

Future Bangalores? The increasing role of Central and Eastern Europe in offshoring services

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GÁL Z. Future Bangalores? The increasing role of Central and Eastern Europe (CEE) in offshoring services, *Regional Studies*. The paper gives an overview of offshoring services into Central and Eastern Europe. Many Eastern European countries invigorated by EU enlargement became important locations for offshore service centres. Building on the region's nearshoring advantages such as geographical-cultural proximity and on its multilingual graduate supply, CEE is likely to utilise more value added and quality-driven services. Trade statistics support the assumption that an expanding export in other business and ICT services has been associated with offshoring services in the NMS. Empirical findings suggest that offshoring services have a significant impact on their locations. The paper reveals the role of offshoring activities in the metropolitan transformation and their growing significance in local and regional development.

Keywords: offshoring, nearshoring, service trade, Central and Eastern Europe, offshoring locations,

JEL classification: F21, F23, L8, R12

„A new round of globalization is sending upscale jobs offshore” (Business Week, 2003)

„Offshoring is a matter of global access to intellectual capital.

In the end, companies will go to low-cost countries

for the people, not for the costs” (CEO of a global TNC)

„New contenders in Central and Eastern Europe

outshine more established offshoring locations” (AT Kearney, 2007)

INTRODUCTION

The key feature of the second global shift is the offshoring of a range of service functions from the USA and Europe to low cost developing countries. Improvements in communication technology helping companies in moving services across international borders has dramatically increased the ability of companies to source production anywhere in the world (global sourcing). The relative price-drop of services, especially those found in the ICT sectors, together with the recent liberalisation of trade is facilitating the spatial fragmentation of value chains alongside the services functions. Offshoring is regarded in the literature as one of the most important globalisation forces. Thomas FRIEDMAN (2005) in his latest book describes offshoring among the major “flatteners” of the technological, economic and social shifts that has effectively levelled the economic world, and “accidentally made Beijing, Bangalore and Bethesda next-door neighbours”. As Friedman argues transportation and communication costs, as well as geographic proximity to customers, workers and suppliers have become less important for many service tasks. A global, internet-enabled platform for various forms of sharing knowledge and tasks in services, irrespective of time, distance, geography has created the flat World. Nevertheless, the world remains far from flat and proximity and geographical factors still matter a great deal for many service tasks, because their exchange requires face-to-face proximity between partners.

The rapid surge of globalisation, opening up of formerly isolated regions such as Eastern Europe, Russia and China to global trade, has substantially boosted task trade and service related cross-border investment. Many Eastern European countries invigorated by the EU enlargement became important locations for offshoring services. The question is whether these locations might stand as a challenge for the overwhelmingly dominant global position of India and the other East Asian countries or only offer a complementary offshoring base for the continental European companies preferring to relocate their services nearby. There is a large amount of anecdotal information underpinned by the recent estimates of consultancy reports, which views the CEE as an attractive region for offshoring even in a global context. Its leading cities are now seen by some analysts as “future Bangalores” in terms of providing offshoring solutions.

This paper attempts to confirm the recent anecdotal evidence by means of using trade and specific location site data in order to overcome the scarcity of consistent empirical contributions in measuring the actual significance of CEE offshoring services. Research on this topic is limited due to the lack of appropriate data while the available data can be used to define offshoring only with certain restrictions. For instance, FDI data can be indecisive because, just like the invested amount, the cost of services investment (e.g. set up of a shared services centre), is minimal. The employment figures of offshoring projects, if they were available, would allow international comparison. The service export data adopted from the

Balance of Payment statistics gives a good approximation to identify those sections of service trade, which can be regarded as offshorable.

The paper is divided into four sections. Following the introduction, the first section puts offshoring into the wider context of the economic literature in order to prove that offshoring processes involve not only restructuring the organisational base and geographical accessibility of firms but also can be interpreted as the key factor constituting the latest phase of globalisation. The second section gives an overview of the international market for offshoring services. The third explores the reasons behind the growing popularity of the CEE as an offshoring hub, examining the service trade trends and the comparative advantages of the East European region. The last section emphasises the impact of offshoring on the local urban network, while the conclusion discusses the sustainability of the region's attractiveness and comparative advantages.

THE SECOND GLOBAL SHIFT IN SERVICES – OFFSHORING IS A NEW PARADIGM OF GLOBALISATION

The fragmentation of production processes across distances, national borders – like globalisation – is not an entirely new phenomenon but advances in ICT have accelerated this trend and enabled inroads to the tradable and commoditised services.¹ It goes along with the growing internationalisation and large-scale spatial dispersion of production and service networks. Service sector offshoring is a geographically determined process of the contemporary global production system as it creates dynamic spatial interactions between different – notably the global, the regional, the national and the local – geographical scales (JONES and KIERZKOWSKI, 1990, 2005).

