Beyond BRIC

Offshoring in non-BRIC countries: Egypt – a new growth market

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Beyond BRIC: executive summary

1. This report has been commissioned as an independently researched report by Hill & Knowlton, who are acting for the Information Technology Industry Development Agency (ITIDA) of Egypt.

2. The work has been undertaken using the people, resources, knowledge and case studies of the Outsourcing Unit at the London School of Economics and Political Science (LSE), as well as independent interviews, analyst discussions, and research, both in Egypt and internationally. The Outsourcing Unit was invited to research the state of outsourcing in non-BRIC (Brazil, Russia, India, China) countries and to set Egypt within the context of these, with special reference to global outsourcing trends. It did this by:

- Comparing Egypt with 13 non-BRIC countries: Romania, Bulgaria, Poland, Slovakia, Czech Republic, Belarus, Morocco, Tunisia, Costa Rica, Mexico, Venezuela, Vietnam and the Philippines
- Using the Outsourcing Unit's longitudinal case database of 1,000 plus global sourcing IT, BPO and offshoring studies from 1993 to 2009
- Including a survey of 18 senior global sourcing analysts
- Interviewing 50 plus client organisations, suppliers and analysts experienced in global sourcing and expert in business and IT service location attractiveness (September 2008–January 2009).

    In chapters 4 and 5 of this report specifically, the analysis of Egypt's attractiveness in particular draws the following conclusions:

3. Egypt has become an outsourcing destination of choice for call centre work, and it is now seeking to extend this capability into back office, BPO, software development, and longer term into R&D. Despite its smaller size, it is hungry to join the BRIC country categorisation, and its current focus is aimed at achieving this. This report has found that Egypt:

- Offers one of the most attractive cost bases for outsourcing work
- Has scalability of high-quality technology graduate numbers, especially qualified in languages. This has made it attractive for call centre work
- Has started to address the environmental issues and has implemented new laws on copyright and intellectual property. It has also been cutting the bureaucracy for business and established a 'one stop shop'
- Has scored lower on infrastructure issues than some of its competitors, particularly due to its traffic problems and the incomplete ring road in Cairo. The government is establishing Smart Villages which are attractive for some companies and get around many of the infrastructure problems
- Is still perceived as a higher-risk destination than some other non-BRIC countries, due to its high inflation, plus a misplaced perception of its terrorism record

- Provides the highest market potential of any country studied in this report, due to:
– Its cultural fit with Western European countries
– Its strong language fluency and capability
– Its convenience for cost-effective 'nearshoring' for European business
– Its positioning as both a partner to other countries (e.g. India), and as a gateway to the Arabic world.

Responding to the challenges

4. All the non-BRIC countries studied are experiencing challenges, made more complex by the recessionary climate. Depth and range of investment in future location attractiveness is a key issue.

- Egypt is competing for its own good quality graduates and this position will become more severe as the market grows. The real sign of a mature market will be its capacity to convert its growing labour pools into ITO/BPO skilled staff and register high retention rates for senior staff. Ability to train, attract and retain good middle managers, which is currently a problem, will ensure ability to build on the foundations already established

- Egypt's government provides an attractive tax regime that helps keep start-up costs low and is key to attracting new international companies and investment. In Egypt, these policies are working, providing the government does not unilaterally reverse the trends based on tactical economic needs

- Egypt is making large strides with the development of its Smart Villages and this trend will overcome critical problems in the cities

- Egypt has taken a stand on introducing laws to protect intellectual property and copyright. Its ability to police and enforce these laws is being monitored by businesses as some start to establish new innovation and R&D labs in the country

- Egypt has an opportunity to position itself as a nearshore country of choice, providing it can maintain the momentum of infrastructure upgrades

- Egypt has adopted an approach of partnering and cooperation that means it may be able to leverage its strengths and open up new markets with third parties

- Egypt can offer a good base for captives and, as the market matures, it will be possible to harness more local companies to work with these overseas units more effectively.

5. Offshoring and outsourcing will retain their criticality through recessionary as well as growth periods. A highly competitive global services market presents opportunities and revenues for non-BRIC countries able to offer the right mix of strong cost, reliable service, and secure location(s).

Beyond BRIC

Offshoring in non-BRIC countries:
Egypt – a new growth market

1. Introduction

The global offshore outsourcing market for IT and business services exceeded $55 billion USD[1] in 2008 and some estimates suggest an annual growth rate of 20% over the next five years. In 2008, India posted some 65% of the ITO and 43% of the BPO market.[2] It is common to talk of Brazil, Russia, India, and China as the BRIC inheritors of globalisation, offering both offshore IT and back-office services, and also, with their vast populations and developing economies, huge potential markets. Indeed, in 2008 India exported $40 billion of such services, while China, Russia, and Brazil managed $5 billion, $3.65 billion, and $800 million respectively. However, by 2009 there were over 120 other active offshore locations offering IT and business process services or captive locations for these. All were looking for new business. Moreover, the BRIC countries are not without their problems, with Brazil and China hardly leveraging their potential. Russia lacks government support and is being led into high-value but niche work, while India and China may even be seen turning to non-BRIC locations for some of the solutions; for example, to secure low cost and labour availability.

All this raises the question: to what extent are non-BRIC countries also potential inheritors of globalisation? This report was commissioned by ITIDA to provide an assessment of the emergence of non-BRIC countries, and their competitiveness, with specific reference to the positioning of Egypt within this group. In order to fulfil this mandate, first the long-term context and trends are set out, through which these countries are emerging as IT and business service 'hot spots'. Then 11 major global sourcing trends and seven pressures are identified that will develop over the next five years, and the implications are assessed of how non-BRIC countries can ride these waves of change. Next, the main active non-BRIC countries fall into four regions, namely Central and Eastern Europe, the African Mediterranean, the Americas, and Asia Pacific. A representative sample of 14 countries provides the focus for comparison of their competitiveness based on 20 criteria organised into six major areas: cost, availability of skills, environment, quality of infrastructure, risk profile, and market potential. Finally, the report turns a more searching spotlight on one non-BRIC country, Egypt, to assess its current positioning, the future path it can take, and the challenges it faces as well as actions needed to get there.

[1] All financial figures are in US Dollars unless otherwise stated.

[2] Willcocks and Lacity (2009) *The Practice of Outsourcing: From ITO to BPO and Offshoring* (Palgrave, London forthcoming). The figure is bavsed on various sources and reflects the more conservative of the estimates given.

2. The non-BRIC context: global sourcing trends 2009–2014

Background

This research points to the fact that the relative attractiveness of BRIC and non-BRIC countries as offshore, outsourcing and business locations is highly dynamic. The evolving attractiveness needs to be understood in the context of the major five-year global sourcing trends and pressures identified in this research. In order to contextualise the findings on the 14 non-BRIC countries selected for comparison (Egypt, Romania, Bulgaria, Poland, Slovakia, Czech Republic, Belarus, Morocco, Tunisia, Costa Rica, Mexico, Venezuela, Vietnam, and the Philippines), and to take a forward look and make recommendations, the major trends and pressures operating in the global sourcing arena are identified and explained.

Specific research was undertaken between September 2008 and January 2009 into 56 organisations, and the findings were combined with evidence from the LSE Outsourcing Unit's case database, which has studies from more than 1,000 organisations. The analysis points to 11 major trends shaping global sourcing, and so impacting non-BRIC activity over the next five years, then draws upon the most recent research and details how the global economic downturn will have mixed but deep impacts on these trends.[3] The implications of each trend are identified for non-BRIC countries, together with their attractiveness and possible responses over the next five years.

2.1. Trend 1: the rising spend on outsourcing markets – BPO will overtake ITO within five years

This study found that the global ITO market has increased each year since 1992. Back in 1989, global ITO was a $9–$12 billion market.[4] In 2008, the global ITO market was estimated to be worth between $220 and $250 billion. The BPO market in 2008 was less than the ITO market, but grew at a faster rate. Based on the evidence, the estimate for the ITO market, over the next five years, is that it will grow by 6–9% per annum while mainstream BPO expenditure is likely to grow worldwide by 10% to 15% a year, from $140 billion in 2005 to potentially $230 billion plus by 2013. BPO expenditure will be in areas such as the human resource function, procurement, back-office administration, call centres, legal, finance and accounting, customer-facing operations, and asset management.[5]

There have been some high-profile backsourcing cases (returning services in-house) in recent years; for example, The Bank of Scotland (2002), JP Morgan Chase (2004) and Sainsbury (2005). Although media-worthy, these cases have never represented a dominant trend towards backsourcing. Based on the 2008–09 case studies and surveys, **the most popular course of action at the end of a contract will continue to be contract renewal with the incumbent supplier.** The research suggests that a quarter will be re-tendered and awarded to new suppliers, and only a tenth back-sourced.

Non-BRIC implications: Offshoring and outsourcing will retain their criticality through recessionary as well as growth periods. A highly competitive global services market presents opportunities and revenues for those able to offer the right mix of strong cost, reliable service, and secure location(s).

2.2. Trend 2: the growth of multi-sourcing

Although ITO and BPO spend is increasing, the average size of individual contracts and the duration of contracts is decreasing.[6] How can the smaller, shorter deals be reconciled with an overall increase in the ITO/BPO markets? The figures suggest that client organisations are actively pursuing more multi-sourcing. Multi-sourcing has always been the dominant practice and the overall growth is driven by client organisations signing more contracts with more suppliers. However, while multi-sourcing helps clients to access best-of-breed suppliers and mitigates the risks of reliance on a single supplier, it also increases transaction costs for managing more suppliers. Multi-sourcing also means that suppliers incur more transaction costs – suppliers must bid more frequently because contracts are shorter, suppliers face more competition because smaller-sized deals mean that more suppliers qualify to bid, and suppliers need to attract more customers in order to meet growth targets. One sub-trend emerging is that clients attempt to streamline their supplier base while retaining the competitive and supply advantages of multi-sourcing.

Non-BRIC implications: Multi-sourcing strategies and shorter contracts offer regular opportunities for offshore locations and services to establish footholds with clients. Where clients move to a primary contractor model, the leading supplier may well draw upon attractive offshore locations and services in a way that the client might not choose to do if directly responsible for all suppliers.

2.3. Trend 3: India's changing role

There is considerable evidence in the case studies that US and European clients initially engaged Indian suppliers to provide technical services such as programming and platform upgrades. As these relationships matured, US clients assigned more challenging work to Indian suppliers. For example, a US retailer first engaged its Indian supplier to help with Y2K compliance. As the relationship matured, the retailer assigned development and support tasks for critical business applications to the supplier. This retailer and other satisfied clients said, "We went to India for lower costs, but we stayed for quality."[7] The supplier executives from three of the largest Indian suppliers all mentioned their wish to assume higher-value tasks for their clients; for example, research and development, and knowledge process outsourcing.

However India, and to a lesser extent China, Brazil and Russia are already experiencing upward pressure on wages, combined with rising, sometimes high, labour turnover rates; what has been called the 'war for talent' is escalating in BRIC countries. For example, both India and China are increasing their own offshoring of IT and BPO work to other countries.

Non-BRIC implications: This trend opens up the market for non-BRIC lower-cost services as a stepping stone to evolving into higher-value work. At the same time, some non-BRIC countries will already be competing with India on higher-level skills and resources, thus offering alternative higher-skilled locations, often with less wage and labour turnover pressures.

[6] For example, the Everest Group found that among the ITO contracts signed in 1998, 24% of contracts were worth more than $400 million and 33% of contracts were worth between $50 and $100 million. In 2005, only 11% of contracts were worth more than $400 million and 57% of contracts were worth between $50 and $100 million. Concerning contract duration, the Everest Group found that 37% of contracts signed in 1998 were more than nine years in duration compared with 18% in 2005 (source: Tisnovsky (2006) *IT Outsourcing in SME Businesses*, White Paper, Everest Research Institute).

[7] Willcocks and Lacity (2009) op. cit.; Lacity and Rottman (2008) *The Offshore Outsourcing of IT Work* (Palgrave, London).

2.4. Trend 4: China's promise

In 2006, China invested $142.3 billion in its ITO and BPO markets, specifically in information and communication technologies (ICT), to secure its global position in the offshore services market. China's long-term ITO/BPO future is expected to be strong. For example, the Everest Group estimated that the Chinese offshore services market was only $2 billion in 2006, but it predicts that China's market will grow 38% annually to reach $7 billion by 2010.[8] So far, the main ITO/BPO suppliers in China are either large US-based suppliers such as Accenture, Cap Gemini, Dell, EDS, HP and IBM, or large Indian-based suppliers such as Genpact, Infosys, and TCS. Neither Indian nor Chinese suppliers want to compete solely on low-level technical skills. Chinese suppliers are trying to show they can fill the needs for product development, systems design, and consulting services.

Despite the optimism, many client organisations are wary of China's ITO and BPO services. Language barriers, cultural barriers, and fears over losing intellectual property remain significant obstacles for many companies in North America and Western Europe. The Chinese government and Chinese business sectors are well aware of these barriers and are actively seeking ways to address them. For example, the Chinese government is investing $5 billion in English language training to target the ITO/BPO markets.

Non-BRIC implications: Non-BRIC locations can compete against China by differentiating their offerings, where China continues to be perceived as relatively weak. At the same time non-BRIC locations and services, especially those in the Asia Pacific region, are attractive to Chinese firms as clients.

