Where will shared services go next?

In choosing a new location for global service delivery deployment, shared services leaders literally have a world of options. While emerging markets with low labor costs receive considerable attention, established locations offshore, near-shore, and even onshore still provide compelling opportunities to support the business. Location decisions today are driven by more than labor-cost arbitrage opportunities, with critical operating factors, risk appetites, and corporate growth strategies also coming into play. A company should additionally weigh its ability to drive efficiencies across the organization and to provide value-added services to the business. With these considerations in mind, we present our views on some hot topics in global service delivery deployment to help executives better frame their thinking about where their shared services centers (SSCs) could go next.

Offshore: Do the rewards outweigh the risks?

Our view	Reports of the death of shared services offshoring have been greatly exaggerated, and are probably outdated. Even though rising costs were speculated to erode their cost advantages, labor-cost arbitrage opportunities continue to exist in some of the most established locations, such as India and the Philippines. Although wages may have risen in recent years, these increases, by and large, have not been prohibitive and companies are still benefitting from substantial wage differentials. Similar concerns about deficits in labor availability and quality have demonstrated to be manageable when companies perform proper analysis and market entry planning. The combined value of accessing a labor supply that is low-cost, productive, and dependable can swing a location decision past concerns about natural disasters, political upheaval, and economic instability — factors that might otherwise cause them to eschew an offshoring strategy. Additionally, pioneering locations continue to pique interest, but fewer companies have been willing to tackle the perceived drawbacks that often intersect with blazing a trail in an emerging, and largely unproven, market. This is particularly the case with companies that are newer to shared services and alternative delivery. These hurdles, which can be both genuine and merely assumed, include shallower talent pools, access constraints, inadequate infrastructure, and higher risk of business disruption (e.g., political, social, economic, safety, and natural disaster). Lastly, there are some cases in which companies have consolidated their operations to locations with higher market costs, but they were still able to achieve positive returns on their investments due to productive talent pools, the resulting efficiencies and systematic improvements gained through shared services, and dogged management focus on getting it right.
Commentary	• Despite rising wages in some established locations, labor-cost arbitrage opportunities remain broad. The scale below, which has been developed based on our field experience, provides a relative sense of labor-cost differentials for non-IT business processes. Excluding pioneering locations, if the U.S. is 100, then: – Philippines is approximately 20-25 – Malaysia is generally in the 30s-40s – Excluding Brazil, most of Latin America (LATAM) is in the 40-60 range – Central and Eastern Europe is in the 50-60 range – India is about 20-25

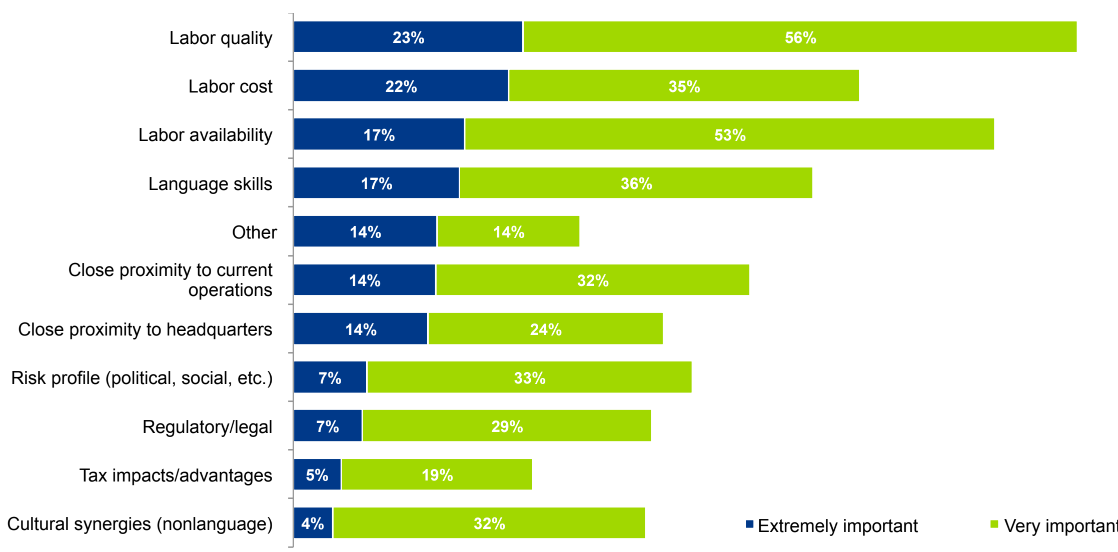
1 Education Indicators in Focus — "How is the global talent pool changing?" May 2012 http://www.oecd.org/edu/50495363.pdf

Commentary (cont.)