However, these production processes have not always been so flexible and 'footloose' in terms of the spatial levels of their operation. Service sectors such as manufacturing were previously mostly exempt from the spatial and organisational fragmentation in the past. Economic activities during the various stages of the two centuries long modernization process produced much differentiated geographies.

In the age of Adam Smith, transportation was costly and therefore the fragmentation of production activities in remote locations was difficult and uneconomical. For the subsequent two centuries, the economic geography as GROSSMAN and ROSSI-HANSBERG (2006) argue was characterised by agglomeration in production rather than fragmentation, and specialisation required geographic concentration. This resulted in the geographic clustering of production and population, although the increasingly cheap transport costs did not necessitate performing production close to consumption. Countries specialised in making goods from start to finish participated in the world economy with the exchange of different complete goods and fostered the rapid expansion of international trade. This period was characterised

by the rapid industrial concentration in the North and southern deindustrialisation (BALDWIN, 2006).

In the last three decades the rapidly decreasing communication and co-ordination costs have fostered the end of the need to perform most manufacturing stages near to each other. The lower cost of transport and information generated a rapid industrialisation in the South. The emergence of Southern industrialisation forced a relative deindustrialisation in the North resulting in a steady shift to services away from industry and as parallel geographical separation of various production stages became more attractive. TNCs in the North started to offshore almost all labour intensive stages of production to low cost developing countries creating a transnational network of affiliates. This was the first global shift associated with relocation of manufacturing employment to low-cost production sites (BALDWIN, 2006). As communication technologies have weakened the link between specialisation and geographic concentration, the separation of tasks in time and space became possible. This second shift of globalisation 'spatially unpacked' the factories and offices from each other and concentrated on the services sector. The relocation of mostly routine tasks and functions rather than sectors became more common. New "trade in task" paradigms developed by GROSSMAN and ROSSI-HANSBERG (2006) shown in Fig. 1. called this process fragmentation. Advances in this process have made it easier for companies to disaggregate their value chains around the globe, all the while maintaining management control over them, or to disperse service production among numerous supplier firms even in distant locations. This is contrary to the earlier stages of globalisation when specialisation required geographic concentration and agglomeration forces prevailed (BALDWIN and KRUGMAN, 2004).

Fig. 1. *Tasks trade: Grossman and Rossi –Hansberg theorem*

Offshoring became a key globalization force and one can argue it is the next industrial revolution or the latest phase of globalisation, which has been challenging the traditional territorial division of labour (BLINDER, 2006). The interaction between organizational and geographical dimensions of national/international/transnational production networks created complex structures in which elements of both concentration and dispersal are apparent. The new economic geography (NEG), focusing on the spatial concentration of economic activities, has been challenged by global fragmentation, which means the geographical spread and decentralization of service activities. Changes in organisation and IT reduced the difficulties of coordinating services from a distance by enabling firms more easily to fragment their production stages. The fragmentation requires infrastructure and service production capacity in distant places, where foreign direct investment can facilitate the process of decentralization. It means the relocation to the host country of all or part of the service production as the companies can benefit from the various alternative locations endowed with

specific local resource based advantages. Some service activities are not fixed in space and can be provided either as a form of foreign trade or by the temporary relocation of a service worker to a client's premises. Other specialist services can be provided only from central locations (BRYSON, 2007).

Today neither the comparative advantage nor the traditional NEG approaches are seem to be adequate to explain the territorial dimension of fragmentation. Service value chains became increasingly offshorable not just within but also across regional economies, which opened up new territorially embedded systems of core service functions challenging obsolete industrial districts by their dispersed global networks. Fragmentation is not simply spatial dispersion in a certain sense but fragmentation means that external linkages interpenetrate the territorially embedded value chains not only in manufacturing but in services, diminishing the home bias even for the core service operation (GROSSMAN and ROSSI-HANSBERG 2007; BALDWIN 2006).

Outsourcing and offshoring² are both regarded as means to reduce costs and also can be seen as the expression of corporate strategies to distribute risks across a number of service providers and different locations. However, offshoring and outsourcing may be associated with a different landscape wherein the former reinforce local-regional growth and the latter reinforce productive efficacy of the global network at the expense of local economic prosperity. In this sense, 'offshoring is more consistent with the NEG supporting regional economic growth, while outsourcing relies on extensive inter-regional growth challenges, the NEG and, in particular the claimed necessity that networks of production and exchange need to be local to create value between network partners' (CLARK and FREEMAN, 2008).