2.5. Trend 5: emerging country competition

In addition to India and China, suppliers from all continents will develop centres of excellence. Many US clients already use Central American suppliers for Spanish-speaking business processes such as help desks, patient scheduling, and data entry. Synchronous time zones are another favourable factor for US firms looking to source in Central or South America. Brazil in particular has the advantages of a large population, innovative creativity of its engineers and government programmes supporting the outsourcing industry, while Chile and Uruguay, for example, have promoted their time zone advantages, back-office proficiencies and government incentives to attract outsourcing work.[9]

[8] Lacity and Rottman (2008) op. cit.; Bahl, Arora and Gupta (2007) *What's happening in China*, Everest Group.

[9] Brown-Wilson Group Inc. (2008) *The Black Book of Outsourcing: State of the Outsourcing Industry 2007*. www. theblackbookofoutsourcing.com

In Western Europe, organisations will increasingly outsource IT and business services to providers located in Central and Eastern Europe. For example, the Visegrad-Four Countries (Czech Republic, Hungary, Poland, and Slovakia) offer Western European firms closer proximity, less time zone differences, and lower transaction costs than Asian alternatives. Within these countries there is some movement of outsourcing work to lower-cost cities (a trend noticeable in many countries, including, for example, India, China, and rural sourcing in the USA). By the end of 2008, the Central and Eastern European ITO market exceeded $3.5 billion, with Russia also exporting over $3.6 billion of IT and business services.[10] In sub-Saharan Africa, several countries are actively seeking to become players in the global ITO and BPO markets and building their economies partly on IT; for example, Botswana and Kenya.[11] South Africa is exporting IT and BP services, primarily to UK-based clients. South Africa appeals primarily to UK-based clients because of the similar time zone, cultural similarities, English-speaking capabilities, and good infrastructure. Mediterranean North Africa already exports IT services to Europe. For example, one interesting study examined five Moroccan IT suppliers that provide services to clients in France. A common language, similar time zone, and cultural capability make Morocco an attractive destination for French organisations.[12] Meanwhile, India and China are already offshoring IT and business services to cheaper non-BRIC locations.

Non-BRIC implications: As overseas client companies and suppliers become more knowledgeable, non-BRIC locations have multiple opportunities to build and communicate their attractiveness as business and service locations in the six vital areas covered by this report: cost, availability of skills, environment, quality of infrastructure, risk profile, and market potential. In many cases they will need active government support to do so.

The trend may well be regionally rather than predominantly globally based for non-BRIC locations, and may be combined with a strong nearshore component. On a broad pattern non-BRIC locations in Central and Eastern Europe and Mediterranean Africa will be attractive to Western Europe and Gulf States, those in Asia Pacific to China, India and Japan, and those in Central and South America to North America. Meanwhile shared language, culture and/or history will continue to influence purchasing decisions (e.g. France to Northern Africa, UK to South Africa, USA to the Philippines). Clearly also the BRIC countries themselves are increasingly interested in non-BRIC services and locations.

[10] Equaterra (2009) *Pros and Cons of Offshore Locales.* Presentation for CIO Insight 2008.

[11] Brown-Wilson Group Inc. (2008) op.cit.

[12] Bruno, Esposito, Iandoli and Raffa (2004) The ICT service industry in North Africa and role of partnerships in Morocco. *Journal of Global Information Technology Management,* 7(3), pp.5–26.

2.6. Trend 6: a second look at 'software as a service'

When the book *Netsourcing* was published in 2002, it was noted that many large companies were not interested in renting applications, services and infrastructure over networks. This was because they already had ASP product offerings and expertise in-house, and they wanted customised services and to source to stable providers, not risky start-up ventures.[13] Many thought that ASP died with the dotcom bust but there are several reasons to believe that large organisations will reconsider ASP for targeted activities, not least as it evolves into software as a service (SAAS). First, large organisations will want net-native applications (proprietary applications designed and delivered specifically for Internet delivery) that are only available through ASP delivery (e.g. Salesforce.com). Second, large organisations may finally be ready to abandon their expensive proprietary suites for cheaper ASP alternatives. Third, ASP providers got the message: clients want customised services, even if the products are standardised. The need for customised services actually increases the service providers' viability because they can generate profits by charging for value-added services. By 2008, the market for ASP-type services was over $4 billion.[14]

Non-BRIC implications: The ASP market looks unpromising in the short term for many non-BRIC locations, but the opportunity lies in building high-quality and reliable technology infrastructure required to host and deliver such services. In the longer term, there is a trend, however, towards this technology facilitated service, which non-BRIC countries need to look at carefully as a potential investment area.

2.7. Trend 7: outsourcing helps insourcing… up to a point

As organisations become smarter at outsourcing, they also become smarter at insourcing. In-house operations are facing real competition in nearly every area and can no longer assume they will retain their monopoly status with the organisation. As a result, in-house operations are adopting the techniques of the market. However, insourcing will be impeded by a shortage of talent within developed countries, particularly for IT skills. The USA is not alone in this. Nearly every research report suggests that other developed countries will suffer a shortage of domestic IT workers within the next five to ten years. For example, research found that the UK will experience a shortage of 714,000 IT workers by 2010. More generally, the USA is projected to be short of 17 million skilled workers by 2025 (comparative shortages are France, Spain and Germany each with 3 million, and Italy and UK 2 million short).[15] The shortages in developed countries, especially within the USA and Western Europe, will be caused by the gap between a strong demand for domestic IT workers and a dwindling supply of domestic IT workers due to the lingering effects of declining educational enrolments today and future effects of 'baby boomers' retiring from IT.

However, while many reports point to the huge numbers theoretically available as part of a globalised workforce, there are critical shortages of skills in organised labour everywhere, including increasingly in the BRIC countries as the most obvious targets so far for offshoring IT and business service work.[16]

[13] Kern, Lacity and Willcocks (2002) *Netsourcing: Renting Business Applications and Services over a Network* (Prentice Hall, New Jersey).

[14] Willcocks and Lacity (2009) op. cit.

[15] Aggarwal and Pandey (2004) *Offshoring of IT Services – Present and Future* (Evalueserve, New Delhi); Cheese, Thomas and Graig (2008) *The Talent Powered Organisation* (Kogan Page, London).

[16] Farrell (2006) Smarter Offshoring. *Harvard Business Review*, June, pp.84–93; Cheese et al. (2008) op. cit.; Kobayashi-Hillary (ed.) (2008) *Building A Future With BRICs.* (Springer, Berlin).

Non-BRIC implications: These IT and skilled labour shortages in both client and supplier companies in Western Europe, North America and Brazil, Russia, India and China, represent both real opportunity and a set of strong challenges to non-BRIC countries eager to develop their attractiveness as business and service locations. They point to the need for long-term strategy and investment in education and training, together with attractive employment conditions to draw in and retain skilled labour.

2.8. Trend 8: nearshoring – a strong trend

'Nearshoring' is defined as outsourcing work to a supplier located in a lower-wage foreign country close in distance and/or time zone. Compared with offshore outsourcing, the benefits of nearshoring include less travel costs, less time zone differences, and closer cultural compatibility. Canada, for example, is a significant nearshore destination for US clients, and indeed some analysts argue that US clients can have lower total costs with nearshoring to Canada than with offshoring to India. In their study of nearshoring, Erran Carmel and Pamela Abbott argue convincingly that distance still matters, and point to customers choosing the nearshore option to gain benefit from one or more of the following constructs of proximity: geographic, temporal, cultural, linguistic, economic, political, and historical linkages.[17] Their study identifies three major global 'nearshore clusters' based around clients in a) North America, b) Western Europe, and c) a smaller cluster in East Asia.

Thus, as one example, the Czech Republic, Poland, and Hungary are significant nearshore destinations for Western Europe. According to a 2006 report by Deutsche Bank Research, imports of IT-based services from Central and Eastern Europe to Western Europe increased an average of 13% per year between 1992 and 2004. This growth rate is nearly comparable to the import of IT services from India, which averaged 14% per year over the same time period. Clients in Western Europe are attracted to Central and Eastern European suppliers for many of the same reasons that the USA is attracted to Canadian suppliers: common language, cultural understanding, minimal time zone differences, and low labour costs. However, Central and Eastern Europe may be more attractive for BPO than ITO because these countries provide excellent general education, but have not graduated IT students at anything near the pace of India. For that reason, IDC has predicted that Western Europe's growth in BPO will increase annually by 14.6% compared with 7.2% for ITO.

However, in addition to this continuing nearshoring trend, there is also what can be called a long-run 'bestshoring' one. The model is exemplified by the five-year contract between India-based Tata Consulting Services and ABN Amro bank which started in 2005. Here Tata Consulting Services provides IT services to ABN Amro offshore (India, Sao Paulo), nearshore (Budapest, Luxembourg) and onshore (Amsterdam). An increasing number of clients and suppliers are moving to such a model for either insourced or outsourced IT and business services.[18]

[17] Carmel and Abbott (2007) Why 'Nearshore' Means That Distance Still Matters. *Communications of the ACM*, 50(10), pp.40–46.

[18] Oshri, Kotlarsky and Willcocks (2007) IT Offshore Outsourcing: Supplier Lessons on The Management of Expertise. *MISQ Executive*, 6 (2), pp.53–65.

Non-BRIC implications: Non-BRIC locations can profit from nearshoring advantages in their specific regional cluster, differentiating themselves from farshore suppliers on proximity criteria, while differentiating themselves from other nearshore contenders on a suitable mix of superior cost, skill availability, quality of infrastructure, government support, and risk profile. At the same time non-BRIC providers of services and location need to be alert to bestshoring strategies of foreign clients and suppliers alike.

2.9 Trend 9: knowledge process outsourcing is increasing

Knowledge process outsourcing (KPO) is the outsourcing of business, market, and/or industry research. KPO requires a significant amount of domain knowledge and analytical skills. KPO suppliers design surveys, collect new data, mine existing data, statistically analyse data, and write reports. Although the KPO market was, in 2008, quite small, industry analysts expected a huge growth in this sector over the next five years. Evalueserve estimated that the KPO market in 2007 was $3.05 billion and would grow annually by 39%. It expected the KPO market to be $16 billion by 2010 or 2011, employing approximately 350,000 professionals globally.

The increase in KPO is directly related to our observation that offshore suppliers are moving up the value chain. As client–supplier relationships mature, suppliers have gained an enormous amount of knowledge about the client's business domain as well as the expertise to find, analyse, and report on domain knowledge. US, Canadian, and UK clients value this deep knowledge and will pay Indian suppliers $20 to $100 per hour for KPO services, compared with onshore rates of $80 to $500 per hour. By 2009 offshore suppliers were struggling to find enough workers with advanced degrees to fill the demand. But it is anticipated that, once employees are hired, labour turnover in this space will be lower because professionals finally have the client-facing and intellectually challenging work they did not find in lower-level offshoring programming.

Non-BRIC implications: KPO should be an ambition for non-BRIC locations in terms of moving offshoring and outsourcing work up the value chain, and in terms of differentiation and finding profitable market niches. Similarities in areas such as language, culture, and legal and regulatory frameworks can make a location more attractive to specific clients, suggesting a high level of granularity is needed in identifying the right client and knowledge work to invest in.

2.10. Trend 10: captives – building and selling

While it is widely recognised that Western companies are setting up sites offshore, there is also an emerging trend that might be called 'The GE Effect'. General Electric may not have been the first US footprint in India, but certainly Jack Welch's enthusiasm for India made it acceptable for other CEOs to locate back offices in India. GE established GECIS (GE Capital International Services) as a captive centre in India, in 1997. In the winter of 2004, GE sold off 60% of GECIS to two equity companies, Oak Hill Capital Partners and General Atlantic Partners. A year later, the name was changed to Genpact, which is now one of the top 10 BPO/ITO suppliers in India. Some have called GE's approach "the virtual captive centre" because GE still maintains primary equity holding.[19] With a virtual captive centre, the company owns the physical operations, but the staff are employed by a third-party supplier. Presumably the virtual captive centre offers the best of both worlds – the client investor still maintains strategic control but the supplier is better equipped to attract, develop, and retain local talent.

There are several examples of US-based organisations selling their captive centres. Beyond the anecdotes, the Black Book of Outsourcing 2007 survey of 18,272 buyers found that selling captive centres may indeed be a significant trend.[20] Among the survey respondents were 487 companies with captive centres in India and the Philippines. The survey found that 29% of these companies were actively seeking to sell out or already had an existing strategy in place. Respondents from large organisations were more likely to investigate a sell out than mid-sized businesses. The main reasons for selling captive centres were:

1. Captive centre was built to protect data and intellectual property which is no longer viewed as a threat if provided by a third-party supplier
2. Senior executives are no longer committed to captive centres
3. It is no longer necessary to keep decision-making authority in-house
4. Third parties are now able to handle complex processes.

There is a difference between the ITO and BPO captive centres: companies are much more likely to erect a captive centre for BPO than ITO. The differences are attributed to the higher maturity of Indian and offshore IT services compared to BPO, as well as the client view that BPO services are more critical to operations.

