- Key Location Selection and Criteria

A vertical specific analysis was performed to establish insights in SSO patterns and location selection. An in-depth analysis of the top SSO locations was conducted to understand their positioning, strengths and weaknesses.

2.2 Scope

To define the scope of this study, Frost & Sullivan have defined SSO as shown in Figure 2.1

Figure 2.1 Definition of Shared Services and Outsourcing (SSO)
The selection criteria for the companies include the following parameters:

- Companies from the Fortune Global 500 and Forbes 2000
- Vertical coverage

Figure 2.2 illustrates the seven verticals covered as part of this study.

**Figure 2.2 Verticals covered for the study**

<table>
<thead>
<tr>
<th>Selected Verticals</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Energy</strong></td>
</tr>
<tr>
<td><strong>Entertainment &amp; Media</strong></td>
</tr>
<tr>
<td><strong>Banking &amp; Financial Services Industry (BFSI)</strong></td>
</tr>
<tr>
<td><strong>Fast Moving Consumer Goods (FMCG) &amp; Retail</strong></td>
</tr>
<tr>
<td><strong>Transportation &amp; Logistics</strong></td>
</tr>
<tr>
<td><strong>Technology</strong></td>
</tr>
<tr>
<td><strong>Healthcare</strong></td>
</tr>
</tbody>
</table>

Figure 2.3 illustrates the functions typically covered as part of SSO operations.

**Figure 2.3 Functions for SSO**

<table>
<thead>
<tr>
<th>Functions for SSO</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Back-Office Processing</strong></td>
</tr>
<tr>
<td>• Data Processing</td>
</tr>
<tr>
<td>• Data Imaging &amp; Digitization</td>
</tr>
<tr>
<td>• Data Maintenance &amp; Support</td>
</tr>
<tr>
<td>• Data Archiving</td>
</tr>
<tr>
<td><strong>Customer Service &amp; Call Centers</strong></td>
</tr>
<tr>
<td>• Customer Support</td>
</tr>
<tr>
<td>• Customer Retention</td>
</tr>
<tr>
<td>• Inquiry &amp; Complaints</td>
</tr>
<tr>
<td><strong>Human Resources</strong></td>
</tr>
<tr>
<td>• Health &amp; Welfare Admin</td>
</tr>
<tr>
<td>• Talent Management</td>
</tr>
<tr>
<td>• Performance Management</td>
</tr>
<tr>
<td>• Compensation Administration</td>
</tr>
<tr>
<td><strong>Sales &amp; Sales Generation</strong></td>
</tr>
<tr>
<td>• Lead generation</td>
</tr>
<tr>
<td>• Lead Qualifying</td>
</tr>
<tr>
<td>• Telemarketing</td>
</tr>
<tr>
<td>• Booking &amp; Reservation</td>
</tr>
<tr>
<td><strong>IT Services &amp; Support</strong></td>
</tr>
<tr>
<td>• Application Support</td>
</tr>
<tr>
<td>• System Design &amp; Upgrades</td>
</tr>
<tr>
<td>• Hardware Maintenance</td>
</tr>
<tr>
<td><strong>Procurement</strong></td>
</tr>
<tr>
<td>• Sourcing Management</td>
</tr>
<tr>
<td>• Continuous Savings</td>
</tr>
<tr>
<td>• Transaction Management</td>
</tr>
<tr>
<td><strong>Finance &amp; Accounting</strong></td>
</tr>
<tr>
<td>• Transaction Management</td>
</tr>
<tr>
<td>• General Accounting</td>
</tr>
<tr>
<td>• Treasury &amp; Risk Mgmt.</td>
</tr>
<tr>
<td>• Tax Management</td>
</tr>
<tr>
<td><strong>Corporate Learning Programs</strong></td>
</tr>
<tr>
<td>• Curriculum development</td>
</tr>
<tr>
<td>• Learning program</td>
</tr>
<tr>
<td><strong>Strategic / Capability Development</strong></td>
</tr>
<tr>
<td>• New/ Emerging Technologies</td>
</tr>
<tr>
<td>• Design/ Testing of new products</td>
</tr>
<tr>
<td>• Prototyping/Development</td>
</tr>
</tbody>
</table>
2.3 Methodology

The overall methodology for this study has been illustrated in Figure 2.4.

**Figure 2.4 Overall Methodology**

<table>
<thead>
<tr>
<th>Primary</th>
<th>Analysis &amp; Scoring</th>
<th>Output &amp; Recommendations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interviews across 7 industry verticals</td>
<td>Cross-validation of primary and secondary results</td>
<td>Overall</td>
</tr>
<tr>
<td>Based on companies identified through secondary research</td>
<td>Forecast of vertical wise SSO spend</td>
<td>Impact of SSO on companies: Revenues, Profits and Market Capitalization</td>
</tr>
<tr>
<td>Questionnaire based on Frost research &amp; analysis</td>
<td>Analysis of primary research (how were drivers, constraints, locations, trends ranked)</td>
<td>Top 10 SSO hubs across 7 verticals</td>
</tr>
<tr>
<td>Secondary</td>
<td>Development of weights for scoring/ranking of locations</td>
<td>SWOT analysis of key SSO hubs</td>
</tr>
<tr>
<td>Identification of companies for 7 verticals based on Fortune Global 500 and Forbes 2000 list</td>
<td>Evaluation of SSO hub attractiveness for each vertical</td>
<td>Industry Vertical Specific</td>
</tr>
<tr>
<td>Additional research on selected countries, companies and SSO</td>
<td></td>
<td>Drivers for SSO: Current and Future</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Concerns for SSO: Current and Future</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Spending Trends on SSO</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Spending Levels of SSO by Business Processes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Evaluation of business processes for SSO as per perceived strategic value</td>
</tr>
<tr>
<td></td>
<td></td>
<td>SSO Party of Choice: Subsidiary, JV, 3rd Party</td>
</tr>
<tr>
<td></td>
<td></td>
<td>SSO Location Selection Criteria in terms of Importance</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Recommenders and Decision Makers on SSO</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Benchmarking of SSO Locations: Overall &amp; Function-wise</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Benchmarking of Top Locations as per key SSO location consideration parameters</td>
</tr>
</tbody>
</table>

**Primary Research**

As part of the primary research, Frost & Sullivan had established contact with 338 companies who have been selected based on the predetermined selection criteria to form the basis of analysis across the seven verticals. The primary research has served as the basis for the quantitative analysis to rank the countries for each vertical and across verticals. The methodology used for analysis has been explained in Figure 2.5 and 2.6.
Figure 2.5 Methodology for Analysis: 1

Methodology for Analysis

Total companies: 338

Weights used for overall analysis:

- In a vertical, countries scored on basis of whether they have been ranked among top of the mind locations by surveyed companies
- 50% weight if ranked as 1st preference; 30% if 2nd preference, 20% if 3rd preference
- Ranking of locations in each vertical allocated weights proportionate to the vertical’s projected SSO spend in 2006 to arrive at overall score

Figure 2.6 Methodology for Analysis: 2

Methodology for Analysis

Cost Efficiency
- Labor
- Infrastructure
- Tax & Regulatory costs

Quality of Human Capital
- Labor force skills and availability
- Education and language level
- Attrition rates

- Companies asked to indicate their top of the mind SSO locations
- Companies asked to rate the importance of each location selection criteria to get relative importance of each
- Companies asked to rate their top three locations against each criteria
Secondary Research

Extensive secondary research has been conducted to serve the following purposes:

- Comprehensively profile the selected companies for primary research
- Understand recent trends in SSO
- Develop an understanding of the strengths and weaknesses of top SSO locations

Focus Group Discussions (FGD)

As part of the project, three focus group discussions and one-on-one discussions were conducted in India, Singapore and the USA. Participants for all the Focus Group Discussions (FGDs) and one-on-one discussions were from senior management levels from Fortune 1000 companies.
3.0 SSO Determinants

3.1 Issues/Considerations

Companies across all the verticals studied have some form of SSO operations and many of them are in the process of expanding existing or setting up new locations.

The following issues and considerations, as highlighted in Figure 3.1 are important factors that need to be integrated while setting up an SSO operation.

**Figure 3.1 Issues and Considerations for SSO set-up**

Adherence to regulations as well as other compliance factors

Regulations and initiatives such as Sarbanes-Oxley (SOX), Basel-II and Data Protection laws significantly impact SSO operations. While the impact of regulations can be most acute for the BFSI and healthcare verticals; they often impact the feasibility and attractiveness of any SSO decision. The US government including the FDA has been increasing the regulatory burden on life sciences corporations. This will impact not only the companies in the vertical themselves, but also their shared services or outsourcing service providers. Stringent regulations are also present in many host countries that impact the attractiveness of the location as an SSO destination. For example, India has strict laws regulating conduct of clinical trials. Malaysia similarly has provisions with respect to storage of data involving Malaysians. A detailed study of relevant regulations in both “host” and “send” countries is essential to build in both the essential safeguards and correct evaluation of SSO locations.
Diversification of risks for SSO initiatives on a global scale

While Asia has been a favorite offshoring location for many years, many large companies have set up facilities with excess of 10,000 employees in a few countries like India and China. This concentration often exposes the company to several risks and serves as a critical parameter when they consider expansion of SSO operations. The Tsunami in 2004, flooding in Mumbai in 2005 and the political turmoil in Thailand in 2006 are examples that show the need for SSO location diversification.