The reason behind the creation of global value chains during the stages of the first and the second global shift also differ from each other (see Table 1). Along with the stages of development associated with the global shifts, the nature of FDI has also changed. Traditionally investments seek access to natural resources, production and market building, while recently services increased their share within FDI (DICKEN, 2003). As argued by METTERS and VERMA (2008) offshoring is not a new phenomenon as it has been applied to the relocation of isolated stages of labour intensive manufacturing to low-wage developing countries in the form of vertical direct investment during the first global shift. What is new now is its application to knowledge intensive business and financial services. However, recently horizontal investment gains importance as strong flows of FDI across countries are motivated not only by low cost benefits but also by the avoidance of exchange risks, quality labour, and by the quest for proximity advantages with a direct local presence (BRÄUNINGER, 2007). Global service providers can locate their units to take advantage of geographical variation of production costs at global scale. In other words, transnational vertical specialisation and integration became feasible, in which different tasks of a service firm's value chain are located in the different parts of the world (BRYSON, 2007).

Table 1. Offshoring is not a new phenomenon: the first and the second global shifts

Offshoring has a strong impact on deciding what kind of jobs are being offshored and what the main differentiating factors are from the earlier wave of relocations. While earlier mainly blue-collar jobs were offshorable, recently a variety of skill-intensive and cross-sectoral white-collar jobs have played a key role in this process. The geography of the second global shift is strongly determined by the educational and language abilities of the service workers located in low cost locations (BRYSON, 2007). Earlier routine tasks were relocated to low wage developing countries and more recently even the core, more skill-intensive core functions became offshorable to new locations of the emerging countries. The second global shift in services offers benefits for countries at both ends of this process and participants can reap the benefits of the new global division of labour by this shift. The receiving countries gain jobs, technology, skills and access to global markets, while the investor countries save costs and improve their competitiveness as they can move into higher value added activities

The driving forces behind the new wave of offshoring are not simply low wages, but increased electronic tradability, lower capital intensity and reduced cost of service relocation, which makes easier to transfer of services to a wider varieties of locations across the globe. Another argument in the literature is that relocation of manufacturing during the first global shift tended to be more geographically embedded as affiliates built stronger links to the local suppliers and markets, while service relocation can be regarded as more footloose (JONES and KIERZKOWSKY, 1990, 2000; ARNT and KIERZKOWSKY, 2001).

Although separating tasks alongside the entire value chain in time and space, (geographic) proximity as HILLBERRY and HUMMELS (2008) argue still matters a great deal for many tasks. While some tasks can be undertaken easily from a large distance, others require more face-to-face contact. It greatly depends on the type of tasks (routine or non-routine) and their information content³. This resonates to GROTE and TÄUBE's (2007) argument in which proximity requirement selects between the different organisational and spatial forms of reorganisation of value chains and it can be a selection tool between the core and non-core activities. The option of outsourcing certain stages of business tasks and offshoring part of the value chain abroad depends largely on the embeddedness of certain functions in relation to their internal corporate structure and to their corresponding locations abroad. They distinguish different kinds of proximities (spatial, organisational, cultural and professional) necessary for the transfer of information and knowledge in financial services⁴.

THE INTERNATIONAL MARKET OF OFFSHORING SERVICES

There are a large number of consultancy reports on service offshoring and each provides rather different estimates of the size and its impact on employment. A study by McKinsey indicates that approximately 35 percent of the work that could potentially be offshored, worth

\$110-120 billion and divided equally between IT services and business processes, actually will be offshored by 2010 (McKINSEY, 2005). The significance of offshoring is often overestimated and this is because still only a small proportion of services are transferred abroad. In fact, offshoring is by no means as important as one might expect from the rapid surge in FDI data and the ongoing political debate on job losses. The offshore outsourcing market is also limited as most outsourcing remains a predominantly domestic affair and only a small share of service outsourcing is international.⁵ According to an IMF study based on trade data of the eight highly developed countries, the share of imported intermediate goods and services (known as offshoring intensity) is about 10 per cent of total intermediate goods and services (AMITI and WEI, 2005a). Service offshoring is even more underdeveloped. The ratio of imported intermediates to gross outputs of industrial products rose from 6 per cent to 10 per cent between 1980 and 2003, whereas the ratio in services was still only 1 per cent in 2003. However, the growth rate for offshoring intensity of services was much higher than in the industry (8.4 per cent to 1.3 per cent since 1990) such as the labour productivity generated by service offshoring.