Non-BRIC implications: Country attractiveness can be defined by the skills, and costs, but in special situations is also defined by the opportunities to create captives. The 'captive' strategy of foreign client and supplier companies needs to be carefully analysed, but may well provide real opportunities for a non-BRIC location, especially where BRIC locations may be increasingly less attractive for captive centres.

[19] Aggarwal (2007) *Person-to-Person Offshoring*, Evalueserve Report; Lacity and Rottman (2008) op. cit.

[20] No details available for 2008.

2.11. Trend 11: outsourcing successes and disappointments

Outsourcing will continue to be a high-risk practice with significant hidden costs for some organisations. Such organisations will be characterised by:

• Painfully slow learning
• Low margins for suppliers
• Lack of client strategy
• Lax approaches to configuring, writing contracts, monitoring and managing the deals effectively
• Overpromising from suppliers who under-deliver
• Additional complexity provided by the global offshoring and outsourcing process.

Extrapolating from the Outsourcing Unit case database evidence, it is estimated that over the next five years some 70% of selective sourcing deals will be considered relatively successful. Typically, clients will be spending anything between 15 and 58% of their operating budgets on outsourcing, usually to several, sometimes multiple, suppliers. In contrast, it is estimated that only 40% of large-scale deals involving complex processes that represent more than 80% of the operating budgets will be successful, 30% will have mixed outcomes and 30% will be seen as failures. Ironically, the client organisations with the messiest back offices will benefit the most from total outsourcing – if they can successfully manage the outsourcing life cycle. In contrast, companies that successfully clean up their back offices prior to outsourcing leave much fewer opportunities for suppliers to add value.

Non-BRIC implications: Offshoring and offshore outsourcing add additional, distinctive risk dimensions for a client company to consider. Non-BRIC countries need to mitigate and offset those risks as much as possible, while demonstrating superior location, cost and service benefits.

2.12. The impact of the 2008–2011 global economic downturn

The global economic downturn will have mixed but deep impacts on the trends identified and discussed above. By early 2009 there was evidence of client behaviours exhibited in previous economic downturns. These included:

• Deferring project decisions
• Consolidating vendor relationships
• Delaying making decisions to commit to new contracts
• Negotiating down rates in current contracts
• Looking for dramatic cost savings, for example:
– In new contracts, reducing the number of suppliers used
– Cutting down on the use of outsourcing contractors
– Contracting to offshore destinations for cheaper captive outsourced services
– Cutting the amount of work carried out in existing deals
– Clients looking for better and longer-term financing and asset transfer deals as part of their outsourcing arrangements.

All this means suppliers will need to be sharper than ever in cost control, standardisation, financial planning and innovation, both for themselves and clients. IT and BPO service companies will exploit global delivery resources to achieve cheapness, scalability, and flexibility. Suppliers will also need to be inventive with how they add value in contracts. This could be by managing sub-outsourcing contracts, helping to introduce innovation or offering some financial terms that are attractive.

Of course, if the downturn deepens, an increasing number of deals will get cancelled where clients cease to exist, or where mergers and acquisitions change requirements, or bring other rival extant suppliers into play. Past recessions have seen IT managed in a variety of ways.[21] At the beginning of a downturn, some organisations take drastic, short-term measures to cut costs and headcount, and put existing and new projects on hold. Others continue to invest in their long-term strategy, though sometimes doing this at a slower rate. As a recession deepens more clients are pressurised into short-term cost-cutting behaviours, including outsourcing contracts and supplier relationships.

At the same time, the ongoing trend of reducing the number of vendor relationships and streamlining internal processes and management has been accelerated by the economic downturn. It is likely that the 2008/09 global economic downturn will deepen and turn into recession in many key economies – some analysts think the economy will start to grow positively around late 2010. Interestingly, in the 2001/03 downturn, in response to cost pressures, corporations turned increasingly to offshoring. In the present climate there are likely to be a mix of demand and supply pressures that will shape offshoring strategies (see below).

Non-BRIC implications: The research conducted indicates that the offshoring and outsourcing markets will remain dynamic, both for BRIC and non-BRIC destinations. Where will pressure for this dynamism come from? The research indicates key pressure points, which are shown in Figure 1.

[21] See Lacity and Willcocks (2001) Global IT Outsourcing: *Search For Business Advantage* (Wiley, Chichester) and Willcocks and Lacity (2006) op. cit. for detailed case studies.

Figure 1– Key pressures in global offshore/outsourcing markets 2009–2014 (source: LSE Outsourcing Unit analysis, 2009)

Where will the dynamism come from? Seven pressure points

Pressure 1:

Large Indian players moving up the value chain, bestshoring, acquiring, moving into new sectors. Recession makes acquisitions likely.

Pressure 2:

Large players offering 'multi-tower' – IT, HR, procurement, finance, administration.

Pressure 3:

Client pressure toward multiple suppliers that are better managed and bound in.

Pressure 4:

Developing outsourcing services in many countries – alternative, improving supply from over 120 increasingly ambitious centres around the world.

Pressure 5:

World economic and business pressures exert continuing downward pressures on costs, but also innovation, exacerbated by recession 2008–10.

Pressure 6:

Managing the sub-contracting… and its hidden costs.

Pressure 7:

Unending search for a) new sources of skill b) better labour models c) at more attractive prices.

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Each of these pressures presents considerable challenges to non-BRIC countries looking to develop their attractiveness as global IT and business service locations. The key for them is to develop their strategy around the sources of attractiveness documented in the next chapter.

3. Country attractiveness –
key factors and assessment

Background

There has been much prior work on identifying the key factors that create an attractive destination for the outsourcing and offshoring of IT and business services.[22] The present research has uncovered additional factors, identifying a total of 20 that are salient. Farrell (2006) is useful in providing a classification that can be utilised to bring all these factors together. She suggests six broad areas, namely:[23] cost, skills, quality of infrastructure, risk profiles, business and living environment, and market potential.[24] In this chapter, these factors are used to assess the relative attractiveness of Egypt against 13 other representative non-BRIC countries also establishing themselves as outsourcing destinations of choice.

Setting aside the BRIC countries, Canada and Ireland, leading analysts place Egypt in the second or third tier of outsourcing destinations.[25] In the present study, 13 other countries which appear regularly in reports on second and third tier destinations are included.[26] These are Central and Eastern Europe (CEE), represented by Romania, Bulgaria, Poland, Slovakia, Czech Republic and Belarus; the African Mediterranean represented by Morocco and Tunisia; the Americas represented by Costa Rica, Mexico and Venezuela; and Asia Pacific represented by Vietnam and the Philippines. These countries are increasingly trying to attract overseas companies – especially those from Western Europe and North America – by offering both a range of outsourcing services, and resources for setting up offshore facilities (captive centres of various types and delivery centres) at competitive costs.

The 21st century development phenomenon of global offshoring and outsourcing of IT and business services raises the question of why these particular countries have become attractive, and more specifically – why now? The answer is multi-dimensional, but one dominating factor is the introduction of a period of stability politically and, for many, economically as well. Stability has meant that the twin benefits of highly skilled graduates plus low cost bases have persuaded many non-BRIC countries to re-evaluate their own positioning and the new market potential. In CEE those countries accepted into the European Union (EU) have been pressurised to change their government, legal and economic structures, and increasingly to integrate these with EU practices. Their universal and comprehensive education systems have accelerated the release of highly skilled graduates and expanded the market for new industries. Similar developments in previously war-torn or divided countries such as Vietnam and the Philippines have led to a new energy and business drive to attract inward investment and encourage further commercial expansion. Ahmed Naguib, Head of Egypt Major Service Centre, established by Orange, summarised the reason for Egypt's attractiveness as follows:

"We are a bridge between Europe, Middle East, and Africa and Asia. We are, if you wish a leader in the area for Arab leads... based on what you may call the offshore concept... we have the ability to do more with less. This means we are a low cost operation, but also have high productivity."

[22] See for example, Minevich and Richter (2005) *Global Outsourcing Report 2005* (Going Global Ventures, New York); Equaterra (2008) *Pros and Cons of Offshore Locales*, CIOInsight.com; Marson and Blodgett (2008) *Can Middle Eastern Countries Fulfill the 'Eastern' Promise?* (Yankee Group, New York); Business Monitor (2008) *The Egypt Business Forecast Report Q1 2009* (Business Monitor International, New York); Dutta and Mai (2008) *The Global Information Technology Report 2007–8* (Palgrave, London).

[23] Farrell (2006) op. cit.

[24] The present study uses these broad headings but details additional factors not included in Farrell (2006) op. cit. This is especially the case for factors under the 'market potential' heading.

[25] For example, Hodges (2008) BPO: *State of The Industry.* Presentation at the European Outsourcing Association (June); Marriot (2007) *Gartner's 30 Leading Locations for Offshore Services* (Gartner Group, Stamford).

[26] For example, Marriot (2007) op. cit.; Dutta and Mai (2008) op. cit.; Business Monitor (2008) op. cit.

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This view is held by many other companies seeking to set up or expand their Egyptian operations. Geographical positioning continues to be a key factor even in a globalising, offshoring world, but is also critical to the attractiveness of all 14 countries.[27]

3.1. Factor one: costs
Companies considering outsourcing IT or business processes typically compare a range of costs including:

- Labour costs (average wages for skilled workers and managers)
- Infrastructure costs (unit costs for telecom networks, Internet access and power, office rent)
- Corporate taxes (tax breaks and regulations, and other incentives for local investment) across potential outsourcing locations. In addition, they are now also looking at value-added dimensions for how they might benefit over time.

The 14 countries investigated show a wide range of salary scales, with the highest being in CEE. Even within CEE there is differentiation with, for example, lower salaries in Slovakia than in Poland and Czech Republic, although all of them are still significantly lower than in the rest of the EU. This situation is, however, beginning to change as the markets change, skill bases grow and the countries become more established within the EU. As a result, costs within these countries are growing more quickly than in Asia. A contributing factor is that property prices in CEE vary significantly; in some places, for example in Prague, monthly rent is on a par with any other Western European city. Typically, rents in the high-tech business parks located in close proximity to other capitals and major cities are significantly higher than in the more remote business parks. Cost rises, competition and access to skills are putting pressure on central city locations and gradually more secondary locations are emerging in CEE countries (e.g. Katowice, Poznan, Wrocław), which have lower property costs, but are also close to or have major universities, thus ensuring the supply of skilled graduates.

Labour costs in Morocco are higher than in Tunisia and Egypt but lower than in CEE and about half the costs of white-collar employees in its major market of France. In Tunisia, operation costs are about 20% lower than in Morocco. In Egypt wages are about half of those in Morocco, and property prices for offices in business parks (called 'Smart Villages') are significantly lower than in CEE while being on a par with those in Asia (e.g. the Philippines). For example, an office rents costs comparison shows Egypt as offering a favourable benefit: (square metre costs: Egypt $180, India $220, Philippines $184, Bulgaria $239).[28]

In Asia labour costs are lower than in all other countries compared, Vietnam being the cheapest (wages are half or less than the average wages of Indian developers). In the Philippines, labour costs are slightly higher than in Vietnam, but travel costs from North America are relatively low, which may make overall costs very similar to those of Vietnam.

[27] Marson and Blodgett (2008) op. cit. suggest the top selection criteria for outsourcing location are: focus on quality, followed by labour costs, linguistic skills, good international communications skills, and open/competitive ICT environment. Other studies cite different rankings of factors, but all tend to make the overall point that, by 2008, lower costs are a necessary but insufficient determinant of offshore and outsourcing choices.

[28] A T Kearney (2007) *Global Service Location Attractiveness Index* (AT Kearney, New York).

The costs of telecommunications infrastructure and Internet are relatively low in all countries investigated, with the exception of Vietnam which has state-owned monopolies to control Internet access. In fact, this keeps the costs artificially high. International phone lines in Vietnam are among the most expensive in the world. In the Philippines, deregulation of local communications pushed down bandwidth costs by 40%. In Egypt costs of power, telecommunications and Internet are amongst the lowest; lower even than in CEE and Asia. For example, this is shown in the telecommunication costs comparison: Egypt $4.97/20 hours; India $6.78/20 hours; Bulgaria $7.32/20 hours.

Governments support their native offshore and outsourcing industries by becoming actively involved in creating jobs and improving the domestic economy. Many governments are seeking to attract foreign companies to establish business units or subsidiaries and use local suppliers. Apart from Poland, where incentives are not as high, most CEE countries offer preferential tax policies and support for investment. More investment incentives have been introduced recently in Bulgaria and Slovakia. The Slovak government, for example, has introduced a new act on investment aid, allowing grants and income tax relief for IT and shared services centres in the country. The Romanian government is trying to attract and retain IT talent by exempting IT professionals from income tax payment.

Currently, some governments, in the 14 countries investigated, offer higher incentives than do CEE countries. Some provide complete tax exemption (thus, the Philippines offers a 4–8-year 'income tax holiday', Tunisia offers tax exemptions on the export of IT-enabled services, Morocco offers full exemption for five years and 50% reduction in the future). The Egyptian government is offering incentives in order to establish clustered groupings in a range of new business parks (Smart Villages). One new development, Maadi Park, currently under construction, will focus on the call centre and business process of outsourcing lines of businesses. It is planned to address the needs of what are called high-audio (call centres), low-margin businesses and will house 50,000 employees in over 40 buildings and 2 million square feet (0.19 million square metres) of prime real estate in downtown Cairo, with metro rail connectivity. Other villages are planned in Alexandria, Mansura and Assiut. The relatively low cost base, linked to government subsidies for moving to either free zones or to Smart Villages, are a strong factor attracting companies to Egypt.