Management of Impact on “Send” (Company) Economy

Often benefits from offshoring and outsourcing are perceived to be enjoyed at the cost of job losses in the ‘send’ countries. In most cases, the internal staff is handed over to the outsourcing provider; however, some job losses are inevitable, especially when offshoring is involved. An example is the deal between Wyeth and Accenture as part of which 150 of Wyeth’s clinical data management (CDM) staff work for Accenture at Wyeth’s facilities.

In the European Union, regulations that protect employees against retrenchment pose a great restraint to companies planning to outsource non-core functions. In the USA as well, with the presidential elections coming in 2008, retrenchment due to outsourcing or offshoring may re-emerge as a key issue. Any offshoring decision is often accompanied by widespread publicity campaigns against the companies involved which may seriously impact the brand image. Therefore most Fortune 500 companies typically maintain a low profile whenever they take such decisions. Companies are also working with local and federal governments to ease the pain of employees affected through outsourcing or offshoring.
Identification of Processes Suitable for SSO: outsource/offshore or onshore

Different verticals have different pecking order for services or functions when it comes to outsourcing or offshoring. For instance, FMCG & Retail companies would not outsource Strategic/ R&D for the reason that it is too core and critical to their overall marketing and product competitiveness in the market. BFSI companies are often forbidden by regulations to outsource certain processes and even when there are no such constraints; they prefer to retain in-house, activities such as interaction with premium customers. Functions such as IT Services and Support of Back Office Processing, which are not seen to be the core competencies for most companies, are often the most outsourced activities. Companies in Japan and Korea are the exception as most of them are still exploring the idea of SSO and are not ready to dabble in either outsourcing or offshoring. However, as a first step, companies need to ask themselves, “Why choose SSO” in the first place? Long-term planning often times falls prey to the operational needs and tactical decisions of the daily business. A closer look at the overall implications and fit into the firm’s strategy as well as cost/benefits is required before arriving at the conclusion of SSO being the optimal solution.

Management of Complexity and Risks

Companies are extremely concerned about losing control over their businesses in pursuit of SSO, given that this could have a serious impact on their reputation and competitive position. Especially for the financial services industry, which handles extremely sensitive customer data, a loss of such data could seriously damage a firm’s reputation and overall business. In 2006, an employee in India was arrested at a data processing center for allegedly siphoning US$420,000 from the accounts of 20 HSBC customers. Although offshoring and outsourcing services can have a significant impact on a company’s cost efficiency, incidents like the one at HSBC holds companies back from fully exploring those benefits. Because of this policy, proper risk management is a top priority for companies planning to take SSO further.

A key issue for companies considering SSO is the monitoring of processes given that offshoring and outsourcing exposes the company to several constraints: from time zone, language and cultural issues to poorly defined contracts and Service Level Agreements.
(SLAs). Lack of monitoring can easily result not only in higher costs than planned but also damages to a firm’s reputation and fines from industry regulators. Proper monitoring through established policy operational guidelines and supporting reviewing mechanisms can also help companies avoid substantial risks. For example, for Northwestern Mutual (NM), IT workers at the insurance company’s provider, India-based Infosys are only provided terminals that do not allow users to alter record or print data. Terminals are linked to NM’s servers in the US via secure, high-speed phone lines.

**Vendor selection & management**

For any company wanting to outsource their business processes, the key question to be answered is which vendor should they select? Should they entrust a single vendor to provide for all their outsourcing needs or should they be faced with management complexity issues and challenges by outsourcing to multiple providers for different functions? An example of a cancelled deal is the one between J. Sainsbury with Accenture. The service level agreement (SLA) commitment needs to be clearly spelled out and understood by both parties to avoid future misunderstandings or disappointment. Continuous and open feedback and communications are pivotal to keeping good working relationships between the buyers and the providers (3rd party providers).

Strong cultural fit and compatibility with the outsourcing service provider is a must for the success of outsourcing relationships. A global logistics company highlighted that oftentimes, senior management are highly focused on the cost-benefit aspect of shared services and outsourcing at the expense of such real-world elements as language and cultural barriers that could potentially arise in call centers, as well as a general tendency among call center staff to be overly mechanical in carrying out seemingly routine tasks. Therefore, companies often prefer to offshore business to countries with strong cultural affinity to its home market. Eastern Europe has benefited a lot from offshoring based on this criterion from other EU countries. Voice based centers located in Philippines have also been able to capitalize on their historic relationships with the USA to gain business. Proximity to customers appears to be the key criteria that media and entertainment outfits select shared service and outsourcing locations.
3.2 SSO Drivers

The key drivers for SSO across the studied verticals have been highlighted in Figure 3.2

**Figure 3.2 Drivers for SSO across verticals**

Small and large organizations across most if not all sectors analyzed in this study cite cost savings as the decisive driver of their shared service and outsourcing initiatives, generating savings ranging from 10 to 30% annually. In a similar vein, such initiatives allow many organizations to reduce operating costs by up to 40%, largely brought about by relatively lower wages in offshore locations. 90% of survey respondents highlighted potential reduction of costs as either High or Very High in terms of its importance as a driver.

The fact that shared services and outsourcing enable organizations to hone a sharper competitive advantage is widely recognized as a key motivator by companies in the BFSI, technology, energy, and transportation and logistics sectors. For technology companies, the deployment of shared services and outsourcing facilitates their efforts in improving products and service quality. 80% of survey respondents cited ability to enhance competitiveness as either High or Very High in terms of its importance as a driver.
The ability to focus on core strengths and free up resources to better serve customers and stave off competition is another critical driver, especially for the BFSI and technology sectors. Over 90% of survey respondents highlighted the ability of SSO operations to allow corporations to focus on core competencies costs as either High or Very High in terms of its importance as a driver.

The need for greater access to talent to help overcome skill shortages, especially in areas that require specific skill-sets, is what drives transportation and logistics as well as FMCG companies to pursue shared services and outsourcing. Multinational organizations have an inherent need for a centralized unit to perform key corporate tasks to support the operations of multiple offices worldwide. To that effect, shared services allow for centralization, enabling multinationals to achieve greater business efficiencies.

Continued business innovation, commonly regarded as a critical factor that shapes a company’s success, drives companies in the technology and media and entertainment sectors to embrace shared services and outsourcing. The creation of innovation hubs in offshore facilitates technology companies’ efforts in driving innovation. Similarly for the technology sector, the abundance of talent in a given offshore location addresses the perceived shortage of qualified R&D personnel in the parent company, thus driving technology companies to look overseas to serve their R&D needs.

Other key drivers include the ability to reduce time to market, particularly in the drug discovery arena. The prevalence of international mergers and acquisitions in the energy sector is spurring the need for greater streamlining of activities, uniformity and standardization. The fact that these may be achieved through shared services drives energy conglomerates to adopt this practice. This view is also shared by large automobile makers that regard shared services as playing a pivotal role in helping them manage complex internal business processes.
3.3 SSO Concerns

The key concerns for SSO across the studied verticals have been highlighted in Figure 3.3.

Figure 3.3 Concerns for SSO across verticals

The top three concerns cited by the surveyed companies across the verticals are potential compromise with confidential information, loss of control and organizational de-skilling. The risk of compromising confidentiality brought about by the widespread customer data theft and poorly enforced data protection laws in some outsourcing countries is holding back many companies particularly in the BFSI, FMCG and transportation and logistics sectors from offshoring non-core tasks. Companies are becoming increasingly wary of the high risk of breach of intellectual property, or IP, especially in countries that ostensibly lack a strong mechanism to safeguard IP rights. The risk of de-skilling along with concern for loss of control that may potentially arise from outsourcing functions that support core components is diminishing the appeal of outsourcing in favor of fully owned shared services centers.
A common concern shared by companies across all verticals is an acute shortage of suitably qualified personnel to manage a particular outsourced function and a lack of domain expertise among existing staff. A poor understanding of customers and cultural nuances are widely viewed as a deterrent for offshoring call centers overseas. The risks associated with government regulations governing outsourcing pose another obstacle to outsourcing and offshoring, particular for BFSI, technology and healthcare companies around the world.

Other deterrents include over-dependence on external organizations, inadequate world-class infrastructure and manpower and reduced service levels. High attrition rates associated with increasing wage levels in some offshore countries have also been cited as a concern by many organizations.