Offshoring is a key driver of geographically re-engineering corporate value chains as relocation of certain service activities requires the geographical reorganization of firms' value chains by choosing among a number of locations. There are a number of factors at play, and these must be considered when drafting a successful offshoring strategy. Besides the lowest cost, other factors have to be taken into account such as hidden costs and the higher risks of a low cost environment that might drive firms to select other more quality based locations. The "closer to home or closer to expansion" strategies are applied when TNCs prefer the establishment of sub-centres nearshore or close to the geographical direction of their future market expansion. Nearshoring just like offshoring is not a new phenomenon. Many US-based companies had been using their relatively lower cost 'offshoring backyards' of Canada and Ireland for many years until India became the dominant player at a global scale. Nearshoring means sourcing service activities to a foreign, lower-wage country that is relatively close in distance or time zone and often within the same continent. The customer expects to benefit from one or more of the following constructs of proximity: geographic, cultural, linguistic, economic, political, or historical linkages⁶.

Nowadays location strategies of companies in global sourcing shift towards the multiple sourcing strategy creating 'global footprints' to improve performance and spread risks among a number of locations and collaborating partners, creating a global quality labour pool. In most cases larger TNCs have developed a global delivery model based on "blended delivery systems" that 'capitalise on the place-based advantages of coupling or blending activities located in a variety of different locations: home–near–far' in order to reduce their dependency on any single location or region. In this context, different territories are in competition as much as firms (BRYSON, 2007).

AN EMERGING OFFSHORING HUB: CENTRAL AND EASTERN EUROPE

The following section explores the reasons behind the growing popularity of CEE as an offshore destination. It tries to measure the region's significance in offshoring examining the trade data to find evidence of offshoring related service intensity, and finally explore advantages of East European locations compared to their Asian counterparts.

Even as most US and UK companies turn to India to relocate many of their service outsourcing jobs, over the last decade a growing number of outsourcing services seekers from Western Europe have found Bangalores in their own backyard; countries in the CEE region, particularly Czech Republic, Hungary, Poland, Romania, Bulgaria, Russia and Ukraine. With the advent of a new generation of service offshoring, major companies after targeting India and its Asian companions as the prime destinations for offshoring technology and call-centre jobs, are now looking towards Eastern Europe to meet their nearshoring requirements.

What are the main driving factors behind the rise of the nearshoring boom in CEE? First, it can be partly explained by external factors, namely by the growth demand and new business strategy direction encouraging more and more European companies to gain benefits of service offshoring. This demand met the increasing supply from the CEE countries wanting to benefit from the new wave of FDI shift to services and they are positioning themselves as ideal nearshore locations. Until the early 2000s, offshoring was almost exclusively 'reserved' for the Anglo-Saxon world with limited opportunities for Japanese, French and German companies. As offshoring services has become part of the mainstream strategy, many of the European companies need service centres that can operate in European languages. As Indian locations cannot support operation in languages other than English, therefore German, French and Scandinavian countries are looking to gain the benefits through relocation to their nearshore East European locations. They require services in their own languages and tend to demand a higher degree of cultural embeddedness, especially in their customer facing activities.

Another driver of nearshore growth is the expansion of offshoring towards new types of services. Not only has the list of offshoring functions grown steadily embracing core competencies, analytical work and more complex customer related services but also these new higher-value functions require more interactions based on language skills, cultural understanding and geographical proximity that only nearshore locations can provide.

The third driver of nearshoring is the rise of the global service delivery model, which creates a pool of global labour located in a large number of service centres around the globe in order to optimise global operation of service.

Countries in Central and Eastern Europe are gaining importance as offshoring locations, although the significance of CEE in the offshoring market is not that big as is suggested by the media. In 2003 CEE with its 1Bn USD share in the global offshoring market (worth to 40 Bn USD) lagged far behind the more prominent locations and the share of the region in the

