



**EXECUTIVE FORUM ON
NATIONAL EXPORT STRATEGIES**

**EXPORT OF SERVICES: HYPE OF HIGH POTENTIAL?
IMPLICATIONS FOR STRATEGY- MAKERS**

**5-8 October 2005
Montreux, Switzerland**

**Exporting Information and Communication
Technology Services**

**A paper contributed by
Emma V. Teodoro
IT Services
Philippine Exporters' Confederation Inc.
Philippines**

EXPORTING INFORMATION AND COMMUNICATION TECHNOLOGY SERVICES

The past five years show a dramatic increase in the export of Information and Communication Technology services worldwide. Feeling the pressure to lower down costs of providing ICT services, many multinationals have opted to use less expensive manpower available in some developing countries. The approach is not brand new nor is it innovative. This strategy has been considered by many leaders for quite some time. However, it is only during the past few years that it has gained exponential popularity. This phenomenon may be because companies have no other choice but to outsource to stay competitive.

I. ICT Services Offered For Export

The most commonly offered ICT services for export are in the areas of:

- Business and Technical Consultancy;
- Software Development and Maintenance;
- Technical Support or Help Desk;
- Call Centre;
- Data Conversion and Transcription;
- Web Development and Maintenance;
- Business Process Outsourcing;
- Animation;
- ICT Training; and
- Other IT-Enabled Services.

These services are offered for outsourcing mainly because of factors like abundant supply of highly educated, English speaking, highly trainable manpower resources and low cost of telecommunication facilities. In addition to this, many governments have offered incentives so that companies will find outsourcing their ICT service requirements more attractive. Such incentives include income tax holidays and free importation of hardware and software. In some cases, real estate locations are also provided for free.

II. Facilities

There are basic facilities needed for outsourcing of ICT services. These are mainly the following:

- Hardware;
- Software;
- Network;
- Telecommunications;
- Office Facilities; and
- Disaster Recovery Facilities.

In general, the total investment per workstation is \$ 5,000 - \$10,000 depending on the volume and the nature of outsourcing job needed. Generating investments to set up such facilities could be quite attractive to developing countries.

Hardware

The cost of hardware has been going down. Only a few years ago, what would have been a mainframe is now a workstation PC. This trend contributes to the popularity of outsourcing ICT services. It is now cost effective to set up hardware infrastructure at another site, which can be connected to the other servers of the organization.

In general, the hardware requirements for outsourcing ICT services would be servers, workstations, peripherals and network infrastructure all generally available from multiple vendors.

Software

Software seems to be a more limiting factor than hardware in setting up ICT outsourcing infrastructure. The costs of software for servers, workstations, project management, development tools and applications, among others, continue to be quite high depending on the requirements of the client. On the other hand, software vendors may offer licensing agreements that will ride with existing agreements with outsourcing companies.

Network

Networking is a must. Computers are now interconnected and it will not be feasible to undertake outsourcing jobs without interconnecting facilities with each other. Requirements include hardware such as routers, network administration tools, cabling and wireless access gateways.

Telecommunications

The age of internet has contributed a great deal in making telecommunications facilities widely available. Thousands of internet service providers have set the environment for wider usage of telecommunications thereby resulting to lowering of costs. This comes during the time when several countries have deregulated their telecommunications industry, thus, resulting to abundant supply of bandwidth and healthy competition.

However, even with the lowering of telecommunications cost, this factor could still pose a considerable amount of investment in setting up outsourcing facilities. One time costs include acquisition of switch and PABXs, modems, load balancer and fail over switches, converters, among others. Recurring costs are the monthly fees to carrier/s.

Telecommunication infrastructure may be set up as dedicated leased line for 24-hour, 365 days a year requirements or as internet service for email, upload and download of files or even for system development and testing. Dial up facilities may be set up on a case-to-case basis if volume of work is not large or is quite intermittent. The bandwidth required depends on number of workers and the size of the files to be worked on. For example, animation may require very high bandwidth but may not need 24x7 availability. On the other hand, software development does not require a very wide band but may require facilities to be up most of the time.

Video conferencing facilities make outsourcing infrastructure complete. Being very useful for meetings and conducting of offshore training, video conferencing has become a regular part of outsourcing.

Office Facilities

Office facilities needed for ICT outsourcing are standard. These may include furniture and fixtures, raised flooring, air conditioning, uninterrupted power supply, generator, rooms for training, meeting, presentation and video conference. In addition, security is a major consideration.

Disaster Recovery

Client confidence is very important in ICT outsourcing. Therefore, outsourcing companies need to define its disaster recovery plan and provide for back up sites and infrastructure.

Training Requirements

ICT outsourcing is about people. Therefore, training plays an important role in setting up projects. Training may be needed to provide general or technical skills, client-specific skills, project management skills and operations and maintenance capability. The modes of training may be in-house or external, self-paced or computer –based.

III. Outsourcing Options

When deciding on a path to take, companies that do not have experience or manpower to define their action plans may opt to hire the services of outsourcing consultants. In many cases, such consultants may have experienced several outsourcing implementations; thus, they may be able to recommend approaches to a successful outsourcing strategy. Some of these are:

- Contracting;
- Cost Centre or Subsidiary; and
- Joint Venture.