- In a number of established locations, governments and universities have begun to implement programs to enhance the skills of the local labor force for language training and back-office proficiency, thus enhancing their long-term potential. Universities in India, for example, still produce more English-speaking college grads than most.[1] Some emerging locations are also taking similar steps to improve their competitiveness. Examples of governments with strong, coordinated efforts to develop a pipeline of talent for attracting SSCs include:
  - Established: Philippines, Costa Rica, Ireland, Poland, and Malaysia
  - Emerging: China, Uruguay, and Colombia
- Selecting not only a suitable country, but also the optimal metropolitan area and appropriate sub-market within it, is critical for endeavoring to provide access to the applicable talent. In our experience, the variance of costs and conditions among cities within the same country can be greater than between countries.
- Taking measures to gain "employer of choice" status is becoming even more critical around the globe. Beyond offering competitive benefits and wages these measures include aligning the human resources and facility strategies with the local culture. For example, family and work environments are closely related in many countries, including India and the Philippines. Accordingly, effective shared services operations in these locations sponsor weekend activities, such as showing movies at the office, for workers and their families. Relationships matter strongly as well. For instance, if a manager leaves his or her job in India, it's common for employees to follow that individual, staying more loyal to the relationship with the manager than to the employer.
- Many offshore emerging locations are evolving in their capabilities and support structures. Some now possess experienced managers and leaders, well-trained and more available labor, stronger local infrastructures, and more favorable and supportive government policies. This ongoing maturation can make it easier to implement shared services than in the past.

Even if the price is right — location decisions are based on more than cost

What were the most important factors in selecting the organization's current SSC location(s)?



Source: Deloitte's 2013 Global Shared Services Survey

Near-shore — Can proximity be gained at lower cost?

Our view	"Near-shoring" is commonly defined as the transfer of business or technology processes to a country that shares a border with, or is close to, the company's home country, with the objective of leveraging the benefits of proximity. These benefits can range from the operational convenience of easy travel to the center, to similar time zones and languages. Some companies also find strategic value in deploying under a regional model, assuaging internal political pressure, and minimizing change by not moving too far, too fast. Near-shoring is often narrowly used in the context of companies headquartered in a mature market , such as the U.S. or Western Europe (e.g., England or Germany). Location strategy is a global consideration, with companies today serving global markets through a network of operations extending throughout the world. This network typically includes regional headquarters, sales and marketing offices, distribution and service operations, manufacturing, and retail. Accordingly, many effective organizations today are pursuing service delivery strategies that align their global markets and operations to regional shared services hubs. Oftentimes this strategy will have a near-shore component to it. For instance, a U.S.-headquartered multinational company may go elsewhere in North America or to Central America to support its North American operations. Regardless, location decisions concerning proximity should take into account both critical short- and long-term operating objectives — and not be based solely on cost.
Commentary	• Near-shoring can serve several purposes: – Language alignment – Cultural alignment – Change management – Proximity to critical operations – Minimal time-zone variances – Travel and logistics – Familiar, reasonable cost – Market entry • Examples of near-shoring, often implemented as part of a regional-hub deployment strategy, include: – Central/Eastern Europe serving Western Europe • Regional language flexibility • Approximately 30-50% cost savings[2] • Growing market opportunity • Minimal time-zone differences – Southeast Asia serving Asia • Regional language flexibility • Little to no cost savings, unless a majority of the processes are migrating from higher cost locations (e.g., Japan, Korea, or Singapore) • Growing market opportunity • Minimal time-zone differences