global business offshoring services was as low as 1 per cent (McKINSEY, 2006). Nevertheless, the share of CEE is rapidly growing as in 2003 only 5 per cent of service-related global FDI projects invested there, while in 2006, 22 per cent of FDI project went to the region.⁷ A.T. KEARNEY (2007) consultancy firm created an index of the most attractive countries for offshoring based on costs (financial attractiveness), economic and political environment (business environment) and human resources (skills availability). As expected India came out on top and more countries from CEE were also in the top quarter. Business process offshoring began to take off in Hungary, Czech Republic and Poland from 1998 driven primarily by the improving investment climate, the development of modern office markets and the cheap labour supply. As the most advanced CEE countries catch up with their western neighbours, nearly all improved their absolute score, although losing ground while emerging locations moved up in ranking. Despite the continued environment improvement in the most established nearshore locations, all fell in rankings of relative cost competitiveness. Once the regional champion Czech Republic (4th place globally in 2004) fell 12 places back by 2007 and Bulgaria replaced it as the only country from the CEE region in the top 10. Besides the Czech Republic, Hungary dropped in ranking because of rising wages and other costs allowing new contenders in the region to outshine these earlier established locations.

New locations, such as Romania, Slovakia, the Baltic States and Bulgaria have emerged since the Millennium⁸. Central and Eastern Europe is still an attractive supplier for European corporations. During the first stage of service offshoring, captives in the form of shared service centres were the main service providers, and recently independent global vendors are also opening their new centres in CEE to serve their European clients.

Considering the shortcomings in different statistical sources, the indecisive evidence of the consultancy reports and the lack of a commonly accepted definition of offshoring, this paper uses trade data derived from the Balance of Payment statistics. This gives a good approximation to identify the trends in those sections of service trade, which can be regarded as offshorable and helps to identify the geographical direction of contemporary relocation processes within the region, and it also highlights the shifts in county level performances in attracting offshored services. Following the international methodology (OECD, 2004; UNCTAD, 2005; AMITI and WEI, 2005b; GHIBUTIU and POLADIAN, 2008; SASS, 2009) two services categories are suitable to approximate the size of trade in offshorable services.⁹ Information and computer technology services (ICT) and other business services (OBS) are the most inclusive categories that can be regarded as potentially offshorable services.¹⁰

The question is whether the data support the widely accepted view that new member states (NMS) are increasingly affected by the relocation or outsourced provision of offshorable services. The tradability revolution in services has resulted in a rapid surge of locational transfers in service activities. The NMS of the EU have achieved enormous progress in modernizing their service industries and from the Millennium have witnessed a rapid shift towards services.¹¹ FDI plays an important role in offshoring, although it is more difficult to

quantify it, and services trade data provide a more reliable source of measurement. Export services data in the case of the six new EU member states (NMS-6) included in this study provide more proxy to define the extent of offshoring services.¹² Exports in services in NMS-6 expanding from a very low base amounting to 63 billion Euro by 2007, which is almost 3 times higher than that in 1996. The share of the NMS-6 in the global service export is still modest (2.8 per cent) illustrating the still lower export services capabilities of the region although its growth rate is higher than the global or the EU-15 average. In absolute terms, shown in Fig. 2, Poland, Czech Republic and Hungary are the leaders in this field.

Fig. 2. Exports of services in the NMS-6 in 1996 and 2007 (EUR Bn)

When looking at the sectoral composition of service exports in comparison with West European countries, the still lower share of other services (including offshoring-sensitive business services) is striking and this means that the higher share of traditional branches of services (travel, transport) reflects the pattern of economic transition.

It is widely accepted that offshoring services means the global sourcing of business and IT services from abroad therefore to find further evidence of offshoring related service development, export data on the so called “offshorable services”, namely on the other business and ICT services can be collected for NMS-6 using the Eurostat database. The increased tradability of these sub-categories is more visible in the patterns of services trade and their export/sales intensity is the largest among services (SASS, 2009). The share of offshorable services within total service exports steadily grew from 16 per cent to 24.2 per cent between 1997 and 2007¹³. The total value of offshorable services in the NMS-6 was equal to 15.3 billion Euro in 2007 and within this aggregate the overwhelming dominance of business services (85 per cent in average) is striking. In absolute term, Poland and Hungary are the largest traders followed by the Czech Republic and Romania (Fig.3.).

Fig.3. Exports of offshorable services and its sectoral composition in 2002 and 2007 (EUR Bn)

The growth rate of offshorable service export increased the most dynamically (by the average of 20 per cent) within the service sector as a whole and Romania, Poland and Hungary experienced the highest growth between 2002 and 2007 (Fig. 4). Due to the rapid growth of offshorable service exports over the period of 2002-2007, in combination with the slower expansion of imports the deficits decreased steadily and this resulted in development of net trade gains amounting to 800 million Euro (2007) in NMS-6. Hungary reached its export surplus by 2004, earlier than other neighbouring countries. Poland reduced its trade

deficits more rapidly, and turned it into small surplus, while Romania achieved the highest surplus by 2007 (800 million) within the shortest period (Fig. 5.).