Summary point: Active government support and attractive tax incentives to help keep start-up costs low are key to encouraging more companies to become based in any of the non-BRIC countries. Labour rates are only part of the story, but rising rates and labour turnover will always occur as a consequence of success in non-BRIC countries, as they have occurred in BRIC countries. As Table 1 suggests, cost will remain a fundamental driver for companies considering non-BRIC countries.

Costs perception analysis

Based on a perception analysis carried out amongst 18 international consultants/analysts, Egypt was considered the most attractive country based on costs. The costs considered were a combination of start-up, infrastructure, and labour costs. The fact that most companies are based in one of the Smart Villages or Free Zones indicates that the government's strategy of using tax and investment incentives to attract businesses is working.

Cost comparison

* The relevant country scores indicated in Table 1 range from,
1 = very poor
2 = poor
3 = average
4 = good
5 = excellent

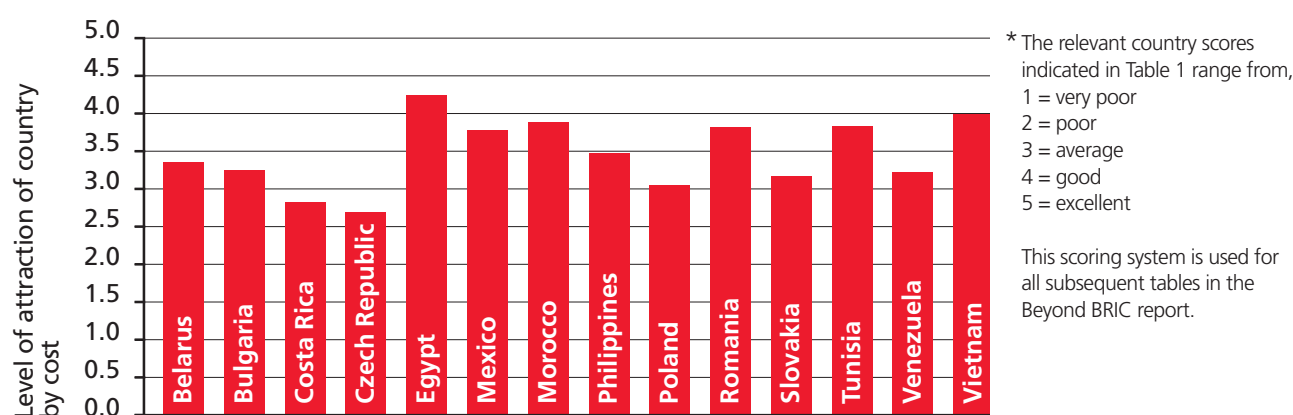This scoring system is used for all subsequent tables in the Beyond BRIC report.

Table 1 – Offshoring – costs comparison for 14 non-BRIC countries*

3.2. Factor two: availability of skills

This factor covers:

- Skill pool (size of labour pool with required skills) which include technical and business knowledge, management skills, languages, and ability to learn new concepts and innovate
- Vendor landscape (size of local sector providing IT services and other business functions).

The education systems in CEE countries are well developed – that is generally strong in sciences, technology and engineering, and accessible to the vast majority of the indigenous population. In contrast, large numbers of people in the other countries studied still live in rural areas and are not educated for IT and business service work. The level of literacy in these countries is significantly lower than in CEE countries. Therefore, while CEE countries are much smaller than Egypt, the Philippines, Venezuela, Mexico, Vietnam and Morocco, the percentage of their population being educated and becoming a highly skilled workforce is much higher. Still, the scalability of labour resources **in the longer term** is a major issue for client companies to consider when deciding on an offshore and outsourcing destination.

The number of skilled graduates produced annually by any country indicates how scalable the labour pool of the country will be in the long run. CEE countries have a highly skilled workforce with technical skills and training in research and applied sciences to engage in research and development (R&D) and innovation. As a result, a large number of Western European and US companies have opened captive R&D and innovation centres in CEE. For example, Morgan Stanley established the Mathematical Modelling Centre in Budapest, and P&G opened its European technology development centre in the Czech Republic. However, the labour pool of CEE countries remains limited and could come under pressure quite quickly in the face of growing demand.

By comparison, Egypt has 330,000 graduates (from all disciplines) per year, 31,000 of these have degrees in technology, science or engineering. With the right emphasis on the skills required in the near future and appropriate adjustment of the education system, a country like Egypt could catch up with the skill levels of workforces in CEE countries and, as a result, attract more highly innovative R&D work. Recently, Orange and Microsoft have established R&D centres in Cairo. Egypt is already able to differentiate itself through what has been called its 'multi-linguinity'. Of the 330,000 new graduates, some 25,000 from Cairo are capable of speaking different languages. For example, English is spoken by about 20,000 of them and somewhere between 3,000 and 5,000 speak French, 1,500 to 3,000 German, and 750 to 1,500 Spanish, while around 1,000 graduates speak Lithuanian!

The impact of this consistent stream of well-educated graduates is that the annual supply ensures a stability of labour costs and a choice of skills and languages. In contrast, CEE countries are mainly engaged in more technical and innovative types of work than their competitors from Asia, the Americas and the African Mediterranean, who specialise in relatively low-tech jobs such as call centres, hosting and some software development. Romania surpasses almost all European countries in its IT resource creation pool. It has excellent R&D and creative skills, and, compared with other CEE countries, it has a higher percentage of the workforce that speak several languages, including English, French, German or Italian.

Typically in CEE countries, language availability comes at a higher cost. Many of the countries in Asia, the Americas and the African Mediterranean investigated offer languages as a main skill. Advanced technical skills might be available (or they can be developed in-house through specialised corporate training programmes). For this reason a majority of these countries attract call centres for Western European and US-based companies where customer support is required in different languages. Here, Egypt has an advantage in that foreign languages tend to be spoken with very little or no accent (accents are often cited as one of the major disadvantages with other workforces). Many Western European and US companies, including Microsoft, Oracle, Orange, Alcatel and Vodafone, have established call centres in Egypt to provide technical support to their customers in different languages. This multi-lingual strength of Egypt gives it an advantage over other countries such as India, whose population speaks primarily English. The low level of multi-lingual capabilities in India makes it difficult for many EU countries to send some outsourcing work there.

When looking more broadly at the skills required, Egypt stands out well in terms of customer support and interaction. Denise D'ella, Vodafone International Services Director, observed that:

"Egyptians are very empathetic people… this helps very much because in a service-based industry you either want to do the job well and you want to help the customer or you don't. This is a behaviour you cannot teach people – you either have it or you don't."

The IT industry in Egypt now employs more than 35,000 engineers and generates approximately $2.2 billion per annum. Even so, Egypt has introduced stringent employment and quota laws. The Egyptian government has one of the toughest frameworks to protect Egyptian jobs through its policy of imposing a 90% local workforce quota. The 10% non-Egyptian workforce can only be breached in exceptional circumstances, and then only if permission is given. To date, the high quota level has not hurt the development of Egypt's outsourcing industry, although there is a lack of experienced middle managers. The shortage is being filled in some cases by temporary consultants usually contracted from India. The process of ensuring such applications are legal is lengthy and usually only followed through by larger companies capable of negotiating the paperwork and permissions.

Mr Wael Abouelmaaty, General Manager, VIAS Egypt 'Valeo InterBranch Automotive Software', speaks for many companies when he said:

"What we are looking for is to get employees with a combination of technical and soft skills. Egyptian universities provide graduates with excellent technical skills; however those fresh graduates need to learn soft skills. I need universities to put more emphasis on soft skills to achieve this much needed combination of technical and soft skills for our graduates."

To help overcome this and other problems faced by companies wanting to work with Egypt, Dr Reda, the Chairman of Allied Soft, has worked with other companies to form the new ITEC (Information Technology Export Community):

"Egypt has promising potential to undertake more projects than it currently does. To this end, ITEC will work to secure the international permits, licences and accreditations required for various sectors, provide training for staff, attract new investments, organise missions abroad, launch awareness campaigns, coordinate with related institutions, and enhance the quality of delivered products and services… at the moment countries such as India and Pakistan have outpaced Egypt in business process outsourcing even though Egypt has more capabilities in terms of its skilled labour force and employment capacity."

To improve the competitiveness of Egypt in the offshore call centres market and strengthen its positioning as an outsourcing destination for IT and software development, the Egyptian government is heavily investing in promoting education and training programmes on undergraduate and post-graduate professional courses. The EduEgypt programme was started in 2007 and produced 3,700 students in one semester. This programme selects students from all disciplines and provides them with education to acquire soft skills, language abilities and other business skills during their third and fourth years at college.

The government has also subsidised a call centre training facility to develop skills required and is funding a university intervention programme to help students prepare for employment. It also encourages companies to obtain appropriate training and certifications. In 2007, 27 Egyptian companies had CMM or CMMi certifications (some having CMMi level 5). Mr Wael Abouelmaaty, General Manager, VIAS Egypt 'Valeo InterBranch Automotive Software', commented:

"The government is very supportive, and helps us in terms of building (Smart Village), training, and the creation of places like ITI, which is a postgraduate school preparing engineers to bridge the gap between what the universities taught them and the real market."

Mr Wael Amin, President of ITWorx, a software company, added:

"We find ourselves worrying about supply and demand of resources of talent. We worry that demand will outstrip supply. We do a lot of work with schools and universities to identify potential leaders of future generations, and work with them through internship programmes."

Other countries are also competing for these markets, specifically Vietnam, the Philippines and Thailand. Vietnam specialises in software development. The IT industry in Vietnam focuses on telecoms, CAD, finance, factory automation, healthcare, and animation. It has an excellent education system that focuses on mathematics and logic, thus creating a good supply of relevant raw skills for its IT industry. While software development work outsourced to Vietnam is typically less complex than work outsourced to CEE countries, its extended labour pool makes it possible for Vietnam to handle large volumes of such work. English still poses a major challenge for companies outsourcing to Vietnam. As Egypt develops more technical skills, it is competing with Vietnam more closely in trying to attract software development business. Better language skills and proximity to Europe and the US (shorter travel time and less time differences) play to Egypt's advantage.[29]

[29] Carmel and Abbott (2007) op.cit.

A skill-related problem identified in all 14 countries is the lack of management skills, in particular in project management. The Czech Republic is probably the most advanced on this front, where some skilled project management is available. Countries find different ways to compensate for the management skills; for example, keeping management roles within the client or European/US-based partner. Clearly, as was found by the early movers to India, this has implications for costs and resources if the project management function needs to be supplied by the client organisation and even re-located to another country (or where the captive centre is based). Introducing more business education (business schools), possibly with programmes and staff educated in Western European or North American countries, would facilitate the development of management skills.[30]

The difficulty that Egypt has is to combine the technical, linguistic and management capability to meet demand and lift itself further up the value chain in terms of outsourcing and offshoring. While EU countries can benefit from easy mobility of labour, countries like Egypt are faced with the need either to attract back Egyptians with the right skills or to encourage immigrant expertise despite Egypt's own stringent work visa requirements. The gaps within Egyptian business are well known. One senior manager of a telecoms company said:

"The cost of skilled labour is definitely becoming an issue and right now to find and retain highly professional people within the company is a challenge. Middle management expertise is a problem."

The question is how the government will work with industry to address this issue within reasonable timescales. Some starts have been made, but timing is also crucial.

Summary point: Almost all non-BRIC countries are looking to produce good-quality graduates, but the real sign of a mature market will be those countries that convert growing labour pools into ITO/BPO skilled staff and register high retention rates for their senior staff. The ability to train, attract and retain good middle managers will ensure the capacity to build on the good foundations currently being established through the university education sector.

[30] Willcocks (2007) Offshore, Nearshore, Bestshore – Are You Sure? *MFT Focus,* Winter pp.14–16.