### 3.4 SSO Trends

**Figure 3.4 Spend on SSO by verticals and projected growth**

<table>
<thead>
<tr>
<th>Spend on SSO Operations</th>
<th>CAGR in SSO Spend by Vertical (2006-2009)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Spend on SSO by Vertical ($ bn)</strong></td>
<td><strong>Healthcare</strong> 26%</td>
</tr>
<tr>
<td></td>
<td><strong>Technology</strong> 22%</td>
</tr>
<tr>
<td></td>
<td><strong>T&amp;L</strong> 9%</td>
</tr>
<tr>
<td></td>
<td><strong>E&amp;M</strong> 10%</td>
</tr>
<tr>
<td></td>
<td><strong>Energy</strong> 6%</td>
</tr>
<tr>
<td></td>
<td><strong>BFSI</strong> 10%</td>
</tr>
<tr>
<td><strong>Average: 15%</strong></td>
<td></td>
</tr>
</tbody>
</table>
Total spend on SSO operations by the seven studied verticals are expected to grow from a base of US$ 930 billion in 2006 to over US$1,430 billion by 2009. Technology and BFSI are expected to constitute over 50% of spend on SSO by 2009. Healthcare and Technology are expected to be the key growth verticals; SSO spend by these two verticals are expected to grow at a CAGR of 26% and 22% respectively between 2006 and 2009. Figure 3.4 highlights the spending on SSO by each vertical (Fortune 500 and Forbes 2000 companies only) and the corresponding growth rates.

While the overall spend on SSO is expected to grow at a CAGR of 15% between 2006 and 2009, this spend as a percentage of overall revenues across these seven verticals is expected to remain stagnant. While sectors like healthcare and entertainment and media will see a significant increase in adoption of SSO; BFSI, technology, travel and logistics and FMCG/ Retail will witness limited increase for the same parameter. The energy vertical is expected to witness a decline for SSO spend expressed as a proportion of revenues for the vertical. This is because the revenues for the vertical is expected to grow significantly given the projections for oil prices while SSO activity is expected to grow at a relatively lower rate. Figure 3.5 tabulates the projections for the spending on SSO and the same expressed as a percentage of overall revenues (Fortune 500 and Forbes 2000 companies only), as well as the outlook for spending for the key functions.

Figure 3.5 Spend on SSO across verticals and key functions

<table>
<thead>
<tr>
<th>Spend on SSO Operations</th>
<th>Functions for SSO (Spending Levels)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Spending Trends on SSO</strong></td>
<td><strong>Strategic/R&amp;D</strong></td>
</tr>
<tr>
<td>4.00%</td>
<td>12%</td>
</tr>
<tr>
<td>4.05%</td>
<td>4%</td>
</tr>
<tr>
<td>4.10%</td>
<td>3%</td>
</tr>
<tr>
<td>4.15%</td>
<td>3%</td>
</tr>
<tr>
<td>4.20%</td>
<td>4%</td>
</tr>
<tr>
<td><strong>SSO Spending (US$ '000 Million)</strong></td>
<td><strong>IT Services &amp; Support</strong></td>
</tr>
<tr>
<td>300</td>
<td>18%</td>
</tr>
<tr>
<td>600</td>
<td>18%</td>
</tr>
<tr>
<td>900</td>
<td>38%</td>
</tr>
<tr>
<td>1,200</td>
<td>52%</td>
</tr>
<tr>
<td>1,500</td>
<td>22%</td>
</tr>
</tbody>
</table>

*Percentages shown are % of total response*
3.5 Degree of SSO by type

Results from this research shows that while many companies have some or the other experience with SSO activity, the degree to which the companies are willing to embrace SSO and outsourcing operations vary significantly from company to company. Frost & Sullivan’s study has observed the usage of SSO across all functions, however, with different emphasis, as highlighted in Figure 3.6.

**Figure 3.6 Mapping of functions for SSO and their adoption by verticals**

<table>
<thead>
<tr>
<th>Function</th>
<th>Verticals with significant adoption of SSO</th>
</tr>
</thead>
<tbody>
<tr>
<td>Finance &amp; Accounting</td>
<td>Energy, FMCG &amp; Retail, Media &amp; Entertainment, Technology, Transport &amp; Logistics</td>
</tr>
<tr>
<td>Back-office Processing</td>
<td>BFSI, Energy</td>
</tr>
<tr>
<td>IT Services &amp; Support</td>
<td>Common across all industries</td>
</tr>
<tr>
<td>Customer Service</td>
<td>BFSI, FMCG &amp; Retail, Media &amp; Entertainment, Technology, Transportation &amp; Logistics</td>
</tr>
<tr>
<td>Human Resources</td>
<td>Common across all industries</td>
</tr>
<tr>
<td>Corporate Learning</td>
<td>Energy</td>
</tr>
<tr>
<td>Procurement</td>
<td>FMCG</td>
</tr>
<tr>
<td>Research &amp; Development</td>
<td>Healthcare, Technology</td>
</tr>
</tbody>
</table>

**IT Services & Support**

As IT becomes more and more closely integrated and an inseparable part of the business environment, organizations feel that the operations and support functions can be handled best if they are either outsourced or centrally managed through a few captive centers around the globe.

All verticals have seen instances of companies outsourcing IT services and support to specialized players like IBM, EDS, and Accenture etc. as a part of multiyear and multimillion dollar deals. A good example to illustrate this type of outsourcing is Vodafone. In October 2006, Vodafone decided to outsource its IT operations to IBM and EDS in a
multiyear contract that spans for seven years. The company has not released any financial details of the deal, however said that it will help it save US$ 600 million in maintenance costs.

**Human Resources**

With business going global and having multiple locations, managing human resources across the organization is becoming more and more challenging. Human Resources departments not only have to deal with host of specialized functions like payroll operations, benefits administration, employee records and data management and asset management services.

The answer to this problem has emerged through HR outsourcing. There are a host of companies specializing in this field, e.g. Hewitt Associates. Sony Electronics has outsourced its HR functions to Hewitt Associates. Sony claimed that Hewitt's HR outsourcing services will enable Sony Electronics to focus on its strategic human resources functions, freeing the HR staff from day-to-day management of essential but non-strategic duties. Standard Chartered for example set up an HR Shared Services Center in Chennai, India with the aim to deliver a consistently high service for its global operations. Services like payroll operations and benefits administration fall under these initiatives.

**Finance and Accounting**

SSO services within this category include: General Accounting (Bookkeeping, A/P, A/R), Bank Statement Consolidation, Payroll and Tax returns, Financial Analysis and Reporting (Balance Sheet Analysis), Non-Profit Accounting, and Check Processing. SSO for finance and accounting services is especially common for FMCG/ Retail and Energy verticals.

BP outsourced its finance and accounting to two centers, one in Budapest to serve the European customers, the other in Calgary to serve the American customers. The Budapest center is run by EDS, with an investment of US$ 8.5 million. The Calgary center is run by IBM, a three-floor data center. ExxonMobil also runs a shared service in Czech Republic for the finance and accounting.
Customer Service

Call center off-shoring has been motivated by two key factors – cost and operating efficiencies. The technology, BFSI, FMCG/Retail and Transportation and Logistics sector has many examples of companies which have either outsourced customer service and call center functions to third party providers in low cost countries or have set up their own captive centers in low cost destinations to serve its customers globally. HP is one good example; HP runs its entire call center operation through its centers in India.

Research & Development

Outsourcing of R&D functions has been a topic of hot debate for the last couple of years. For example in the technology sector, what started as Original Equipment Manufacturing (OEM) outsourcing and transformed into Original Design Manufacturing (ODM) is now transforming into full fledged outsourcing of R&D functions.

Similarly, in the pharmaceutical sector, generic drug companies from Asia, which were considered a threat to big pharma from the USA and Europe, have now become strategic partners in the quest to discover new chemical entities and drug discovery. These generic drug companies also offer a host of specialized services in the clinical trails phase. FMCG companies on the other hand typically tend to keep R&D in-house.

Corporate Learning Programs

In lines with HR processes, several companies have also outsourced Corporate Learning programs to specialists. BP outsourced corporate learning programs to Exult that provides global access for all BP employees to a tailored digital skills curriculum to support the development of IT skills and a global hosting environment for custom BP e-Learning.
**Back-Office Processing**

Back-office processing make up the largest portion of the BFSI SSO market, credit card and other transaction processing, for example. Bank of America has a shared services center in India for back-office processing. HSBC set up its Electronic Data Processing unit in Hyderabad, India, which controls back-office processing in Bangalore, Visakhapatnam. The three processing centers have a staff of more than 4,500 employees. Citigroup chose China as a location for its back-office operations.