Fig. 4. Average annual growth rates of different export sectors in NMS-6, between 2002 and 2007 (%)

Fig. 5. Net trade in offshorable services in the NMS-6 in 2002, 2005 and 2007 (EUR Bn)

Service trade statistics are supportive of the preliminary assumption that offshoring generated expanding exports in particular service categories and a large proportion of business export services in the NMS has been associated with offshoring. However, it is obvious that not all this kind of trade is provided by offshored services. These data do not show how much of the offshorable service exports really provided by offshored service centres and do not distinguish between the different organisational forms of offshore outsourcing and captive offshoring at the same time.

Due to the methodological constraints, quantitative data alone are not suitable to reveal the complexity of offshoring services. Besides findings based on statistical data there are qualitative approaches to define the comparative advantages of regions which arise from the combination of geographical, organisational and cultural proximity to Western Europe. It can be argued that the attractiveness of CEE is based on talent and geography, rather than on low wages and a vast labour pool. Three groups of apparently important capabilities drive the nearshoring advantages of CEE.

First, these countries have close geographical, political and cultural ties with Western Europe that allows proficiency in clients' languages. The advantages of EU membership not only diminished the external risks but dramatically simplified the administration cost as well. CEE as a nearshoring location scores high marks because of its lower cost for communication between the customer and service provider. Nearshoring locations not only reduce costs and risks of working with distant foreign companies but also simplify personal contacts. The directness of communications and common cultural understandings have always been important cultural elements of successful interactions. Besides close proximity that may improve the efficiency of day-to-day information exchange to a service provider, nearshoring allows companies to develop intimate working relations. Being in the same time zone is a huge advantage especially if projects require frequent travelling demands and also CEE is particularly interesting for companies who require voice and customer-facing services in their mother languages¹⁴ (MEYER, 2006).

Second, the comparative advantages of CEE still to a large extent lie in the wage differences as cost savings are still one of the most important motives for offshoring. In CEE, labour costs are 40 to 60 percent lower than in Western Europe, although it varies largely

within the region. Hungary, the Czech Republic and Poland have the highest average salaries while, Romania and Slovak Republic have relatively lower average salary levels (ECONOMIST, 2005). Comparative advantages in wages between countries and regions can change relatively fast, although CEE will remain relatively cheap for the near future. Ultimately, no low-cost country can remain low-cost forever. Most of the CEE countries are not among the cheapest locations and outpace those of the low-cost Asian countries. As costs in the most advanced CEE countries converge towards EU levels, companies are moving farther East in their search for high-skill and low-cost solutions (Russia, Ukraine, and Turkey).

Third, much has been said about the quality of labour in the region which consists of a highly educated, well-trained and motivated workforce, achieving a high degree of productivity and flexibility. In total, CEE produces a much lower number of university graduates than its large Asian counterparts. However, the CEE graduates turn out to be far more suitable to work for TNCs. According to the McKinsey survey job candidates from CEE had higher suitability rate (around 50 per cent on average, whereas 80 per cent in developed countries) across all occupations than their Asian or Latin American counterparts (McKINSEY, 2005). While the technical universities have maintained their quality standard the share of science and engineering graduates is lower than Indian or West European averages, which in turn is diminishing the region's capability to specialise in IT or sciences-based service provision.

A few studies have tried to estimate the impact of Eastern European nearshoring locations on the global market and on the largest global players, such as India. India emerged as the "destination of choice" for offshore delivery of almost all kind of IT and business processes, and as a leading destination in terms of market share as well as the depth of services work, it cannot be easily challenged. India will remain the leader in global sourcing and CEE provides a much smaller scale of different factors facilitating service sourcing from there.

There are several reasons, listed in Table 2, besides size why CEE countries cannot outpace India's potential. Firstly, companies from the US and UK are still the leading purchasers of offshoring services while the continental countries of Europe generate a larger demand towards the CEE countries but are responsible only for 20 per cent of all European offshoring expenditure (MEYER, 2007). However, compared with other trade flows the quantitative significance of offshorable services and IT services in particular, is still lower than in India. In India 78 per cent of total export services are produced by ICT and other business services, while the corresponding figure for NMS-6 is 39 per cent. India has developed a massive net surplus position already since 1996, while only a few NMS have achieved net trade surplus in offshorable services (Fig.6a.). The average annual growth rate of offshorable export services in India between 2002-2007 amounted 29.6 per cent, while the corresponding rate was 19.3 per cent in the NMS-6. India's leading role especially in ICT service provision is unquestionable. In India 56 per cent of the total offshorable export