Skills perception analysis

The skills perception analysis places Egypt with the highest level of skills availability, coming ahead of the Philippines. As has been referred to, this perception is grounded in the fact that Egypt has the capacity to produce an annual supply of good-quality graduates with multi-lingual skills. It is this breadth of linguistic ability on top of the technical supply that is extremely attractive to international companies and puts Egypt ahead of other countries with more qualified technical skills. Mexico has also been rated highly because of its proximity to the USA, and its good education in business skills and the Spanish language.
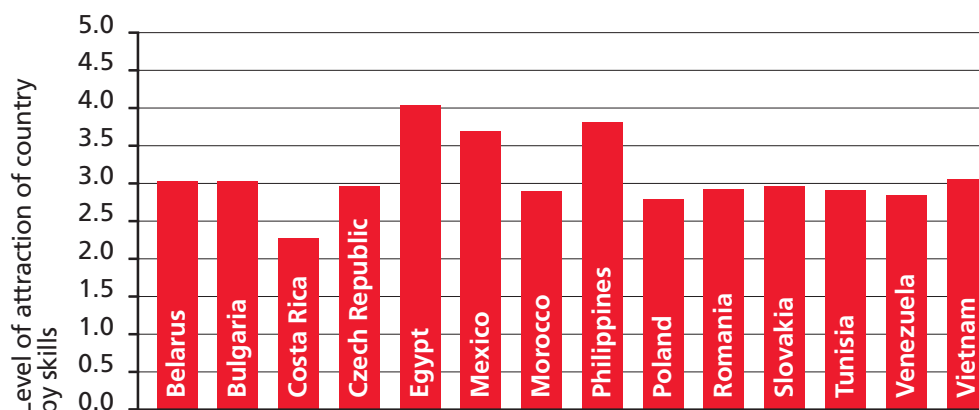
Availability of skills comparison

Table 2 – Offshoring – availability of skills comparison for 14 non-BRIC countries

3.3. Factor three: environment
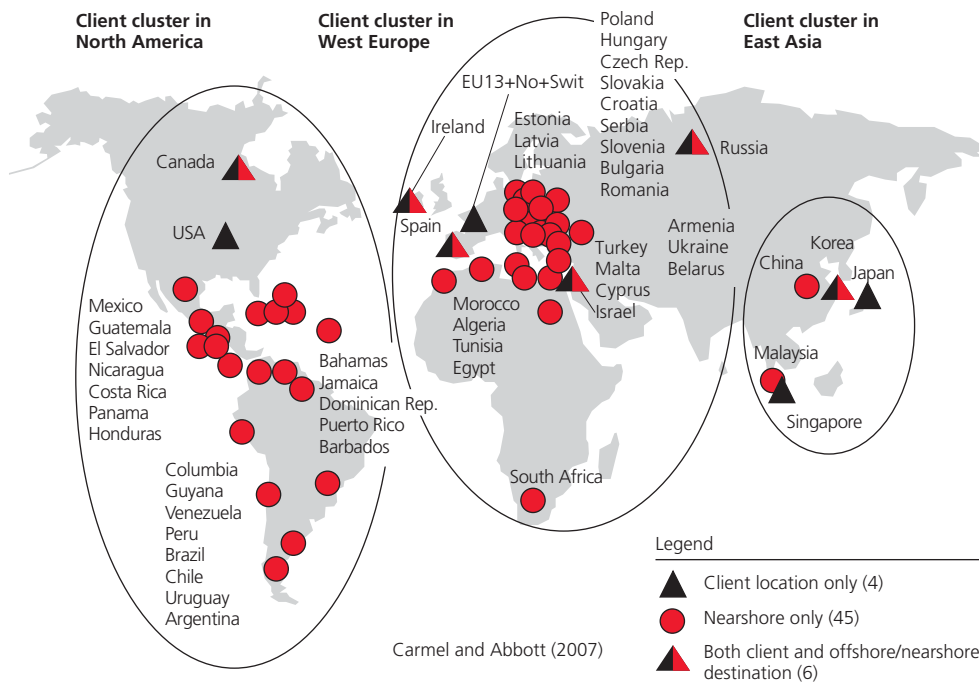
This factor covers:

- Government support (policy on foreign investment, labour laws, bureaucratic and regulatory burden, level of corruption)
- Business environment (compatibility with prevailing business culture and ethics)
- Living environment (overall quality of life, serious crime per capita)
- Accessibility (travel time, flight frequency, time difference).

Governments are keen to attract more foreign investment. One way of doing this in the non-BRIC offshoring and outsourcing countries has been to set up development zones that are often given special name status (e.g. 'Free Trade Zone' or 'Smart Village' in Egypt, 'Offshore Programming Zone' in Belarus or 'Nearshore Centre' in Morocco). Essentially, these sites are established on green field compounds where new state-of-the-art infrastructure can be installed, with additional help from the government, which offers tax breaks, less complex administrative procedures and, in some cases, more flexible labour rules. In Egypt this approach is overcoming the infrastructure building problems often faced in the major cities (e.g. Cairo, Alexandria, Assiut). For example, the Smart Villages can benefit from a high-speed broadband fibre optic network connecting all office buildings to ensure ongoing data exchange, voice and video transmission, virtual private network connections, voice over Internet protocol (VoIP), cable TV, and video-conferencing systems. A competent power supply network guarantees uninterruptible business activities.

Egypt is positioning itself as a gateway to communicate with the growing markets of other Arab-speaking countries, yet is ideally positioned to operate on European timescales as well as Mediterranean and African timeframes. In terms of the business environment, CEE countries are attractive destinations for European companies looking to outsource or offshore (or rather nearshore) business processes or services. Culturally, these countries provide a good fit with Western European cultures. Time zone difference is one hour and they can easily be accessed by air. Egypt, Morocco and Tunisia are further from Europe, though Morocco being close to its major client France works to its advantage. Egypt is only four hours away from most EU countries and has only a one- or two-hour time difference.

Figure 2 below shows the nearshore clustering that has been developing across the world.[31]

Figure 2 – The nearshore geography of globalising IT and business services

Carmel and Abbott (2007)

Legend

▲ Client location only (4)

● Nearshore only (45)

◤◢ Both client and offshore/nearshore destination (6)

[32] Based on research by the Outsourcing Unit appearing in Oshri, Kotlarsky and Willcocks (eds.) (2008) *Outsourcing Global Services* (Palgrave, London), and Lacity and Rottman (2008) op. cit.

[33] Kotlarsky, Oshri and Van Fenema (2007) *Knowledge Process in Globally Distributed Contexts* (Palgrave, London).

In practice, offshoring or outsourcing to sites in distant time zones can be an expensive choice, especially for software development projects.[32] Although the bill rate may be low, communication black-out times will raise costs. For example, India is about 10 hours ahead of the US East Coast. This means Monday in one country is already over in the other. Efficient software development is the product of the collaboration of ideas, business knowledge, technology experience, and the development skills of an entire team. That is why an in-house team sitting in the same vicinity is ideal. The next best thing is a team that can remotely collaborate within real time, using desktop sharing, VoIP, and Internet white board technologies.[33] Nearshore teams working in a US-friendly time zone usually have higher bill rates than the rates found in China and India. However, with service in places like Brazil, Panama, or Mexico, North American companies are getting much more flexibility, interactive collaboration, and the ability to use these resources more like in-house staff and still at a reduced cost.

Compared with Egypt, countries in Asia and the Americas require longer commutes and present large time zone differences for companies based in Europe. For call centres that operate 24/7, time zone differences do not create major challenges. However, where outsourced software development has to be managed remotely, time zones create a number of real challenges, in particular when projects are extremely complex. As a result, more recently some software development has been undertaken in closer locations like Egypt.

The geographical and time convenience has helped to attract other types of work to Egypt; for example, Intel-El Boraq assembling Intel motherboards and IBM's and Microsoft's establishment of new R&D centres.

For North American companies, CEE countries provide a good cultural fit. However, in terms of travel time and time zones these countries are much further than Costa Rica, for example, for North American countries to choose. Likewise, flights to CEE are shorter and easier for Americans than flights to Egypt.

Corruption is perceived as an issue in some of the 14 countries studied. Most governments understand that strong action is required to eradicate this. However, in developing countries this is not always so easy to police. While the Czech Republic has the least corruption in CEE, corruption is perceived as pervasive in Belarus which now ranks 151st out of 163 countries in Transparency International's Corruption Perceptions Index for 2006. Owners of import–export businesses in particular complain that corruption exists at every point in a transaction.[34] Meanwhile in the Gulf States and African Mediterranean, The Heritage Foundation comments:

"The ongoing transformation of innovative states in Bahrain, Qatar and the United Arab Emirates (UAE) may yet light the way for economic growth regionally."

Meanwhile Egypt made the largest worldwide leap in economic freedom over the last year, gaining four percentage points.[35] Egypt attracted an unprecedented amount of foreign direct investment in 2007, while the GDP grew by 7.1% and is expected to be 5.3% in 2009.[36] However, companies wishing to invest in the country are aware that several sources identify pervasive corruption as a major obstacle to doing business. In contrast, according to a US Commercial Services report 2008, many investors, while acknowledging the existence of corrupt low-level officials, have not identified corruption as a major impediment to foreign investment into Egypt.

Amongst the largest culprits in the EU, Romania and Bulgaria are particularly singled out for comment in reports. Corruption is growing in both countries, and, according to the EU Commission, justice reform and the fight against organised crime require more policing. The Commission's 2008 report on the management of EU funds in Bulgaria gave little grounds for hope that the situation will improve. The EU has threatened the two countries with harsh sanctions.[37]

Summary point: Positioning a country to benefit from its nearshoring opportunities provides strong market growth potential, especially in the current environment of economic uncertainty. To make nearshoring attractive, non-BRIC countries need to demonstrate unwavering government support, and need to work ever harder at improving the business and living environment factors under their control.

[34] The Heritage Foundation (2008) *Index for Economic Freedom* (The Heritage Foundation, USA).

[35] The Heritage Foundation (2008) op. cit.

[36] FT Special Report on Egypt, December 17th, 2008.

[37] European Commission (2008) *Report to the European Parliament and the European Council on the Management of EU-funds in Bulgaria* (EU, Brussels).

Environment perception analysis

Egypt has overcome many challenges to develop a climate that is perceived to be more attractive for business. The government's allocation of investment for infrastructure and its determination to address some of the major building issues is paying off. In addition, the government's reforms and implementation of laws to protect intellectual property rights are beginning to secure a favourable environment for longer term business commitment. There still remain worries about whether Egypt can continue this policy regardless of which political party is in power. This is yet to be seen.
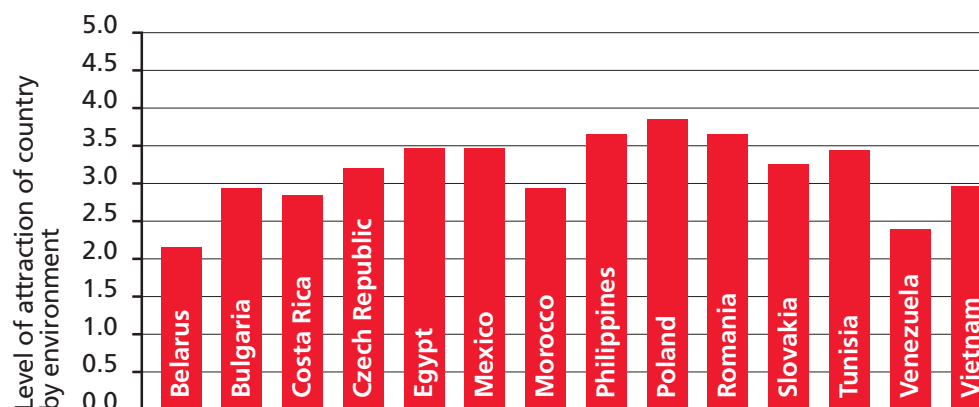
Environment comparison

Table 3 – Offshoring – environment comparison for 14 non-BRIC countries

3.4. Factor four: quality of infrastructure

Quality of infrastructure includes:

- Telecoms and IT (network downtime, speed of service restoration, connectivity)
- Real estate (availability and quality)
- Transportation (scale and quality of road and rail network)
- Power (reliability of power supply).

The standard of telecoms and IT infrastructure in several CEE countries is improving and becoming comparable to that of Western European countries. Bulgaria, the Czech Republic and Slovakia, for example, have excellent network and infrastructure. In Romania, the domestic telecoms infrastructure is still poor but improving. The Romanian government has announced that it aims to transform Romania to the 'Internet hub' of the Black Sea region. In the last few years the country has witnessed one of the largest growths in mobile communications in Europe.

In most parts of CEE, the stability and quality of telecoms and IT infrastructure is reliable across the entire region, but in other non-BRIC countries availability and quality of telecoms and IT infrastructure vary significantly depending on location in the respective country. Generally, in these countries there is good-quality infrastructure available at special high-tech business parks and large cities, but limited or no access in rural areas. For example, Tunisia has a large number of high-tech parks (called 'Technopoles') with state-of-the-art IT infrastructure and telecoms facilities, while Morocco has a better telecoms infrastructure than Tunisia but only in special development zones. The Philippines stands out as having a particularly good telecoms infrastructure with a reliable domestic and inter-island service as a result of the US establishing its military bases there. In Vietnam, where telecommunications and power need improvement, infrastructure is the major barrier to the growth of IT in the country.

In contrast, Egypt has an electrification rate of 98% and, in the past few years, the telecoms field has been substantially liberalised. The process of licensing a second fixed-line operator to work alongside Telecom Egypt is underway, and there are three mobile phone operators (Mobinil, Vodafone Egypt and Etisalat) all of which have licences to provide 3G services. Internet penetration is however low and sporadic, although connectivity and the lowering of costs are considered by many businesses outside the Smart Villages to be the crucial issue needing government attention. According to a 2008 report, Egypt ranked 63rd in the world on 'Networked Readiness'. But, of course, this is a relative measure. Thus, the UK is 12th and India 50th. Amongst other non-BRIC countries Tunisia, Slovakia, and Czech Republic do better than Egypt; Mexico, Costa Rica, Romania and Poland do much the same; while Bulgaria, the Philippines, Venezuela, Vietnam and Morocco do worse.[38] Egypt, however, registers the biggest improvement across all the 127 countries analysed. Between 2006 and 2008 it advanced 17 places, due to improvements in the environment, regulatory environment and government readiness **"pointing to an increased emphasis on ICT penetration in the national development strategy".**[39]

For Egypt, the Smart Village enabled the country to get around some of the infrastructure issues dominating the larger cities. The evidence is that international companies are moving to the Smart Villages because they can finance new buildings and infrastructure, and access staff locally. They also provide bus services for their staff locally, and this helps to avoid the major traffic problems faced when crossing the city and a lack of an integrated transport system.