**Procurement**

Procurement has emerged as a key business processes for SSO for FMCG/ Retail vertical. It is also extensively practice by IT verticals especially for IT related procurement. Tasks within this function include supplier sourcing and management (supplier’s pricing & performance), continuous savings implementation and transaction management. Walmart, in China, procured more than US$ 7.5 billion worth of Chinese goods through its procurement center in Shenzhen, Guangzhou province (south of China), which is more than half of its global volume of direct imports. While some firms prefer to have a wholly owned procurement unit, some companies outsource this function to specialized procurement service providers. For instance, Kimberly Clark hired procurement specialist ICG Commerce in 2005 for its procurement needs, as part of a five years contract.
3.6 SSO Party of Choice

There are currently three models of SSO being adopted by the Global Fortune 500 and Forbes 2000 companies. They either own the operations fully, set up joint-venture with reputable third/external party or completely outsource the operation to SSO providers. Their preference for either mode of operations is shown in Figure 3.7. 64% of the SSO operations of the surveyed companies are wholly owned; the corresponding numbers for Joint Venture and 3rd party outsourcing are 17% each.

Figure 3.7 SSO Party of Choice across verticals

<table>
<thead>
<tr>
<th>SSO Party of Choice</th>
<th>SSO Party of Choice per Function</th>
</tr>
</thead>
<tbody>
<tr>
<td>Third Party</td>
<td>Wholly Owned: 64%, Joint Venture: 17%, Third Party: 17%</td>
</tr>
<tr>
<td>Joint Venture</td>
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</tbody>
</table>

Own Facility

In this model, the organization owns the entire physical infrastructure. In addition, the company is directly responsible for its employees' recruitment and welfare. Companies which are concerned about loss of control, protection of intellectual property and might face regulatory hurdles choose this model. This model is most extensively used by BFSI companies for their business processes which cannot be outsourced due to regulatory constraints and also by companies in other verticals willing to maintain greater control.
For example, Shell runs five shared service centers that are fully owned subsidiaries: located in Cyberjaya (Malaysia), Glasgow (UK), Krakow (Poland), Manila (Philippines) and Guatemala. The reasons for Shell to choose fully owned centers are concerns about losing command and influence with outsourcing. Boeing and Maersk’s corporate learning programs are conducted internally while Qantas and Northrop Grumman’s procurement activities are centrally managed from their respective shared service centers.

*Hybrid Relationships*

The two most common forms under this model are joint ventures and collaborative partnerships. This model is sometimes preferred because of the element of control it provides without the risks of running subsidiaries. In 2004, Quintiles and Solvay entered a unique risk-sharing agreement under which Quintiles will invest US$25 million worth of development services for ten of Solvay’s phase II projects from 2004-06, thereby bearing around 50% of the risk. Solvay would provide Quintiles with milestone payment for each of these projects reaching phase III. Unlike similar previous deals, however, Quintiles will not receive royalties from drug sales.

*Third Party Provider*

This model is where third parties carry out majority if not all of the organization’s specified business processes. This model has been most prevalent for IT services across all verticals. As part of a US$1.8 billion outsourcing initiative, Dutch bank ABN Amro, in 2005, signed a deal with Indian IT services companies Infosys and TCS for application support and enhancement. The bank already had a US$1.5 billion desktop outsourcing deal with EDS for its wholesale operations. As HR outsourcing matures, Frost & Sullivan are likely to see this model adopted in for HR services as well. In February 2007, TalentTrack announced outsourcing agreement with Tenet Healthcare Corporation to assist its hospitals in developing an efficient, consistent and centralized physician recruitment process that will support the system’s targeted and aggressive growth initiatives. Similarly, companies are increasingly outsourcing their call centers to external parties. BSkyB is just an example of an increasing number of companies that have outsourced their call center operations, in this case, to U.K. based Response Handling.
3.7 SSO Locations

3.7.1 Selection Criteria

Key factors considered while deciding upon location for SSO are compensation, infrastructure, and tax and regulatory costs; labor force experience and availability and regulatory environment for IP as highlighted in Figure 3.8.

Figure 3.8 Location Selection Criteria for SSO across verticals

Labor Costs and Availability

Historically, companies have regarded labor costs and availability as paramount to their decision in its selection of SSO locations. Across verticals, search for low cost options for operations have driven SSO activities. As an example of labor cost arbitrage: In Ireland, a call center agent’s average salary is around US$ 23,000 – US$34,000 annually as compared to a US$2,800 annual salary for a similar position in developing countries such as Malaysia and the Philippines. A growing number of Hollywood studios are already harnessing the scalable pool of animation talent that India has to offer at half the cost of performing the same services in the United States. In the healthcare vertical, CROs are
expanding into low cost geographies especially to India and China. Costs are low in these countries not only because of shorter time taken to recruit patients for clinical trials but also due to lower salaries for the employees involved. The presence of excellent institutes for higher education in India, China, East Europe and Russia has made these locations attractive for high end R&D activities, especially for the healthcare and technology sector.

However, high demand has caused attrition rates and remuneration to increase sharply in India, especially for jobs that require better skilled programmers and for middle management. Firms like ABN Amro face situations where they invest several months into training individuals only to see them shift to competitors after one year for higher salary. It is this wage inflation that made companies to consider countries like China which are at the earlier stages of SSO demand. The problem with alternatives in the region is that in the case of China for example, graduates and professionals are not necessarily equipped with sufficient language and domain skills.

**Intellectual Property & Confidentiality Protection**

A location’s ecosystem for protecting intellectual property plays a key role while deciding SSO locations, especially for functions involving data or concepts essential to core competitiveness of the company. The US and especially the EU have laid down strict and clear provisions over the transfer of data to third countries. As a consequence, some FMCG & Retail companies rather set up their SSO operations in the USA, UK or other European locations where the regulatory systems are well enforced and clearly written. Several SSO locations are now taking active measures to address these concerns. For example, India is initiating to draft bills which are similar to UK’s Data Protection Act and would negotiate for an agreement that resembles the US-EU efforts in providing for ease of transferring data between EU nations and the USA documented in the US Safe Harbor framework.
Infrastructure Costs and Quality

Across verticals, infrastructure quality and cost is a key determinant to its overall attractiveness for SSO. For example, BMW regards telecommunications costs as an important consideration in its selection of offshore locations. Top energy vertical companies such as ExxonMobil, Shell and BP have their shared service centers located in South East Asia and Eastern Europe where the infrastructure cost is much lower compared to North America and Western Europe. Many respondents feel that even though India’s overall labor costs is low, the cost benefit is to an extent overrun by its poor infrastructure. Apart from power supply, logistics and transportation infrastructure are critical for FMCG & Retail companies, especially for its procurement centers where China scores substantially better than India.

Government incentives (Tax and Regulatory costs)

Many companies have highlighted favorable government policies to be a compelling reason as to why they want to start their SSO operations in a particular country. Czech Republic provides up to 50% of eligible business expenses as subsidy, 35% of special training costs and 60% of general training costs for companies interested in setting up their SSO centers there are also eligible for subsidies. China has Special Economic Zones (SEZ) that promote high international quality standards in the Hainan Province, Shenzhen or Shantou with financial incentives. India is also deploying a comprehensive SEZ scheme. Flexible labor laws that make it easy to attract foreign talent are key drivers as well. Locations like Singapore and Dubai deserve special mention in this context. Among other factors, proximity to key markets have also been highlighted as a key decision criteria.
Proximity to Key Markets

Another criterion that is growing in importance is proximity to key markets to help monitoring and eliminate language and cultural issues when it comes to SSO. Many utilities and media companies chose to set up their shared service center in their home country. These companies are generally not multinational companies and hence, prefer to stay in home country. Often these companies are also the chief source of employment in the region and fear political backlash if they were to offshore functions.

Another trend for large companies is to have one hub in Asia to serve the APAC region, one hub in Europe to serve the European region, one Latin American country to serve the South American markets, and so on instead of one or two hubs to serve many regions. Denmark, that provides good geographical position to enter the Nordic region, has been thereby able to attract companies like Christian Dior and the Gillette group (under Procter & Gamble). As many companies have highlighted that even though there are many cheaper locations for them to choose from such as Russia, India or China, they feel more comfortable if they are able to fly their team in within a short span of time (less than 6 hours) if there are any issues in their SSO centers to resolve those problems. Coca-Cola for instance, kept their shared services center onshore in Tampa, Florida, USA which is only a mere 1.5 hour’s flight to its headquarters in Atlanta, Georgia, USA.

When it comes to decision making, key decision makers are the CEO, COO and Functional heads. Regional/ Geographic managers and interdepartmental teams are the key people involved when it comes to recommending locations for SSO.
3.7.2 Top of the Mind Locations

Based on the research and interviews with companies across all seven industry verticals, Frost & Sullivan have identified India and China as the top locations for SSO. Ireland, Singapore and Malaysia are ranked third, fourth and fifth respectively with limited difference between their overall scores. Compared to Frost & Sullivan’s previous study, the preference for Malaysia and Mexico as an SSO location has improved whereas that for Philippines and Canada has dropped. The section below provides a detailed overview of the leading and emerging ten countries.