services are ICT services (77 per cent in 2002), while the corresponding figure in NMS-6 is 15 per cent showing no strong export specialisation in IT (IMF BoP statistics, 2006, 2007). Consequently CEE plays more important role in business service provision, though Czech Republic and Romania show a relatively stronger specialization in IT services indicated by the above average share (21 per cent and 18 per cent respectively) of ICT export within offshorable services trade. The recently achieved positive trade balance in offshorable services at aggregate level of the NMS-6 is led mainly by the export increase in other business services (Fig. 6a-b.).

Table 2. Offshoring environments: India versus Central and Eastern Europe

CEE cannot compete with the vast supply of Indian university graduates. India's 380 universities and 11,200 higher education institutions produce 2.1 million graduates each year of which 350,000 are accounted for by IT graduates alone. Consequently, India has twice the labour supply in six selected professional occupational groups as Czech Republic, Poland, Hungary and Russia together and seven times as many calculating without Russia (McKINSEY, 2005).

*Fig. 6a. Net trade in other business services and ICT services in India in 1995-2006
(ECU/EUR Bn)*

*Fig. 6b. Net trade in other business services and ICT services in the NMS-6 as a group in
1996-2007 (Bn USD)*

Not only are most of East European offshore units smaller compared to their Indian or the Irish counterparts but also independent homegrown East European service vendors cannot be compared with the well-known Indian global players. However, there are hundreds of local providers, for example in the Russian IT sector, most of which has a small number of employees. These local vendors are only few years in business and most of the offshore projects are simply too large for them to undertake. The low level of government incentives, the bureaucratic environment and the lower level of office availability are similarly disadvantageous factors for the position of Central Europe. Despite its lagging behind, the comparative advantages of CEE in business offshoring services enabled it to attract new processes in customer-facing services and core business functions. A survey on specialisation shows that the region is best equipped to be a provider of more complex back-office processes and recently a shift is seen to R&D services. Nevertheless, more and more NMS are attracting

R&D based jobs, therefore IBM ranked these countries among the top 10 global destinations for IT and R&D sourcing in 2005.

These issues give enough reason to someone to argue that while the CEE is at best a niche cluster especially in business services, India is at the same time a volume cluster with the highest value in IT services. In addition, CEE is a regional player while India is a real global platform.

FUTURE BANGALORES? NEW GEOGRAPHIES OF EMERGING OFFSHORING LOCATIONS IN CEE

Offshoring can have benefits for the host market and generates changes within the service sector as a whole. It also can have the potentially positive effects on consumers of final services, and on producers using intermediate services in terms of better service provision and spillover effects. The following section examines the implications of offshoring for the home markets in CEE, and in particular assesses its impact on their locations and on the urban network.

What is the most likely impact of offshoring services on the home economies? GDP growth of nations largely depends on service innovation. Offshoring services gains a particular importance in the CEE countries after their EU accession as it helped to mitigate the fear of TNCs' outmigration in manufacturing and it substituted the decreasing share in manufacturing FDI by service investments. The offshoring of service tasks results in additional export-oriented capacities in services and increased productivity, which may result in spillovers to the local economy, thus accelerating growth and providing additional employment, higher wages and skills diffusions. Offshoring enables the host countries not only to shift towards higher value services also to create their local brands in knowledge intensive business services (SASS, 2008).

Besides the general home market effect, the process of selecting and opening new locations is similarly important as offshoring has a strong impact on the cities selected. A key reason to offshore is to save costs, and most discussions on cost revolve around wages at offshoring locations. This can be extremely misleading because it precludes several other operating costs — support staff salaries, cost impact of attrition, training, management costs and corporate overheads, real estate, communications and technology costs. These costs vary across cities, and can influence a company's decision to relocate there. Nevertheless, there is little doubt that not purely the cost saving is the primary driver of location selection.