2 Based on Deloitte project experience.

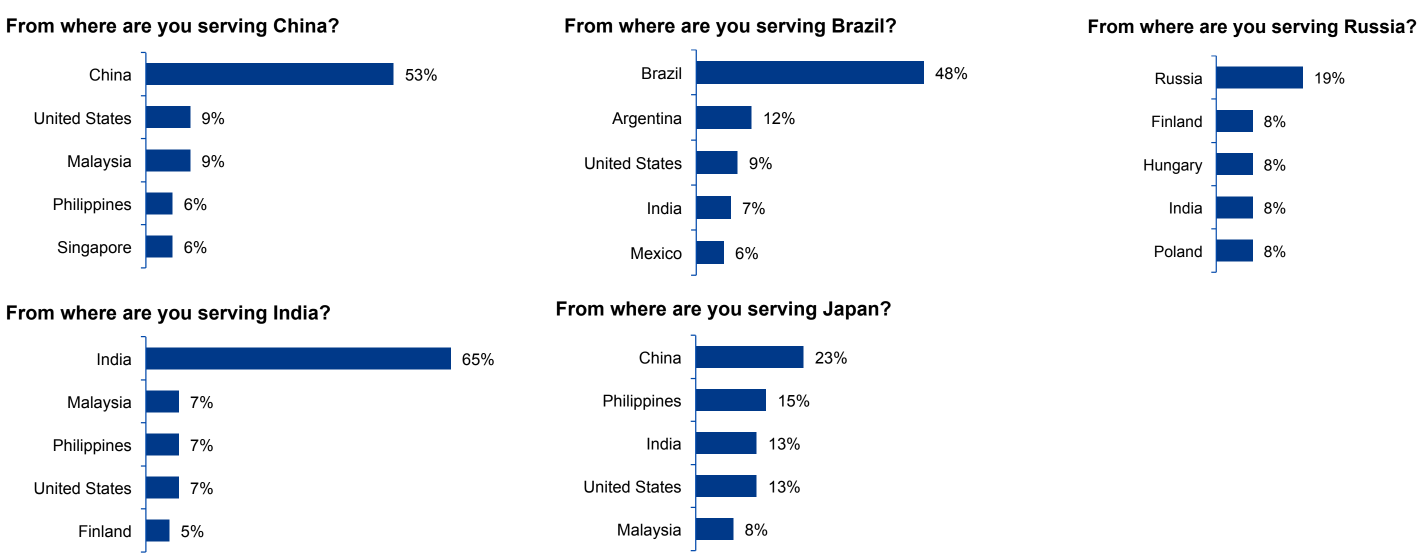
Commentary (cont.)

- Latin America serving Latin America
  - Spanish language, limited Portuguese
  - Accent clarity
  - Cultural alignment
  - Little to no cost savings, unless a majority of processes are migrating from higher cost locations (e.g. Brazil and Chile)
  - Growing market opportunity
  - Minimal time-zone differences
- Latin America serving all of the Americas
  - Language access (Spanish, English, and limited Portuguese)
  - Cultural alignment
  - Approximately 40-60% cost savings, as compared to U.S. operations
  - Minimal time-zone differences

- A few nations are difficult to serve via a regional hub. Brazil, Russia, India and China (the BRIC countries) and Japan stand prominent. These countries are large markets within themselves; therefore, many companies already have substantial, existing operations within them. In addition, the political power wielded by their company country leaders often requires these nations to be served by some form of shared services operation located within their borders. Even when it is politically possible to serve these nations from elsewhere, language access constraints, regulatory requirements and protectionist policies often make it uneconomic or less feasible to do so, even from a near-shore location. However, facing the costs and complexity of operating from within these countries, companies find creative approaches for servicing the countries from outside of the country.

Some countries are more likely to be served from the inside out

From where are your SSCs providing services for China, India, Brazil, Japan, and Russia?



Source: Deloitte's 2013 Global Shared Services Survey

Onshore — Is this the time for the U.S.?