Incumbent Top - India

Current SSO Situation

India is the leading SSO destination in the world. While service providers are maturing and moving up the value chain, the market is experiencing consolidation and high levels of absorption. Providers are also expanding their onshore presence to strengthen their global delivery capabilities. Demand for experienced professionals is outpacing their supply and attrition levels in the industry remain between 25-40 percent. India hosts both captive and outsourced operations of major corporations like JP Morgan, British Airways,
GE, Accenture, IBM, etc. with several of these centers employing in excess of 10,000 employees.

Strengths & Weaknesses

- Strengths: Large talent pool, English speaking labor force, cost efficiency, and increasing sophistication of local BPO and ITO players are some of the strengths that India possess as an offshoring destination.

- Weaknesses: Poor infrastructure, rising wages, and the appreciation of the Indian Rupee against the US dollar.

Government Initiatives to promote SSO

The central and state governments have whole heartedly supported the industry. Some of incentives provided are – Special tax arrangements, rebate on cost of land, concession in power tariff, special incentive packages for project valued at more than US$ 10 million. Indian state Governments have taken the following steps to boost the growth of the SSO industry within their domains:

- A majority of the states have enacted laws to allow employees to work on National Holidays; allow women to work in night shifts; and offices to function 24 hours a day, all through the year (i.e. 24x7x365).

- State Governments have announced IT policies that seek to create (through focused Human Resources Development (HRD) programs), a trained pool of manpower with the skills and aptitudes appropriate for the SSO industry requirements. Bridge programs for engineering graduates, communicative English, soft skills, accent neutralization, IT ENABLED SERVICES (ITES) sub-domain level training, etc. have been given focused attention by the state governments.

Most of the states in India have Software Technology Parks (STPs) and Export Processing Zones (EPZs) offering world-class infrastructure with reliable data communication facilities.
SSO Outlook

India will continue to be a leading destination for offshoring in the near future. The advantages which India offers far outweigh the concerns. Indian outsourcing outfits are growing rapidly and becoming global players. For example, Tata Consultancy Services (TCS), Infosys, and Wipro have each over US$ 3 billion in sales and in excess of 60,000 employees located across the globe. In addition to this, already established global players continue to add to their headcount in India. India is also emerging as a location of choice for high end research and design work especially in the technology, automotive and the pharmaceutical sector.

Leading Challenger - China

<table>
<thead>
<tr>
<th>Country Snapshot</th>
<th>SSO Environment Snapshot</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>GDP per Capita</strong></td>
<td>US$7,600</td>
</tr>
<tr>
<td><strong>GDP Growth</strong></td>
<td>10.5%</td>
</tr>
<tr>
<td><strong>Population</strong></td>
<td>1.3bn</td>
</tr>
<tr>
<td><strong>Total Workforce</strong></td>
<td>918m</td>
</tr>
<tr>
<td><strong>Business Environment Conductiveness</strong></td>
<td>Politically stable given a single party ruling, the Communist Party of China.</td>
</tr>
<tr>
<td></td>
<td>Rated poorly in terms of corruption</td>
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<td></td>
<td>45,400 km of expressway, 78,000 km of railway network in 2007 as well as over 500 airports.</td>
</tr>
<tr>
<td></td>
<td>Spent just over US$136 billion on R&amp;D in 2006 and it now ranks second worldwide with 926,000 researchers</td>
</tr>
<tr>
<td><strong>Cost Efficiency</strong></td>
<td>GDP growth at 10.5%</td>
</tr>
<tr>
<td></td>
<td>Annual salaries for entry level staff starts at US$5460, Team Lead with 2-3 years experience can earn US$8,800 annually and managers with 5 - 8 years of experience can obtain a salary package of US$13,732.</td>
</tr>
<tr>
<td><strong>Quality of Human Capital</strong></td>
<td>629 higher learning institutions across China with the most famous being Tsinghua and Beijing University, the equivalent of MIT and Harvard in China</td>
</tr>
<tr>
<td></td>
<td>Out of the 202,600 graduates in China, 38,400 are PH.D and 164,200 are master’s degree holders.</td>
</tr>
</tbody>
</table>

Current SSO Situation

China remains a favorable hub for SSO activities given its talent, ability to scale, huge local market, world class infrastructure in major cities, and other attractive factors that will spur China ahead, such as the hosting of the Olympic Games in 2008 in Beijing as well as the Expo 2010 - World Fair in Shanghai in the year 2010.
China has managed to attract names like IBM, Accenture, SONY, NEC, Rockwell, BearingPoint, Matsushita, Ericsson, Nokia, GE, Dell, SAP, Satyam and other MNCs to establish their application development centers as well as BPO and IT Services centers in software parks across China. From the banking industry, Citigroup chose China for its back office operations in addition to its existing center in Singapore. Japanese outsourcing to Dalian, China, reached US$ 375 million in 2004. Major pharmaceutical companies such as Roche, GlaxoSmithKline and Eli Lily have established their R&D centers in Shanghai, China thus implying the high quality of Chinese talent in the R&D segment of biotechnology and healthcare. For the FMCG & Retail sector, China is at the forefront for procurement tasks.

**Strengths & Weaknesses**

- **Strengths:** Abundance of human capital especially for R&D functions, relatively cheaper human resource than most competing nations, and huge potential of local market

- **Weaknesses:** Lack of English speakers and domain expertise (e.g. for BFSI), no single government body to handle and coordinate SSO enquiries/ investments and IP related risks

**Government Initiatives to promote SSO**

There is no single government body such as MDeC in Malaysia or iDA in Singapore to handle SSO related matters. Corporate tax rates are non-uniform across China. For example, Shanghai and Guangzhou taxes are at the high end of 33% and 30% respectively whereas Zhuhai stands at an attractive rate of 15% and Dalian at 24%. The Chinese government has designated several cities in China to be the hub of excellence for SSO activities, namely, Beijing, Shanghai, Hangzhou, Tianjin, Nanjing, Chengdu, Xi’An, Shenzhen and Dalian.
SSO Outlook

China is unique compared to other SSO contenders due to its ability to cover lower end functions such as back office processing to high value functions such as R&D. Even though the Chinese government has earmarked many major cities in China as hub of excellence for SSO, there is a lack of collective measures from the various government agencies involved to ensure the success of these cities. However, China will remain as one of the strongmen in the arena of SSO given its labor force skills and availability and demand from primary markets (support services to the ‘Global production house’).

Legacy Sustainer - Ireland

<table>
<thead>
<tr>
<th>Country Snapshot</th>
<th>SSO Environment Snapshot</th>
</tr>
</thead>
</table>
| **Business Environment Conductiveness** | • Total investment of approximately US$ 250 billion for national development in the next 7 years.  
• Ranked 2nd out of 60 countries in World Competitiveness Report for education system and 3rd for per capita productivity  
• One of the most beneficial corporate tax regimes in the world with 12.5% corporate tax. |
| **Cost Efficiency** | • Labor costs are fast increasing; higher than many EU countries |
| **Quality of Human Capital** | • 3rd out of 60 countries for per capita productivity in the World Competitiveness Report 2005  
• Over 39% of Irish people aged 25-34 have a third level education  
• Highest output of Science and Engineering graduates within Europe. |

| GDP per Capita | US$43,600 |
| GDP Growth    | 5.2%      |
| Population    | 4.1m      |
| Total Workforce | 2.1m |

Current SSO Situation

The base layer of the offshoring value pyramid – running infrastructure and applications – is currently where most of the action is in the Irish offshoring market; however, this tends to be a commodity business and therefore, Ireland is losing its share. However, many healthcare and technology companies have established their R&D centers in Ireland with the entertainment and media vertical exploring the location for their offshoring initiatives.
Global leaders such as Accenture, Allergan, Black & Decker, Citigroup, Colgate, Oracle, Pfizer, Microsoft, Whirlpool, Xerox, Hertz, IBM, Dell, RCI, AOL, eBay, SAP, Siemens, Bertelsmann, etc. have located pan-European/EMEA/Global centers in Ireland.

**Strengths & Weaknesses**

- **Strengths:** World class infrastructure, talented workforce and government support
- **Weaknesses:** Small size of labor force and high cost of living

**Government Initiatives to promote SSO**

Ireland has one of the most favorable corporate tax environments in the world. Ireland's tax credits are provided for incremental expenditure on Research and Development. Ireland also has a favorable holding company regime and double taxation agreements with 44 countries.

**SSO Outlook**

Going forward, Ireland is likely to continue losing share in low value operations. Though it has held on to its position as a top location for SSO, its value proposition is eroding fast. However, it is generating significant interest for higher value activities like R&D with leading healthcare and technology firms such as Wyeth, GlaxoSmithKline, Microsoft and Oracle investing in R&D facilities in Ireland.
Emerging Proposition - Malaysia

Current SSO Situation
Malaysia has established itself as a strong player in BFSI, T&L and Energy verticals and as an emerging location for Technology. Recent SSO investments include Dell’s Malaysia Enterprise Command Center, Satyam’s Global Solutions Center and Al-Jazeera’s regional broadcast center. Successful SSO operations include DHL, Shell, HSBC, Standard Chartered’s Scope International shared services center, Monster Technologies, TRW and British American Tobacco’s Group Service Delivery (GSD). Malaysia is also witnessing continued expansion from existing players such as IBM with its recent Asia Pacific Finance Regional Support Center.