While CEE countries have well-planned and relatively good-quality roads and an integrated public transport system comprising rail, metro and buses, countries in Asia, the Middle East, Africa and the Americas have developed infrastructure in specific centres, where the workforce with required skills is available. Usually this is near to the international airports and major cities. Such 'high-tech islands', often surrounded by slums or a desert, provide high-quality IT infrastructure, have better roads and offer high-quality office space and other facilities (e.g. cafeterias, fitness facilities) at Western European standards.

[38] Dutta and Mai (2008) op. cit. page xix.

[39] Dutta and Mai (2008) op. cit. page 16.

The government of Egypt is investing in the building of roads, and improving the transport infrastructure in Cairo, but estimates that it needs to spend $1.7 billion on major road construction and expansion projects (including $258 million on the completion of the Cairo ring road). One of the major criticisms of transport in Egypt has been the unfinished ring road around Cairo. The government is also targeting the third Cairo metro line (the Egyptian government has estimated the cost of Phases One and Two at more than $1 billion), which will aim to ease congestion.

In addition, Egypt's railways have suffered from long-time neglect and under-investment. According to the Egyptian government, only 47% of the railways' locomotives are serviceable and only 15% of the rail network is electrified. However, there is progress and in 2008, people started using trains from downtown to the 6th of October village. The high number of fatal injuries sustained also indicates the poor standard of the infrastructure. In the last decade, more than 500 people have died in accidents on the Egyptian railways. All this adds up to serious investment required in the Egyptian rail infrastructure. The Egyptian government has recently announced an infrastructure stimulus of $2.75 billion made up mostly of water, sanitation, road and transport projects. A further $2.75 billion of public–private funds will be injected into the economy.[40]

Summary point: The legacy of bad infrastructure in many non-BRIC countries is being overcome by establishing ring-fenced new business parks with state-of-the-art facilities which can operate at international standards with guaranteed services, telecoms, broadband and service facilities. Government support for, and involvement in, long-term infrastructure improvements are key indicators of location attractiveness.

[40] FT Special Report on Egypt, op. cit.

Infrastructure perception analysis

Egypt has had to inject massive investment in a comparatively short time, in order to make up for years of neglect of its infrastructure. The strategy of providing new facilities and establishing Smart Villages has been successful, but is still in its early stages. Connectivity outside cities in the rural areas is still patchy and transportation problems still dominate, particularly in Cairo, despite plans to extend metros and public transportation.
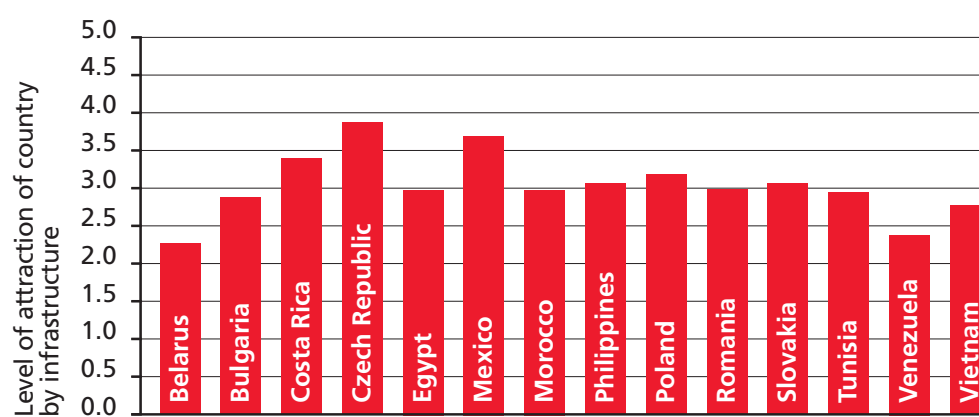
Quality of infrastructure comparison

Table 4 – Offshoring – quality of infrastructure comparison for 14 non-BRIC countries

3.5. Factor five: risk profile

Offshoring and outsourcing are inherently risky, and companies need to draw up very detailed macro and operational risk-mitigation plans. In this section we assess the following risks at the country level:

- Security (risks to personal security and property from fraud, crime and terrorism)
- Disruptive events (risk of labour uprising, political unrest, natural disasters)
- Regulatory risks (stability, fairness, efficiency of legal framework)
- Macroeconomic risks (cost inflation, currency fluctuation and capital freedom)
- Intellectual property risk (strength of data and intellectual property protection regime).

Overall, with the exception of Belarus, CEE countries, in particular those within the EU, are considered more secure to live in and visit than countries in the Middle East and Africa, Asia and some parts of the Americas. The Czech Republic is considered one of the most stable post-Communist states. CEE countries have less history of natural disasters than countries in Asia and the Americas (e.g. flooding in Prague in 2002 caused minor damage compared with the devastation caused in Thailand by the Indian Ocean earthquake and tsunamis in 2004).

Egypt's image has been damaged as a result of the rare terrorist attacks on the resorts of Dahab in April 2006 and Sharm El Sheikh in July 2005. There is a perception in some quarters, notably the US, that Egypt is unsafe, which obviously affects the choice of business destination. The Egyptian government is trying to reverse this perception by enforcing security measures, with cars and packages being thoroughly checked and people being searched for weapons or explosives on the entry to office buildings and hotels. In fact, the recent survey of 448 outsourcing users by Black Book Research rated Cairo as the world's 10th safest outsourcing city in 2008. Cairo was preceded by Singapore, Dublin (Ireland), Santiago (Chile), Krakow/Warsaw (Poland), Toronto (Canada), Prague/Brno (Czech Republic), Budapest (Hungary), Monterrey (Mexico), and Beijing (China). When it came to the most dangerous outsourcing locations, the survey listed Jerusalem (Israel), Mumbai (India), and Rio de Janeiro/Sao Paolo (Brazil) as the top three. This survey was conducted a month before the Mumbai bombings.[41]

Inflation in Egypt is seen as a major risk for the economic stability of the country and to its ability to continue to attract external investment. This inevitably severely impacts businesses where they are forced to raise salaries to help meet costs of living. Inflation has risen to 20% in the past year and the government itself has been hit by the need to raise salaries and to cut tax benefits and corporate tax relief to do this.[42]

While the level of software piracy in Egypt is dropping, due to the government bringing in anti-piracy laws and laws to protect intellectual property rights and copyright, there are severe problems in many other non-BRIC countries. In Venezuela, Vietnam and China, for example, the software piracy rate is above 80%; in Thailand, Tunisia and Russia it is between 70% and 80%.[43] In Morocco, Romania, Bulgaria, the Philippines, Costa Rica and Mexico, the piracy rate is between 60% and 70%. In Egypt it is 60% and 57% in Poland. In Slovakia and Hungary it is between 40% and 45% and, the lowest 39% in the Czech Republic.[44] While Vietnam is perceived as a stable and secure environment, it is also recording extensive illegal copying and a culture of software piracy. In CEE, Poland and Romania are known for software piracy and the lack of intellectual property rights protection. Many governments, including Romania, Costa Rica and the Philippines, are taking steps to strengthen and enforce intellectual property rights protection and copyright laws. In Poland, however, this is not a current high priority for the government.

[41] Financial Week, December 11th, 2008.

[42] FT Special Report on Egypt, December 17th, 2008.

[43] The piracy rate is calculated as the total number of units of pirated software deployed in 2007 divided by the total units of software installed.

[44] http://www.nationmaster.com/graph/cri_sof_pir_rat-crime-software-piracy-rate.

In terms of political instability, Thailand currently is facing the most severe pressures and is seen as an unsafe destination for business investments until its political status is resolved. According to the Global Competitive Index for 2008/09, Egypt ranks 81st (out of 134 countries assessed), down four places from 2007.[45] Despite some improvements, macroeconomic instability remains a major challenge for the government, as mirrored in the 125th rank the country obtains on this assessment. High government debt, double-digit inflation and a high – although decreasing – budget deficit continue to weaken the macroeconomic environment, despite improving fiscal management. In addition, labour market efficiency is poor in international comparison. At the same time, Egypt has made progress in fostering technological readiness (see above). To benefit further from internationally available technology, Egypt needs to upgrade its educational institutions, which continue to receive a weak assessment in this particular study.[46] Business Monitor (2008) puts the issue another way: although levels of education are relatively high, there is a considerable mismatch between the skills taught in schools and those required by most employers.[47] The EduEgypt programme has been put in place to help address this gap, but it is in its early stages.

Summary point: Many of the major risk factors are unpredictable, however, non-BRIC countries establishing strong legal, educational and economic structures are more attractive to business, and attract new investment, collaboration and development.

[45] Porter and Schwab (2008) *Global Competitiveness Report* 2008–9, World Economic Forum. http://www.weforum.org/pdf/GCR08/GCR08.pdf.

[46] Porter and Schwab (2008) op. cit.

[47] Business Monitor (2008) op. cit.

Risk perception analysis

Egypt has not had a terrorist attack since 2006, however the perception persists that it is open to regular attacks despite evidence to the contrary and despite other countries suffering similar or worse attacks since. This perception has been attributed partly to the lack of marketing of Egypt per se, and partly to the press continuing to refer to it on a regular basis allied to Middle East troubles. Egypt is currently also experiencing uncontrolled inflation and this, plus the issues surrounding continuity, stability and the government's capacity to protect businesses once they are established, means there is hesitation at giving a higher rating at this stage. In contrast, countries in the EU have a lower risk profile, due to their international compliance with economic and regulatory frameworks, and the lack of major internal attacks.

Note: In the graph below, countries with a higher score are perceived as having a lower risk profile.
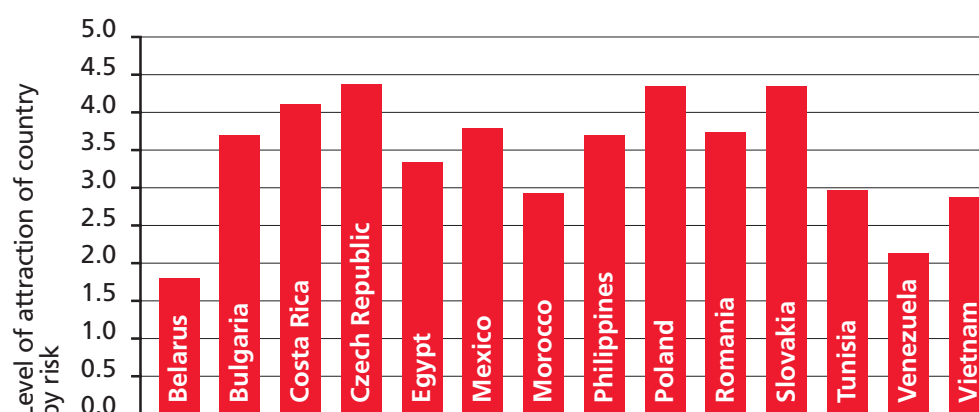
Risk profile comparison

Table 5 – Offshoring – risk profile comparison for 14 non-BRIC countries

3.6. Factor six: market potential

Market potential here refers to a country's future attractiveness as an offshore location for IT and business services. This may take one or more forms:

• As a captive operation using local labour, infrastructure and resources
• As an outsourced operation using local IT service suppliers
• As an ITO/BPO supplier to organisations based in the host country and nearby region.

Looking at the CEE countries, the Czech Republic and Poland stand out as countries with notable market potential. Each already has $500 million a year in revenues from ITO/BPO service exports. They are attractive both as captive and outsourcing locations. While the Czech Republic has language and cultural compatibility with Western European companies as well as good infrastructure, its low wages are rising, as are property costs, and it has a low level of service maturity. Its main threats are other CEE countries that will also seek to penetrate further into the adjacent Western European market. Poland is also a strong nearshore destination for Western European companies and is strong in R&D and infrastructure, with a well-educated if small-sized IT workforce. It faces similar threats and opportunities as the Czech Republic. Romania has a smaller market potential and starts at a lower base – some $100 million from ITO/BPO exports in 2008. It has attractive cost competitiveness and strong software development capability, but a small labour pool that needs more investment in IT skills and education.

In terms of ITO/BPO services, the market is growing as CEE countries become more 'Western' and the quality of life in these countries moves toward those of Western European countries. Local CEE demand for software and IT-related products and services is expected to continue growing, which means that Western European companies already present in CEE are able to take advantage of their good access to such markets.

At present, the Middle East and Africa are less attractive than CEE for Western European companies, partly because of a lack of knowledge and partly because of perceived language and cultural differences. However, this is changing with Morocco and Tunisia focusing on French (and Spanish) speaking countries to attract potential clients. Egypt is positioning itself to exploit its strengths and target Western European and US clients through its multi-lingual workforce (fluency in English, French, German, Spanish, Portuguese, and Dutch); lower labour costs than in surrounding low-cost regions; time zone proximity with Western Europe; and relative familiarity with Western European culture over traditional outsourcing destinations such as India and China. Egypt's IT sector is forecast to grow from $889 million in 2006 to $1.3 billion in 2011.