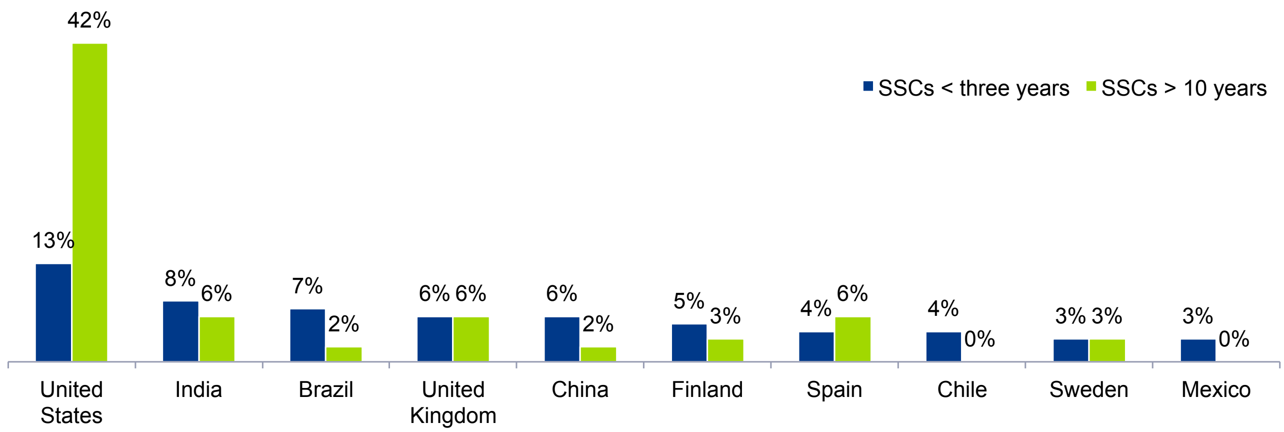
Our view	Onshore is still a common strategy for companies in several mature, established locations, including the U.S. There have been occasional media stories about American companies that have brought offshore operations back to the U.S. These stories have been the subject of recurrent debate within shared services circles. Are they based on facts or are they anecdotal? Do they indicate a trend? It's hard to conclude based on a handful of these reports that offshoring does not work or that the U.S. is now the "right" choice for shared services operations. The decision to move shared services operations away from the U.S. is often made in the context of larger global alternative delivery strategies, and it is typically driven by labor-cost savings and market entry and expansion goals. But pursuing these goals may also come with tradeoffs: the need to deal with substantially more risks, while managing distant operations in less familiar and often challenging business and operating environments. Some companies are willing to accept these trade-offs in order to realize the cost savings and strategic benefits; some are not. Despite media reports to the contrary, this has normally been the case. The U.S. today still remains an onshore consideration and it is often the applicable choice for some U.S. companies, especially those with headquarters and administrative operations in higher cost metro areas. For them, smaller U.S. metropolitan areas can be very attractive, offering capable talent pools, safer political and business environments, minimal risks, 25-35% lower costs,[3] and opportunities to "employ American."
Commentary	• The U.S. is a desirable location for implementing shared services for many companies. • Wage arbitrage of 30% or more may be realized[4] by moving processes from high-cost large metro areas to mid-sized and/or central ones. – If the U.S. average is 100, then several coastal cities are in the 120-130+ range (e.g., New York, Los Angeles, San Francisco, Boston, and Washington, DC) – Several options at or below 100 can be found, particularly in Central and Southern states – Reducing tenure and re-marking salaries to market can further reduce labor costs • Larger "household name" companies may have recruiting advantages in these markets, with employer-of-choice strategies providing a further edge. • Onshoring can be particularly appropriate when the vast majority of a company's "global" presence is based in the U.S. • Business units may be reluctant at first to support sending processes offshore, especially the more complex and higher value ones. One tactic for gaining their support is to use the U.S. as an initial step for shared services, later moving offshore after the processes are effective, efficiencies are demonstrated, and the organization is aligned. • Despite its importance, cost isn't the only consideration in the location decision. Many factors come into play that can affect a company's willingness or reluctance to send work offshore. These include economic/political stability, intellectual property risk, currency stability, taxes, regulatory familiarity, perceived talent quality, and language clarity.

3 Based on Deloitte project experience.

4 Based on Deloitte project experience.

The U.S. is still home to a high-quality deal of activity — How have the locations of SSCs shifted over time?

Top 10 locations of SSCs three years or younger



Source: Deloitte's 2013 Global Shared Services Survey

Closing comments

Geography is an essential element in achieving the objectives of a company's shared services strategy and operations. Regional and global "hub and spoke" deployments are now becoming standard. But when it comes to choosing a location, don't rely on hearsay. Many of the old stand-bys still have a lot to offer; pioneering locations hold promise; and onshore opportunities may exist in one's own backyard. Each location strategy, however, has a distinct balance of risks and rewards. Understanding the trade-offs involved is critical and so is weighing them against the individual priorities of each organization. Whether journeying to new lands offshore, near-shore or onshore, companies should investigate the risks, rewards, and priorities of the topography before setting out.

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