Strengths & Weaknesses

- **Strengths:** Multilingual and multicultural workforce to serve different regions, low wage inflation (5.5%) and the lowest turnover (5%) of staff in Asia Pacific (source: MSC Malaysia)

- **Weaknesses:** Lack of qualified human resource especially in the field of R&D
Government Initiatives to promote SSO

MSC (Multimedia Super Corridor) Malaysia status companies operating in Cyberjaya, Technology Park Malaysia, Kuala Lumpur City Center, Kuala Lumpur Tower, Bayan Lepas, (Penang) and Kulim High Tech Park in Kedah enjoys the following incentives:

- Eligible companies can apply for Pioneer status that provides tax exemption of 100% for a period of 10 years or Investment Tax Allowance of 100% on the eligible capital expenditure incurred within 5 years (to be offset against income for each year of assessment)

- R & D grants (for majority Malaysian owned MSC Malaysia status companies)

Other advantages of MSC Malaysia include duty-free import of multimedia equipment, excellent physical and IT infrastructure, a focused single point of contact (the Multimedia Development Corporation to provide assistance within MSC Malaysia), high quality, planned urban development, etc.

The MSC Malaysia KDI (K-workers development institute) initiative to help graduates develop and acquire the necessary skills in ICT is lauded by many respondents as a good measure to improve the technical skills of SSO workers.

SSO Outlook

While Malaysia may not be able to meet the growing requirements of SSO operations as compared to countries with an abundance of workforce such as China and India, it will remain a highly attractive proposition when compared to similar competing locations such as Eastern Europe, Philippines and Latin American countries given the traction it has received in key verticals such as Banking and Finance, Energy and Transportation and Logistics.
4.0 Vertical Analysis

4.1 Finance & Insurance

The Banking, Financial Services and Insurance industry (BFSI, or FSI for short) consists of major players such as Citigroup, Goldman Sachs, American Express or American International Group. Increasing pressure to outperform competitors and the search for new revenue streams is driving the overall business landscape and strategies of the industry. BFSIs will further try to profit from the favorable economic conditions to widen their reach and improve product and service portfolios. Size matters – and is leading BFSIs into developing markets that provide access to a vast customer base – e.g. China. Apart from a strong and ideally global presence, BFSI’s find that their customers want to be treated with excellent services and products that are tailored to their needs. All these factors need to be considered with while adhering to increasingly strict regulatory requirements such as Basel-II and Sarbanes-Oxley. The following sections provide an overview on how Shared Services and Outsourcing affect the BFSI industry as it strives for increasing competitiveness while reducing costs. The top two locations remain India and China with Singapore coming in at number three.

Despite the high attrition rates and wage inflation, respondents believe that India will remain top choice for FSIs in the medium term. Apart from also having a huge and highly educated workforce, China attracts companies with lower wages, and improving English language capabilities. BFSI companies work together with local universities to develop curriculums that especially cater to their needs and churn out graduates that are perfectly trained for the companies’ needs. With the 2008 Olympics coming up, the event may give the country a big boost that will further stimulate its attractiveness as offshoring location. Singapore’s progressive Finance sector is facilitated by its positioning as a strategic mid-office center and as an emerging global private banking hub, e.g. regional financial control and credit (e.g. mature foreign currency market) management and risk management. Among banks with SSO presence in Singapore include Citigroup, ABN Amro and Deutsche Bank. Malaysia is also a key location for SSO with organizations such as HSBC and Standard Chartered having set up extensive operations to capitalize on the robust reporting standards and also the diversity of talent.
In regions outside of Asia, looking at the restrictive environment in the EU, BFSIs in this region look towards Eastern Europe for their language abilities and similar cultural basis. Although those locations do not have wages as low as Asian countries, but they offer a highly skilled workforce that is available next door for a good price. For North America, destinations like Canada or South America are attractive for the same reasons. Although countries in Asia may offer lower wages, firms find it easier to handle SSO operations if the offshoring location is nearby, i.e. can be reached within one or two hours by plane and offers language as well as cultural similarities. Other emerging locations include Dubai and Philippines. The Philippines is especially preferred for customer service and call center functions. Dubai on the hand has set up a dedicated Dubai Outsourcing Zone (DOZ) to target SSO investment among BFSI (e.g. AXA Insurance) and Technology (e.g. Microsoft) verticals.
4.2 FMCG & Retail

With a predicted rise of global middle class by the World Bank, and most Fortune 500 and Forbes 2000 FMCG & Retail companies recording double digit growth in terms of net income and sales in 2006, the sector looks set for a rosy and healthy future.

USA based FMCG & Retail companies account for a large majority of both the Fortune 500 and Forbes 2000 lists covering a total of 54.1% and 47.95% respectively in terms of number of companies in the lists. European based companies come in second place at 34.43% in the Fortune 500 and 28.77% for the Forbes 2000 list. In other words, any hiccups or movements in the USA and European based FMCG & Retail companies would have a major impact on the overall market worldwide. In mature markets, retail sector companies are constrained in their ability to grow and maintain profit margins as a result of a pressure on prices, market saturation, and slowing population growth. Threat to house prices in the US also poses risk for consumption growth.

As a consequence, the strategic focus of the sector is moving towards the emerging economies and expanding consumer markets of Asia and Central & Eastern Europe - China and India in particular - which offer new opportunities for growth through global sourcing, off-shoring and the development of modern retailing.

Some unlikely names are not only the top of mind locations for SSO operations but also actual sites which host a multitude of SSO functions for many Fortune 500/Forbes 2000 FMCG & Retail companies. The most commonly heard names are India, USA, UK, Poland, Czech Republic, Mexico and Malaysia. China is not on the list as many FMCG & Retail companies view it as only a great hub for procurement but not other functions.

After tallying in the top of mind rankings from the FMCG & Retail industry respondents, it is learned that India, USA and UK are the top three SSO locations for this vertical with India and USA tying in terms of the number of number 1 rankings (20% each).
India leads in terms of overall cost efficiency due to its relatively cheaper wages. USA leads the pack in terms of overall business environment conduciveness and that is not difficult to see why because many FMCG & Retail companies are headquartered in the USA and the familiarity to the USA helps to boaster its image as a hub of excellence for SSO operations. In terms of human capital quality, USA workers emerge at the top.

India’s ability to attract major retailers such as Supervalu (US), Tesco (UK) and Target (US) along with FMCG giants such as Unilever (Netherlands), Procter & Gamble (US), are testaments to India’s attractiveness as a shared services and outsourcing center. India is especially favored for IT Services & Support function, which many FMCG & Retail companies feel that India has a sufficient pool of such talents from shared services & outsourcing centers from other verticals with the necessary transferable skills. Scalability is also not an issue for SSO centers operating from India as can be seen by Tesco’s interest to double its Hindustan Center headcount and many other FMCG & Retail companies’ future plans to increase headcount for their SSO operations in India.
The homeland to most FMCG & Retail companies, USA is also within the radar of being one of the hot favorites for FMCG & Retail companies to base their SSO operations in. It should be noted that most FMCG & Retail companies in the Fortune 500 and Forbes 2000 lists are headquartered in the USA, which explains why they prefer to work within a familiar territory. Coca-Cola’s Finance & Accounting shared services center in Florida, Royal Ahold group’s IT services operations in Pennsylvania and the State of New York and Levi Strauss in Oregon are some of the many examples of FMCG & Retail SSO sites in the USA.

UK has not only been very successful in convincing many of its ‘local’ Fortune 500/Forbes 2000 companies to host their SSO functions there but also attracted many ‘foreign’ FMCG & Retail companies to establish their SSO presence there. For instance, US based Procter & Gamble has a Global Business Services Center in Cobalt Park which serves the European, Middle East and Africa markets, home grown retailer Marks & Spencer operates its HR, Finance & Accounting and Customer Service & Call Centers in Manchester, US based FMCG giant Kimberly Clark currently hosts a Finance & Accounting shared services center in Brighton, England’s own J. Sainsbury established a Finance & Accounting in Streatham, and US food company Kellogg’s has a Finance & Accounting shared services center in Manchester city. The presence of all these brand names in UK indicates the country’s good standing as a shared services hub and many respondents highlighted that UK was chosen due to its close proximity to many European countries, the English language capability, the experienced workforce for high end functions such as risk & tax management and the excellent educational system which churns out valid and marketable graduates for the shared services and outsourcing industry.
4.3 Technology

Though the Technology industries — semiconductors, software, computers, telecommunications and networking — have matured over the past 25 years, technology companies have to wrestle with constant challenges. Access to capital, faster time-to-market, and finding and keeping the right talent are more critical than ever; so is managing stakeholder and financial market expectations.