As one senior executive explained:

"The new positioning is based not so much on outsourcing, as on cooperation. We can now help Western companies go to new markets… we go together and get business from a third party."

Another factor in Egypt's favour is the relationship it has established with India. From this relationship Egypt is positioned to gain from the benefits of 'reverse outsourcing'. Where India needs to be nearer to some of its clients, Egypt may be a suitable base. Indian outsourcing providers are striving for an optimal cost-service mix of onshore and offshore operations that pleases clients, while increasing revenues and maintaining profitability. As wages continue to rise in India and the US dollar's value decreases against the rupee, it becomes expensive for Indian companies to maintain operations solely in India. One scenario is Egypt's potential to become the 'India of the Middle East'. In addition, Egypt has better relationships and better cultural fit with the 'Western' worlds than many other Arab-speaking countries in the Middle East, so putting Egypt in the position to act as 'middleman' between Western and other Arab-speaking countries.

Nearshoring represents a major way in which non-BRIC countries can compete with India for market share. The top Indian firms now offer a location menu of choices to their clients, which mitigates some of the currency costs incurred in uncertain markets. For example, India-based TCS can offer its British clients services that are farshore (India), nearshore (Budapest, Hungary), and onshore from their offices in London, Nottingham, or elsewhere.[48] Another Indian firm, Infosys, has 'Proximity Development Centres' and like other Indian firms has also refined its internal processes in mitigating time zone difficulties.[49]

In the Americas, Mexico succeeded in recording $650 million of ITO/BPO exports in 2008 (Egypt registered $750 million in its ITO and BPO exports for the same period). Proximity to the US is a major strength, together with its labour pool as well as Spanish and improving English language proficiency. Mexico has some weaknesses in cost competitiveness and service maturity, but its market potential lies with Spanish-speaking call centres, especially with US customers. Most of the companies outsourcing and offshoring work to Costa Rica and Venezuela are US companies that are more concerned with proximity to the US and are linked to the US dollar currency. Venezuela, for example, is one of the smallest markets in the Latin America region and therefore is not seen as an immediate competitor for the future.

[48] A detailed TCS case study by the authors appears in Oshri, Kotlarsky and Willcocks (2007) op. cit.

[49] Carmel and Abbott (2007) op. cit.

In 2008, the Philippines recorded $4.1 billion ITO/BPO in exports. Whether for captive or outsourcing services, the Philippines offers cost competitiveness, as well as an educated workforce and English proficiency – all of which has played well into the US market though it does need to improve its service maturity and IT skills levels. The Philippines has yet to move into other markets and is threatened by emerging lower-cost destinations, not so much in voice-based customer support, as in other types of BPO. In the Asian countries, and in particular Vietnam and the Philippines, demand for software and IT-related products and services in the local market is growing, but much more slowly than in CEE and mainly in the major cities, as large proportions of the populations are still rurally based. Local demand in Thailand is also emerging but is still behind Vietnam and the Philippines.

Another way to look at market potential is on a more fine-grained analysis of offshore city hot-spots around the globe. Looking just at the non-BRIC countries, one recent analysis suggests that Cebus City, Ho Chi Minh City, Cairo, and Hanoi, are in the top 15, while Krakow, Prague, Pasig City, Warsaw, and Brno, are in the top 30 such emerging cities.[50] These cities are being increasingly used as both first choice but also as second tier complementary destinations within the same country or across different countries (e.g. Bangalore and Coimbatore; Mumbai and Budapest). Such cities and combinations are rapidly becoming recognised as hot-spot global hubs for specific IT and BPO functions.

Summary point: The competition between non-BRIC countries for clients is increasing as more of them offer language and basic call centre support facilities. In order to expand the markets, countries are looking to raise their level of expertise and establish niche market capabilities. Some countries such as Egypt are positioning themselves to benefit from the relationships they have established with BRIC countries and are focusing on nearshore opportunities.

[50] Global Services-Tholon (2007) *Top Fifty Emerging Outsourcing Cities*. www.globalservicesmedia.com. The top 30 list includes 13 cities in BRIC countries.

Market perception analysis

Egypt has scored highest on market potential of all the countries. This is because of its unique geographical positioning, which means it can work with Mediterranean, European, African, and Arab countries. This potential is only now becoming available and analysts and businesses see this as a real opportunity to expand markets and develop new services based on the strong educational and linguistic skills of the population. The issue is how to convert the potential into large-scale growth.
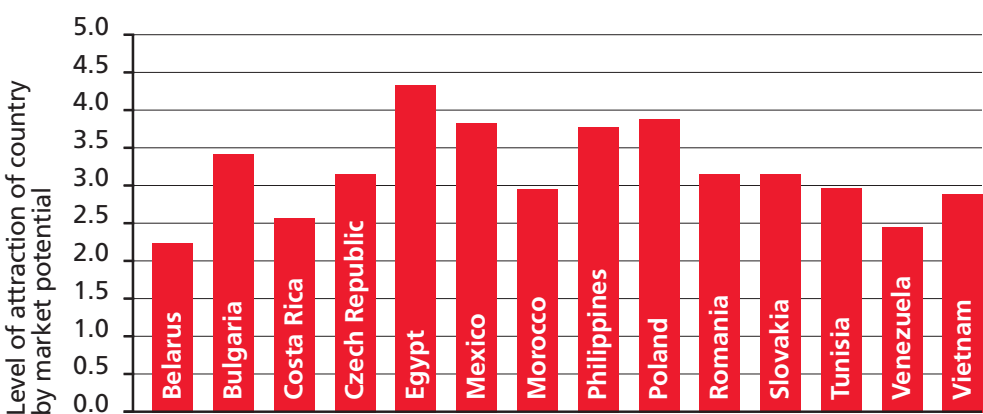
Market potential comparison

Table 6 – Offshoring – market potential comparison for 14 non-BRIC countries

An LSE Outsourcing Unit report

4. Competitive positioning of Egypt

Current outlook

Having compared representative non-BRIC countries on six factors, here we provide a more searching assessment of one country – Egypt – and its competitive positioning in the global sourcing market.

4.1. Egypt's advantages

Egypt offers a distinctive business proposition for companies interested in outsourcing, nearshoring or offshoring. This positioning is based on a combination of its strengths. These are:

- **Labour scalability:** Egypt is actively ensuring a constant supply of resources at competitive costs.

- **Linguistic skills:** Egypt offers a great variety of languages that are spoken with little or no accent (a distinctive skill profile, only available elsewhere at a premium).

- **Cultural fit:** Egypt has better relationships and a better cultural fit with Western European countries than many other Arab-speaking countries.

- **Nearshoring:** Egypt offers a convenient, cost-effective destination for 'nearshoring' for European companies. The small time zone difference with European clients is similar to that in CEE countries where costs are higher.

- **University links:** Egypt has begun encouraging large foreign companies and top universities to build stronger relationships. Some of these companies already take the best graduates and help to customise teaching programmes to develop the required skills. However, similar advantages are available in many countries investigated. Therefore, it is simply becoming mandatory to do this. In order to speed up this process, some companies in Egypt, for example, ITS, have established their own academy for graduates to help bring in the skills they need.

- **Call centres:** Egypt is already an attractive call/contact centre destination for large multi-nationals with multi-lingual clients around the world. Competition in this is growing from such countries as the Philippines and Morocco. In the Philippines there are currently 124 major contact centres, and 198,000 full-time employees working for companies such as Dell, AOL, J P Morgan, Siemens, HSBC, Shell, Citibank, and many others. The Philippines has 380,000 graduates each year (slightly more than Egypt), 15,000 of them focused on technology (less than in Egypt). The main difference in the skills is the variety of languages on offer by Egypt. Based in a former US colony, call centres in the Philippines mainly provide services in English. Therefore, the Philippines' past relationship with the US plays to its advantage. Egypt is working hard to attract various markets (French-speaking, German-speaking and Spanish-speaking as well as others).

Egypt competes with Morocco for French and Spanish clients. Morocco already has a large number of call centres that serve major companies in France and Spain (in 2005 Morocco hosted about 50% of French offshoring) and is looking to attract more European francophone countries (Belgium, France, Luxembourg, Switzerland). Other (smaller) players in the call centre market are Tunisia, which offers call centre work for French-speaking countries, and Costa Rica, which is more attractive to US clients because of its proximity to the US (a short flight), languages (Spanish is the main language and English is spoken widely) and low costs (lower than India).

4.2. Responding to the challenges

There is no single ideal offshore sourcing destination that suits every company. All locations, including top-tier BRIC countries, Canada and Ireland, have their disadvantages and much depends on the client country, the services required, and the time period. However, the ability of a country to identify its weaknesses and develop strategies to minimise their impact will increase its potential competitiveness in the long run.

Egypt has a number of weaknesses which are, however, hardly unique to Egypt:

4.2.1. Poor management skills

All the countries investigated (as well as BRIC countries such as Russia, Brazil and China) have similar problems at some levels. Countries find different ways to compensate for the lack of management skills; for example, keeping management roles with Western European and US-based clients or partners, or bringing in specialist expertise from overseas. This has implications for costs and resources, if project management functions need to be supplied by the client organisation and even re-located to the country of the supplier (or where the captive centre is based).[51] Egypt currently has a gap in middle management knowledge which is perceived to be growing as the market expands. It is not yet clear what the strategy is to address this on a wide scale.

4.2.2. Development work

Egypt is not yet a substantial centre for development work (as opposed to call centre work). There are a few examples of captive centres set up by, for example, SQS, Valeo and Oracle that are involved in software development and even innovation centres (Microsoft, Intel and IBM). However, these form a small proportion of all the work outsourced and offshored to Egypt. The vast majority of the work is call/contact centres and telephone support work. In order to attract more high-end software development work (e.g. more technical work and innovation), Egypt needs to develop more creative skills and expertise in applied sciences, as has been happening in CEE countries.

[51] For illustrative US-based case histories see Lacity and Rottman (2008) op. cit.

4.2.3. Negative perception

Egypt still suffers from a negative perception and a belief that it is a country regularly targeted by terrorists. While it is impossible to ignore the history of terrorist activities in Egypt, it is important to stress that some other countries, in particular India, have had more terrorism in the past, and more recently. While this hit the economy temporarily, it did not stop companies outsourcing to India. Furthermore, in Egypt outsourcing and offshoring businesses set up around Cairo, which is now included in the 10 safest outsourcing locations worldwide in an authoritative report by the Black Book Research and Brown-Wilson Group.[52] The issue needs further presentational work by Egypt, and there is a need to give companies confidence that they are operating in a legally enforceable framework.

4.2.4. Transportation system

Egypt's transportation system requires improvement to tackle limited public transport, poor quality of roads and traffic problems. This is also true of many countries, including BRIC countries, but they have found ways to address it in their major centres. Among the countries investigated here, it is only CEE countries that have reliable transportation systems. The government of Egypt is encouraging investment in the transportation system; for example, by introducing more public transport trains to connect downtown Cairo with its Smart Villages, but this needs to extend across the country.

4.2.5. Working hours

Differences in the legal working week and national holidays clash with Western European and US calendars, though not with Middle Eastern countries. Clients considering outsourcing or offshoring complex work may require frequent interactions with project teams based in Egypt and in real-time (synchronous) collaboration. On the one hand, Egypt has only a few hours' time difference with European countries, but on the other hand, differences in the legal working week and different national holidays reduce this possibility. To answer the concerns of potential clients and investors and set up realistic expectations, it is important to address this issue explicitly; for example, by explaining how businesses in Egypt can adapt to the different working week. Companies in India do this already. Furthermore, some cultures, for example Indian and Russian, are very flexible about working hours. By contrast, Western European cultures are stricter about fixed working hours and do not easily agree to work outside these. If potential clients and investors are well informed they will be more attracted to engaging in business relationships with Egypt.

4.2.6. Education

The high level of illiteracy in the country could hold Egypt back, particularly as there is a perceived worry that the current graduate supply may outstrip demand. In Egypt the percentage of the educated population is much lower than in Central Europe. A large percentage of the population lives in rural areas and is not currently well educated.

These six issues are not insoluble and indeed have received, and continue to receive, active attention from the government, its appointed agencies and the business and education sectors. But a good barometer for those looking to Egypt as a business location will be the extent to which these issues are being resolved and even solved over the next two years.

[52] Source: http://www.financialweek.com.