Contracting

In the seventies up to the eighties, outsourcing of ICT services started with specific projects that had well-defined set of deliverables. Usually, these are either new systems development projects or conversion projects. With such projects, the deliverables for the different phases of software development life cycle have to be defined and documented with great amount of clarity to ensure success. Opting for an arms length approach to the team, management preferred to look for appropriate offshore vendors from which they choose their contractor.

This approach had definite advantage as it was faster to implement and did not require top management approval. Being a tactical approach, the level of MIS head or application owner was sufficient to push for the project. Furthermore, this approach was easy to manage from a risk standpoint, as the budget would be limited to the contracting amount especially if a fixed price project was agreed upon by both vendor and company. The disadvantage of this approach is that the organization would not be able to assimilate the experience and consequently, the knowledge that such an approach would generate. In addition, the organization would not gain from long term benefit should outsourcing be successful for them.

From the vendor perspective, the advantage of contracting arrangements is the independence that the vendor has from the client. As such, the vendor gains both from a revenue standpoint as well as from more technical and management depth derived from project experience. An added plus is that the vendor will be able to use the project as part of its reference in the future. The risk of the vendor is cost overruns in a fixed price if project gets delayed. Poor estimation may lead to considerable losses and dissatisfied clients. There are also risks of resources being on slack due to projects being stopped in the middle or waiting for new projects to start. Poor project estimation and slack are two major causes of losses in the ICT business.

Cost Centre or Subsidiary

In the eighties, there were some groups such as Andersen Consulting and James Martin & Associates that strategically formed their cost centre or subsidiary offshore. As such, these set up are backed up by deep pocket support and enjoy the prestige of their mother companies. Many of these organizations also provided services to their local markets and did not exclusively focus on offshore services. Since then, many of these organizations have reengineered their operations and may have a different outsourcing model now.

The advantage of setting up cost centres or subsidiaries is that this will be completely under the control of the head office. It will be much easier to follow standards and processes that are currently being practiced. There will be no reinventing of the wheels and the learning curve within the new organization is much faster.

The revenues of such operations are normally computed based on transfer rates within the organization. The head organization enjoys a certain margin between actual billing to end client and the revenue transferred to offshore facilities.

Joint Venture

Joint venture would require a lot of groundwork to implement. First, there is a need to undertake due diligence by parties involved. Each party puts on the table its contribution and shows how it is going to help make the joint venture a success. The relationship of the parties is important. If

there has been previous relationship between parties, due diligence and defining the joint venture agreement may not be a stumbling block in developing the joint venture.

Requiring some legal paperwork, joint venture partners have to agree on the following: type of relationship, capitalization, equity distribution, rules that both parties will abide to, management structure, hiring policies, fiscal management, among others. Once threshed out, joint venture arrangements may provide the best of both worlds for parties involved. As a separate entity, the joint venture company develops its own identity without losing its relationship with its principals.

IV. Philippine Scenario

The Philippines was one of the major users of IT in the late 60s and early 70s. In addition to this, the official language of the country has been English since American occupation.

With this background, the Philippines became a major source of IT skills in the world and started to provide offshore ICT services to US, European and Asian clients starting in the early 80s. During this period, telecommunication cost was one of the major costs of offshore projects but strategically, the Philippine government with pressures from the private sector, deregulated telecommunications industry in the early 90s. Since then, telecommunication cost has gone down dramatically paving the way for nation-wide installation of internet infrastructures by more than 200 Internet Service Providers.

More than 2.5 million tertiary level student population and an annual graduate of more than 700,000 make the Philippines a good source of highly trainable manpower resources. However, in the 80s, many schools started to use Filipino in teaching major subject areas thereby affecting the English proficiency level of graduates. Human resources development is now one of the major challenges faced by the government and private sector alike.

The solutions that are being implemented to improve the quality of manpower are:

- The shifting back to English in teaching most of the major subjects in schools;
- Industry-academe partnerships;
- Establishment of several English language training institutions;
- Introduction of competency-based training and other measures to enhance employment readiness;
- Establishment of a National Certification Program for ICT Professionals;
- Extension of training of ICT professionals to business and management; and
- Development of community e-centres to push ICT training and capability to the municipality level.

In additional to expanding the manpower development programs of the country, the country has to build more ICT centres. This is being addressed by large real estate developers in the Philippines such as Ayala Land, Inc., SM Realty, Filinvest, etc. and would result to more than 400,000 square meters of additional space for ICT business use in the near future.

To strengthen ICT industry players in the Philippines, the following moves have been initiated:

- Promote use of quality standards;
- Collaboration among industry players;
- Build and operate shared development centres for SMEs;
- Promote strategic partnerships with foreign companies;
- Development and implementation of a strategic marketing communications program;
- Creation of incubation program to support start-ups;
- Provide financing opportunities to small ICT enterprises;
- Promote investments in ICT business;
- Develop and implement a broad-based Intellectual Property Rights campaign; and

- Inclusion of Data Privacy Act, Anti-Cyber Crime Act, amendments in the Labor Code and Government Procurement as part of legislative agenda.

With these initiatives, the country aims to create additional one million ICT jobs by 2010.

V. Summary

In summary, different types of ICT services have been discussed. Facilities needed for outsourcing were enumerated and various models used to export ICT services presented. The advantages and disadvantages of setting up cost centres, organizing subsidiaries or subcontracting, and joint ventures were explored. The challenges facing the Philippines ICT business are discussed and strategies adopted to develop ICT business in the country are presented.