The most preferred locations for SSO operations for the technology vertical are India, Ireland and China as highlighted in Figure 4.3. Emerging locations include east European countries, Malaysia and a few Latin American countries. India ranks very high on key parameters.

Figure 4.3 Technology: Evaluation of Top SSO Locations
The growing demand for outsourcing jobs in India is attracting several new entrants into the business, increasing competition and resulting in higher wages. However, India is also moving up the value chain with global majors such as Texas Instruments, Sony Ericsson, Cisco etc. having set up R&D centers there. Several global technology majors, including Google, Motorola, and Toshiba, have begun deploying R&D or shared services centers in China. Ireland has been able to sustain its positioning as the preferred location for R&D functions and regional headquarter operations with firms such as SAP, Oracle, Microsoft, Lucent, etc.
4.4 Energy

The Energy sector can be broadly represented by two categories. They are Oil & Gas (Petroleum Refining) and Utilities. Top 5 Oil & Gas Operations include ExxonMobil, Shell, BP, Chevron and ConocoPhillips while top 5 Utilities include State Grid, EON, Électricité De France, Suez and Gazprom. Oil & Gas Operations generally have operations worldwide while Utilities typically have offices and are usually the main energy providers only in their home countries. According to OECD, global demand is expected to grow by more than half over the next quarter of a century. Investment needs exceed US$20 trillion, mainly because of higher unit costs.

Oil and gas prices are at record highs, and are not expected to decline given the growing demand for these resources. Energy companies are diversifying their product mix, as non-traditional fuel sources become more price competitive, and alternative fuels are gaining interest. New investment in LNG, oil sands, oil shale, ethanol and other sources and products are showing rapid growth.

Things are equally turbulent for the utilities sector where previously sacrosanct national boundaries are falling as cross border investment progresses, particularly in the EU.

The most preferred locations for SSO operations for the energy vertical are the Singapore, Malaysia and Philippines as highlighted in Figure 4.4; emerging locations include Poland while Ireland is witnessing decline. The comparison of top locations is shown in Figure 4.4.
Singapore, with its strong business environment conduciveness and high quality of human capital, becomes the top of the mind SSO location. The ease of recruiting talents, robust infrastructure and logistics together with stable politics form some of the factors that have attracted these companies to locate their SSO centers in the island. For example, ExxonMobil has a 60-high quality team in Singapore, comprising experienced systems engineers and business specialists, and the country is the Asia-Pacific project and support center for its Global Enterprise Management System (GEMS). The GEMS platform supports common worldwide business processes, including procurement, production planning and quality management and customer orders.
Malaysia ranks in the second place in the top of the mind SSO locations ranking. The country provides a relatively high standard of labor force in the region, with multi-lingual capability at relatively low cost. Shell Information Technology is a notable example as it serves as a regional center to provide centralized IT services and solutions. ExxonMobil Business Support Center, on the other hand, provides regional shared services and data support activities to its internal customers.

The Philippines, with its strong cost efficiency, is another top of the mind SSO location. The Philippines provide high standard of infrastructure quality at a lower cost due to its liberalized telecommunications industry. Furthermore, its strong tie with USA in the past provides an attractive force to American companies and a strong momentum for European companies to set up SSO in the Philippines. For example, Chevron set up its Manila Shared Service Center in 1998 to support the Asia Pacific and US operations. The center offers 3 services, namely Finance and Accounting, SAP support and HR support. The other notable shared service center that follows the trend is Shell Shared Services.

Poland is one of the main SSO hubs for major European companies, due to its geographical proximity and cultural similarity advantages. For example, Shell has a shared service center in Krakow while Centrica plans to open a call center in the same place in 2009.

Many utilities companies located in USA prefer to set up domestic SSO centers. This is because they are often not a multinational entity with most employees residing in the home country like in TXU’s case. While the infrastructure cost is high, most of these costs are sunk costs by nature. The utilities are not able to take advantage of the lower tax incentives in the foreign countries because much revenue is still derived within the country. And even with tax saving in certain states, the saving will usually pass to the consumers due to intense competition. Furthermore, most utilities are one of the major recruiters in any city and fear potential political backlash in case they relocate operations.
4.5 Healthcare

Patient and managed care, pharmaceuticals and life sciences & biotechnology constitute the healthcare sector. The healthcare sector faces a growing imbalance of supply and demand. On the demand side is a large population of aging patients, specifically in the USA and Western Europe, putting pressure on healthcare systems. The supply side, however, is constrained by increasing regulatory oversight, declining profitability, thinning R&D pipelines, growing generic competition, and skyrocketing operating and marketing costs.

**Figure 4.5 Healthcare: Evaluation of Top SSO Locations**

<table>
<thead>
<tr>
<th>Location</th>
<th>Overall Score</th>
<th>Score across Key Parameters</th>
</tr>
</thead>
<tbody>
<tr>
<td>India</td>
<td>3.78</td>
<td>3.76 4.05 3.49</td>
</tr>
<tr>
<td>China</td>
<td>3.64</td>
<td>3.42 4.09 3.37</td>
</tr>
<tr>
<td>Ireland</td>
<td>3.53</td>
<td>2.15 4.15 4.34</td>
</tr>
</tbody>
</table>

- **Score across Key Parameters** include:
  - Cost Efficiency
  - Quality of Human Capital
  - Bus. Envt. Conduciveness

- **Emerging Locations**: East-EU: Czech Republic, Poland; Singapore
- **Stable/Declining Locations**: UK, Canada
The most preferred locations for SSO operations for the healthcare vertical are India, China and Ireland as shown in Figure 4.5 provides their comparison. India was ranked as the number one choice for SSO operation by 10% of the companies. Even though China was indicated as the first choice by 12% of the companies, factors like quality of manpower, cost effectiveness etc. tilt the balance in favor of India as the most preferred destination. Ireland came in third as most preferred destination for healthcare SSO operations.

Pharmaceutical industry in India is one of the fastest growing sectors. The industry has achieved global recognition as a producer of generic products and low-cost high-quality bulk drugs and formulations. There is also an increase in collaborative outsourcing to India. For example, Ranbaxy has made an agreement with GlaxoSmithKline in discovering and developing new drugs for some of the selected therapeutic areas. According to Confederation of Indian Industry (CII), R&D in India has rapidly grown from US$52 million in 2000 to US$320 million in 2005, which will account for 5% of total turnover of local pharmaceutical sector. It is estimated that in the coming eight to 10 years, the total pharmaceutical R&D outsourcing from the United States to India will be valued at US$1.5 billion. CII also suggests that the cost of clinical trials in India is less than one-tenth of the costs in Western countries. The total R&D investment from India's top 10 pharmaceutical companies crossed US$170.0 million in 2004. The number of international pharmaceutical firms with a research presence in India has increased significantly during the past five years. AstraZeneca had established a major R&D facility in 2003, and also expanded its pharmaceutical division during 2004. At present, Sanofi-Aventis, Eli Lilly, Novartis, Pfizer, GlaxoSmithKline, have established clinical research operations in India.

While the CRO market is fragmented with a number of small companies, reputed players have gained significant traction with over 50% CAGR over last three years. Global majors like Quintiles, PPD, Parexel, MDS and ICON have either set up their own operations in India or have partnered with local players. Larger Indian CROs are tying up with global majors to obtain relationships and expertise in project management e.g. Siro-Covance.
The Chinese pharmaceutical market is growing at an impressive double digit pace with a projected value of US$ 25 billion by 2008. The Chinese pharmaceutical market is highly fragmented with thousands of small pharmaceutical companies involved in manufacturing one or two generic drugs. Quality control and cost concerns are also present among the manufacturers in China. These led to increased supervision from the government to maintain the quality of the pharmaceutical products. Also, with the increased interference from the government, a gradual shift is happening from generic to innovation led development of contract research markets. This resulted in increased partnership with multinational pharmaceutical companies and other bodies. The inherent limiting conditions (with respect to IP concerns) prevalent in this country have curbed the Western firms from full capitalization on R&D potential. However, big pharma companies are increasingly interested in China. Roche has a US$11 million R&D center in Shanghai, one of five global R&D centers; also conducting genetic epidemiology studies on diabetes, Alzheimer’s etc. in collaboration with Chinese National Human Genome Centers. Eli Lily has a 100 people R&D center for chemistry services in Shanghai together with Shanghai ChemExplorer. Novo Nordisk has a R&D center in China, a first outside Denmark for molecular biology, protein chemistry and cell biology. It plans to grow from 20 to 60 scientists. GSK has established a Global Over The Counter (OTC) R&D center; GSK has invested US$2 million towards combinatorial chemistry R&D with the Shanghai Institute of Medical Materials (SIMM).