5. Egypt – strategising the future

If Egypt's ambition to break free from the non-BRIC pack is to be achieved, there are a number of factors that need to be addressed.
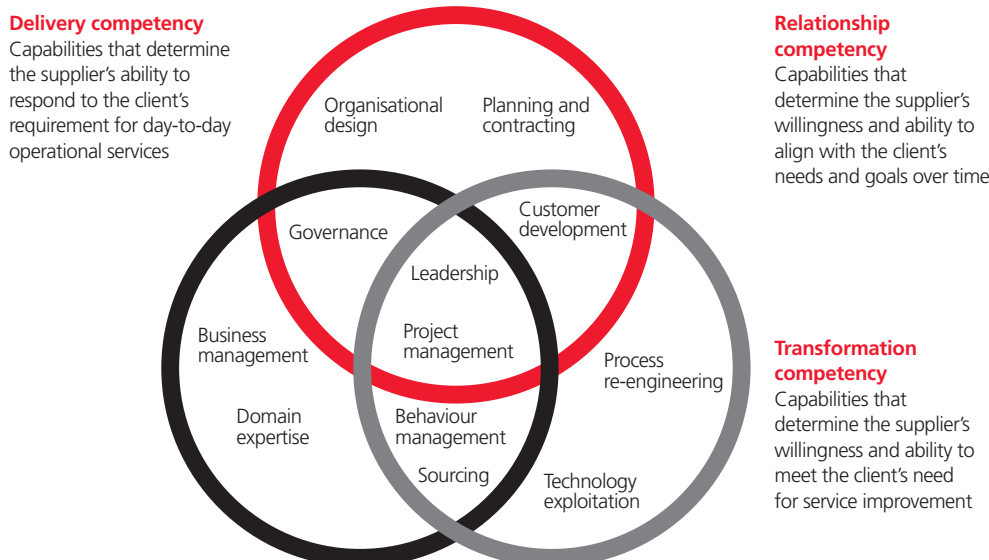
5.1. Develop suppliers of software development work

In order for Egypt to attract more high-value software development work and establish itself as a preferred outsourcing location, it needs to develop the capabilities of local suppliers so they move up the value chain from call centre work. The government of Egypt is already promoting local companies to invest in software development and software manufacturing, but this is at an early stage. Targeting grants, investments and tax incentives to smaller firms, to qualified individuals, and to training programmes will help to facilitate local entrepreneurial initiatives and make them more attractive to graduates looking for careers in Egypt. In India, international captives lose their best talent to other local suppliers such as Infosys, TCS, and Wipro who offer more interesting work and better career paths to their employees. The main reason why Indian vendors are able to offer better career paths and more challenging work to their employees is because they are able to attract high-value software development work and win long-term contracts with major Western European and US clients.

5.2. Relationship and transformation capabilities

Clients are looking for suppliers who can respond to the customer's changing needs (i.e. have a delivery competency); can radically improve service in terms of quality as well as cost (i.e. have a transformation competency); and are willing and able to align their business model to the values, goals and needs of the customer (i.e. have a relational competency). Countries that have suppliers able to do this are in a better position to attract more complex, knowledge-intensive and strategic activities. The maturity of Egyptian vendors can be assessed based on 12 capabilities that are leveraged into three key competencies, as shown in Figure 3.[53]

Figure 3 – Core capabilities of outsourcing suppliers

Delivery competency
Capabilities that determine the supplier's ability to respond to the client's requirement for day-to-day operational services

Relationship competency
Capabilities that determine the supplier's willingness and ability to align with the client's needs and goals over time

Transformation competency
Capabilities that determine the supplier's willingness and ability to meet the client's need for service improvement

Organisational design
Planning and contracting
Governance
Customer development
Leadership
Project management
Business management
Process re-engineering
Domain expertise
Behaviour management
Sourcing
Technology exploitation

The 12 capabilities that local Egyptian suppliers need to develop are detailed in Table 7

Table 7 – Building Egyptian supplier capabilities

1. Leadership	The ability to identify and deliver overall success throughout the deal. A capable leader should have a strong relationship with client-side leaders and with top management in the supplier's organisation.
2. Business management	The ability to deliver according to the service agreements and business plan agreed between client and supplier.
3. Domain expertise	The ability to retain and apply professional knowledge. In particular, ability to apply business knowledge and experience in a client's specific business context and environment.
4. Behaviour management	The ability to motivate and inspire people to deliver high-level service. (Signs such as high turnover might indicate that this capability is weak.)
5. Sourcing	The ability to access resources as needed in an effective and efficient manner. (Suppliers, assertions on economies of scale, infrastructure and procurement practices; availability of specialised professional skills, their quality and costs at various locations would provide indication of this capability.)
6. Process re-engineering	The ability to incorporate changes to the service process to meet (dramatic) improvement targets (for the client).
7. Technology exploitation	The ability to deploy new technologies swiftly and effectively (technologies that were not available to customers before).
8. Project management	The ability to deliver a series of inter-related projects. (Expanding the use of the supplier beyond the original outsourcing arrangement might indicate this capability being strong.)
9. Customer development	The ability of a supplier to enable its clients to become customers who are able to make informed choices about service levels, functionality and costs.
10. Planning and contracting	The ability to deliver 'win-win' results for the supplier and the customer. (Evidence of a supplier communicating its vision of the potential reward for both parties and a coherent process for achieving it would indicate this capability being developed.)
11. Organisational design	The ability to design and implement an organisational arrangement that would match customer needs (e.g. sometimes suppliers may need to be flexible and adopt different organisational structures for different clients to optimise client–supplier organisation fit).
12. Governance	The ability to track and measure performance (e.g. some kind of review committee that defines, tracks and evaluates performance over time and works closely with clients).

5.3. Create business opportunities for captive centres

The definition of a 'captive' is when a company sets up its own, wholly owned facility for software development, IT support, back-office data processing, call centre operations, or business process outsourcing usually in another country. The basic strategy followed by the parent company needs to change over time to take advantage of evolving business opportunities. For example, many of the companies that established captive facilities in India have switched strategies for managing their captives during the last few years.[54] Some companies have decided to sell their captive centre services to outside customers – in addition to using the services for their own needs – while others outsourced non-core tasks to local vendors to reduce costs. Still others sold off majority stakes in their captive centres to improve the firm's operations and balance sheet. As captives in Egypt become more mature, it is important for them as well as for local vendors to understand the business opportunities for improving their efficiency.

Research shows there are three different captive models. These are explained below.

5.3.1. Hybrid captive strategy

The hybrid captive is where the local company performs core business processes for the parent company, but outsources non-core work – say human-resources tasks – to a local vendor. By farming out non-core tasks, the captive centre can invest more time and money in higher-profile work, as well as cut costs. The downside is that the projects being outsourced often involve small budgets and repetitive work, so they are of low priority to vendors and as a result usually suffer from high staff turnover. A hybrid captive must also develop management skills, which are initially provided or borrowed from the parent company.

In Egypt, captives set up for non-call/contact centres may consider outsourcing call centre activities to local vendors. Alternatively, as captives and local vendors mature, they may restructure their resources to take on more complex and strategic assignments from the parent company. This could provide local vendors with the opportunity to attract more work in Egypt.

[54] Oshri, Kotlarsky and Liew (2008) Four Strategies for Offshore 'Captive' Centers, *Wall Street Journal*, Business Insight section, May 12th, 2008.

5.3.2. Shared captive strategy

The shared captive performs work for both its parent company and external customers. This enables it to become more efficient and valuable because it services multiple projects. If competition for customers is driven by cost, local vendors may have an advantage. Therefore, shared captives should look for clients internationally, in the locations where they would have cost advantage over local vendors. For example, some clients that are hesitant to outsource to a vendor in Egypt may find a business proposition of outsourcing to a Western company working from Egypt very attractive. However, if local vendors can offer the same services cheaper, and demonstrate their credibility and experience, they could compete with captives that have adopted shared captive strategy.

5.3.3. Divested captive strategy

The divested captive centre is one that was sold off by its parent company yet still provides services to it. In India several captive centres were sold to major local vendors, such as TCS and Infosys. This process and model may become more relevant in the future, as the market matures in Egypt.

6. Research base and methodology

This study draws upon primary research conducted by the authors between September 2008 and January 2009. This consisted of:

1. A quantitative, comparative analysis of 14 selected competitive non-BRIC country locations servicing three main world regions – EMEA, Asia Pacific and the Americas. Benchmark assessments of the UK and India were provided from our own database analysis. Data on the additional 14 countries were then obtained by questionnaire from 18 senior global sourcing analysts working in client (5), supplier (6), management consultancy (3), market analysis (2), and research (2) organisations. These analysts were carefully selected as a) highly experienced and knowledgeable professionals in the global sourcing field and b) proportionately representing the Asia Pacific, EMEA and the Americas regions.

2. Further interview research with 50 client organisations and suppliers, and six market analysts. All respondents were experienced in global sourcing and expert in business and IT service location attractiveness. Interviews of between 45 and 70 minutes were conducted, and the tape transcriptions verified with respondents.

3. Total research was through a mix of interview, questionnaire, desk research, and client and supplier site visits in Europe, Asia Pacific, and North Africa across the September 2008–January 2009 period.

The study also draws upon the Outsourcing Unit's 16-year longitudinal case database of 1,000 plus global sourcing IT, BPO and offshoring arrangements studied in-depth from 1993 to 2009. The first research base consists of 112 sourcing case histories (mainly in the area of IT) studied longitudinally from 1990 to 2001. These are described in Lacity and Willcocks (2001) *Global IT Outsourcing: In Search of Business Advantage* (Wiley). The second is a study of relationships through seven case histories. This appears in Kern and Willcocks (2001) *The Relationship Advantage* (OUP, Oxford). The third is a 2001–2005 longitudinal study of business process outsourcing practices, with a particular focus on four cases in aerospace and insurance. See Willcocks and Lacity (2006) *Global Sourcing of Business and IT Services* (Palgrave, London).

The study also draws upon a fourth research stream consisting of 10 cases of application service provision, published in Kern, Lacity and Willcocks (2002) *Netsourcing: Renting Business Applications and Services Over a Network* (Prentice Hall, New York).

A further research stream analysed vendor capabilities, including innovation, and is represented in Feeny, Lacity and Willcocks (2005) Taking the Measure of Outsourcing Providers, *Sloan Management Review,* 46 (3). A further five outsourcing surveys were carried out in USA, Europe and Australasia in 1993, 1997, 2000, 2001 and 2002 covering multiple sectors and over 900 organisations. Another research stream, by Sara Cullen, assessed 100 ITO/BPO initiatives of a variety of business functions during the decade 1994–2003 to determine what worked and what did not work, what drove the various degrees of success and failure, and the emerging lessons. The research is represented in Cullen and Willcocks (2004) *Intelligent IT Outsourcing* (Butterworth) and Cullen, Seddon and Willcocks (2005) *Managing Outsourcing: The Lifecycle Imperative MISQ Executive, 4(1).* This study uses the findings from the 2006–09 research undertaken into offshoring and business process outsourcing. This covers multiple case studies and is represented in Lacity and Willcocks (2009) *Information Systems and Outsourcing: Studies in Theory and Practice* (Palgrave), Oshri, Kotlarsky and Willcocks (2008) *Outsourcing Global Services* (Palgrave), Kotlarsky, Oshri and Van Fenema (2008) *Knowledge Processes in Globally Distributed Contexts* (Palgrave) and Willcocks and Lacity (2009) *The Practice of Outsourcing: From ITO to BPO and Offshoring* (Palgrave).

Combined, this work forms a 1,000 plus case research base held by researchers at LSE, Melbourne and Missouri, St. Louis Universities. (Including survey work, the research base represents data from 1,900 plus organisations.) The cases are in-depth and longitudinal (i.e. studied qualitatively and quantitatively), in some cases over three generations of outsourcing. The research base covers all major economic and government sectors, including financial services, energy and utilities, defence and aerospace, retail, telecoms and IT, oil, transportation, central, state and local government, health care, industrial products and chemicals, and is drawn from medium, large and multinational organisations based in Europe, USA and Asia Pacific.

7. About the authors

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8. Conclusion

A key finding of this report is that the non-BRIC countries investigated are creating new and profitable outsourcing and offshoring opportunities, capable of development and exploitation even in recessionary times. Their ability to deliver on the opportunities and deal with the related challenges will serve as a foundation for moving further up the value chain; for example, in some cases from mainly call centre work to software development and effective R&D. IT and skilled labour shortages in client and supplier companies in Western Europe, North America and BRIC countries represent both real opportunities and a set of strong challenges to non-BRIC countries. They point to the need for long-term strategy and investment in education and training, together with attractive employment conditions to draw in and retain skilled labour.

The larger issues of environment, risk and legal conformity are driven and policed by governments, and this determines the levels of confidence that businesses have in making investments. The non-BRIC countries that have provided stable economic and political environments are attracting more complex and longer-term offshoring and outsourcing contracts. The current findings show that a major trend toward non-BRIC locations exists, but is being driven primarily by regional rather than global customers, with nearshoring becoming a notable market phenomenon. This is likely to increase in the current recession as the time convenience, cultural fit, skills, language accessibility, and niche market compatibilities become more sought after and more widely known.

Egypt needs time and further investment to build on increasingly solid foundations and to deliver on its considerable promise. Egypt's attention to investment, strategy and focus is paying off and is creating the right environment for offshoring and outsourcing business to grow. In terms of attractiveness, the country has already scored highly on cost, skills and market potential. It has further room for improvements in environment, risk and infrastructure. In each of these categories, the government has put in place new strategies and prioritisations to address the gaps. The impact of these will take time to show. For Egypt, one of the areas for development is the encouragement of start-ups and the development of its own small local businesses to fill the gaps, to provide specialist expertise and to offer new services.

A key opportunity identified in this report is the growth of the policy of establishing 'captives' overseas. This has been driven by a need to mitigate corporate risk by not having all work undertaken in any one country. All non-BRIC countries stand to benefit from this policy. Egypt has already made a substantial start in this market. How it and other non-BRIC countries build on their foundations is yet to be seen. The signs are favourable, and the opportunities large but challenging.

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