According to China’s Department of Drug Registration, demand for clinical trials in China has increased significantly. Applications for clinical trials increased by over 400% to 2,500 in the first half of 2003. Several new hospitals were added to the existing list of 165 hospitals permitted to conduct human clinical trials in China. However, a considerable proportion (47% in 2001) of the trials is for traditional Chinese medicines. The State Food and Drug Administration (SFDA) is taking steps to further increase the attractiveness of the Chinese trials market. Standard rules for conduct of trials were released in 2003 and 2004 and Good Clinical Practices (GCP) training was made compulsory in April 2004.

Ireland was the third most preferred location for SSO operations amongst the healthcare vertical. Pfizer, Takeda, Wyeth and GSK are some the major corporations to have set up SSO locations in Ireland.
4.6 Transportation & Logistics

One of the world’s largest industries, transportation & logistics covers a broad range of sectors ranging from automobiles, aircrafts, trains, transportation and logistics services as well as express delivery services.

The global automobile landscape is rapidly changing as demand grows for lower priced automotive components, spurring component suppliers to look to China for low-cost production. Along with that, soaring global demand for Asian cars that are enjoying a rapidly expanding customer base worldwide has resulted in mounting pressure on major American automakers to adopt cost saving measures and regain market share in the face of escalating domestic labor costs and intense competition from foreign-based firms. Faced with mounting costs, stringent labor laws, and unfavorable government regulations, some European car manufacturers also continue to generate dismal earnings.

The airline industry continues to be affected by staggering fuel prices, triggering increases in airfares by some airlines which, in turn, are intensifying already fierce competition between established airlines and discount carriers. With competition stiffer than ever, innovation is a vital ingredient for developing a sustainable competitive advantage.

Leading the innovation race are airlines in the Asia Pacific region, most of which have already deployed in-flight communication technology in an effort to grow their market share of premium customers, particularly itinerant business travelers. Conversely, despite paving the way for many of the technologies that are now being harnessed by airlines globally, highly leveraged North America carriers are putting the brakes on technology innovation to focus on streamlining operations.

Across all geographical regions, both established and budget airlines alike have mounted aggressive campaigns to reduce costs and ultimately, narrow the gap between the two airline segments as is evident from widespread investment in automated passenger facilities such as e-ticketing and self-service kiosks.

In the logistics service industry, consolidation is becoming a widespread practice as more and more logistics service providers begin to recognize the benefits that may be realized through mergers and acquisitions, principally economies of scale and skills.
India, Singapore and Malaysia are the top three locations with parts of Eastern Europe and Latin America, China and South Africa the top emerging locations for SSO in the transportation and logistics sector as. The comparison of the top locations is presented in Figure 4.6.

Figure 4.6 Transportation & Logistics: Evaluation of Top SSO Locations

While India attained the highest overall score, it also achieved the highest rating for cost efficiency and business environment conduciveness. On the other hand, Singapore earned the highest rating for quality of human capital. British Airways formed WNS Global Services in 1996 as a wholly owned captive business process outsourcing division in Mumbai, India. The UK carrier’s initial objective of setting up an outsourcing arm in India was primarily to support the airline’s back-office operations and manage ticketing. However, the completion of WNS’ IPO on the New York Stock Exchange a decade after its inception ended the airline’s equity relationship with its Indian offshore outsourcing.
unit. Today, British Airways continues to be WNS’s third largest client accounting for 12% of its revenues amounting to US$ 202.6 million in FY 2006. British Airways also awarded contracts for software development work to NIIT and Tata Consultancy Services in India which manage lower-level application development and programming.

FedEx’s financial services center in Singapore serves 14 markets and handles such transactions as invoices and collection for the package carrier’s operations across the entire region.

Although Jetstar’s call centers are currently based in Kuala Lumpur to serve the Asia Pacific market, the budget airline is also considering the Philippines for the provision of call center services. The top three locations have also emerged as attractive hubs for IT support and customer services.

Companies with finance and accounting, human resource, and call center functions carried out internally or outsourced to external organizations demonstrate a preference for locations that are situated near their source of business and/or markets. Air France’s finance and accounting functions are outsourced to external parties in France as well as Mexico and Peru, while Air New Zealand and Lockheed Martin’s human resource administration functions are performed at their corporate shared service centers in Auckland and various locations throughout the United States respectively.
4.7 Entertainment and Media

In considering the media and entertainment landscape, it is vital to take into account the prevailing trends that are evolving rapidly in diverse sectors spanning television and radio broadcasting, satellite and cable television, movie production, news and media agencies as well as information providers.

The onslaught of alternative delivery methods such as IPTV combined with the availability of video and music entertainment on multiple platforms, including mobile phones and iPods, are allowing for broader choice and greater control among consumers while perpetuating more intense competition between traditional and new media players.
For example, traditional cable and satellite television firms are contending with telecommunications companies offering triple play services – voice, television, and Internet services – to maintain their market share. Equally, traditional radio broadcasters are also struggling to maintain their listenership that is rapidly being undermined by satellite radio broadcasters; likewise, newspapers are also facing heated competition in maintaining readership as Internet-based news content proliferates.

As such, all sectors of media and entertainment are facing the burgeoning issue of maintaining control of content and audiences while harnessing the potential benefits of a growing number of innovative digital delivery venues that continue to fuel the market with more and more options.

The US, India and UK are the top three locations with Ireland the top emerging location for SSO in the media and entertainment sector. While the US attained the highest overall score, it also achieved the highest rating for quality of human capital. A close second, India surpassed other countries with respect to cost efficiency.

The formation of corporate shared services is proliferating across the media and entertainment sector in both the United Kingdom and United States, primarily to serve a number of key functional areas including finance, human resources and procurement. For instance, British Sky Broadcasting’s (BSkyB) human resources are carried out at their shared service center in England. Additionally, in what is referred to as “Project Forward”, The Nielsen Company has established corporate centers of excellence in numerous locations in the United States to manage selected processes for its global businesses. Along with the aforementioned processes, such centers also have overall responsibility over real estate and facilities management and outsourcing.

Broadcasting companies in the United Kingdom demonstrate a proclivity to maintain their customer support services and call centers within the country as is practiced by the BBC and Virgin Media, which has call centers operating in various locations including Glasgow, Manchester, and Teesside.

In the same way, cable and satellite television service providers in North America exhibit a similar inclination to keep their customer care services and call centers within the United States as is the case with Comcast and DirecTV.
Viewed as a prime location for IT services by numerous sectors, India is also regarded favorably by the media and entertainment sector as a preferred offshore destination for the outsourcing of IT support and services. The Nielsen Company started to outsource jobs at its marketing information division to India, primarily for data services.

Cablevision has strategic partnerships with Indian IT vendors, both to augment internal IT development capabilities and to help plan, design and implement new projects. Similarly, McGraw-Hill has developed a strong partnership with IT service providers in India, outsourcing a fair amount of code development work to various locations across the country.

IT aside, India has also grown in prominence as an offshore center for finance and accounting services. The BBC’s financial and accounting services are housed from a mix of locations not only in the United Kingdom, but also in India.

Not least, India is also gaining more and more impetus as a highly favored location for animation and content development outsourcing. Disney, Fox Entertainment, Lionsgate, NBC Universal and Sony Entertainment are just a handful of global entertainment outfits harnessing India’s 3D animation capabilities at fractionally lower costs.

A considerable amount of IT and non-IT related activities are also outsourced to or carried out at shared service centers across Ireland and Northern Ireland. The BBC’s human resources are currently outsourced to a third party in Northern Ireland, while some non-technology related activities of McGraw-Hill’s global businesses are managed centrally at the publisher’s shared service operations in Galway, Ireland.
5.0 Conclusion

Companies worldwide have been using Shared Services and Outsourcing to cut down on costs and streamline their processes in an effort to improve overall business and strengthen their market position. As the 2007 Frost & Sullivan study shows, MNCs across industry verticals are not just continuing but increasing their SSO efforts. The learning curve that built up in recent years by outsourcing and offshoring, mainly non-core, non-critical processes to low-cost countries such as China, India, Malaysia or Eastern Europe has increased companies' comfort-level and SSO might slowly gain a foothold in more core areas. While some industries like BFSI might never be able to use the full potential of SSO due to the stringent regulations they are facing and the risk to their reputation among customers; others, like Technology or Healthcare are exploring or already pursuing such opportunities. On the other side of the scale, more countries are exploring ways to tap into the lucrative SSO market to boost their economies by attracting world class companies. As a consequence, such countries will have to ensure that they do not just offer cheap labor but more value for money in terms of tying close knots with the industry to understand their needs and provide excellent SSO solutions to cater to them. This includes a strong effort to ensure that whatever processes or data is outsourced or offshored, is both safe and protected by IP regulations which are strictly enforced to provide a high level of comfort and security to companies.

There is no doubt that SSO will continue to be a key component of companies' efforts to grow and improve their business. With MNCs at the forefront of the SSO movement and more medium and small service providers offering outsourcing and offshoring services, SMEs are in the starting position to take SSO to the next level by jumping on the wagon that promises lucrative benefits.
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