Location strategy making is a multi-faceted process, with different indicators coming into play as the focus is narrowed from macro-regions to countries, cities, districts and finally individual property level. However, choosing a suitable location is not just a matter of selecting the right country. Nevertheless, companies searching for locations should first focus on defining their priorities in terms of countries (cost, skills, business environment, and

proximity) before ranking their specific locations. The country versus city approach is heavily dependent on the selection criteria and it is equally important to distinguish between some county and city-centric parameters of location sourcing. The legal system and business environment are more or less the same for all the cities in a country, the availability of raw manpower, infrastructure and risk are moderately similar within a country, while availability of university graduates, labour and real estate costs, and the maturity of the ecosystem in a particular offshoring location can be very different within a country. Employment costs differ widely among cities because of limited labour mobility and varying unemployment rates. Companies need to spend time to scrutinise the attractiveness of cities. They must consider various elements of cost, not just salaries and the specific skill sets that each city can provide. Locations that meet requirements for resource availability, quality and operational flexibility have to promote themselves to become preferred destinations. In choosing a city, companies need to focus less on low wages and more on the other endowments of candidate cities fulfilling their business needs.

Offshoring has given a new spur in metropolitan development as the EU has expanded eastwards. The subsequent stages of systemic transformation, global transformation characterised by the reintegration of the Central European capitals into the world-city network. Three capital cities of the region (Budapest, Prague, and Warsaw) entered successfully into the world city system with fully-fledged gateway functions in the 1990s. The metropolitan transformation accompanied by both the rapid deindustrialisation and expansion of services has resulted in the concentration of the high-level business and financial services into the capital cities (LUX, 2007). Simultaneously interactions and symbiotic competition emerged between the capital cities, as they have been competing for attracting investments and have aspiration for business centre function with significant international scope. EU accession, competitive infrastructure costs and strong education system as favourable preconditions supported the first group of capital cities, such as Prague, Budapest and Warsaw in the first wave of the offshoring boom, and they have been recently followed by Bucharest and Sofia due to the saturation of the forerunners (see Figure 7). These cities were the most successful to reposition themselves during the early stages of transition by exploiting their comparative advantages on global markets. At the beginning, costs (labour cost, real estate prices and facilities) were the most important driver in selecting these locations mostly for routine offshoring activities. However, these capitals have relatively higher wages compared to their Asian and Latin American counterparts. Nevertheless, cost differentials with Western Europe are still significant, making these cities still attractive for higher value added nearshore service activities.

The offshoring location survey conducted by JONES LANG LASALLE (2004) points out that CEE capitals are the clear winners in their quality-driven scenario based on quality labour supply and improving business environment. When labour quality is considered Budapest, Moscow, and to a smaller extent Prague and Warsaw rank highly by this index, though on the

labour supply side, they cannot compete with the Asian cities. Concerning the business environment Central European cities scored more highly than those in Asia, and Prague and Budapest proved to be more innovative environment than Warsaw at the beginning. In terms of real estate market Central European cities have the required transparency, although their office availability is lower than the market demand.

The list of the Top 50 outsourcing cities worldwide based on the THOLONS's survey (2007) includes 13 cities from CEE, although only Kraków and Brno are not capitals. Bucharest, Sofia, Kiev, Tallin and Moscow have already established locations in the eastern fringe of the region. The first wave of cities in the offshoring boom, including the first tier capital cities are beginning to become congested in terms of skilled labour and infrastructure, to the point that raises the opportunity for the second tier cities within and capitals in other countries. As seen, companies initially located in the first tier cities, pushing up costs and attrition rates as direct consequences of market saturation. The growing demand for new offshoring locations, as the more mature destinations saturated, gives an opportunity for governments and their investment agencies to attract further service investments and create high-valued jobs with the introduction of few policy changes. In terms of labour costs, especially Warsaw and lesser extent Budapest and Prague proved to be the most expensive locations. To find alternative locations in the midsize provincial cities and to tap their unexploited talent pool has become an increasingly important operational consideration. This makes the identification and accurate profiling of emerging tier-2 cities increasingly relevant. In Central Europe according to the survey conducted by the McKinsey, beyond the already established locations there are 40-50 provincial cities with universities appropriate to supply a highly skilled labour force. The fact that many university graduates do not live in major cities with international airline connections (key criteria for multinational companies seeking an offshoring location) and are unwilling to move provides possibilities for the creation of suitable service centres in lower rank cities. At least 35 of these Tier 3 cities with no offshoring activities considered as undiscovered locations (McKINSEY, 2006).

Similar to the shortcomings in county level statistical measurement there are also several methodological problems in identifying the territorial dimension, namely the geographical direction of offshoring. There are no existing comprehensive data, which would inform about the number of offshoring projects and about the location of service sourcing units. In most cases, the types and the employment figures of these service provision units are not accessible through official statistics.¹⁵ Therefore, in order to overcome at least partially these constraints, it needed to map the major offshoring projects, namely those captive offshoring and independent service (offshore outsourcing) centres, which created. Data sources provided by national investment agencies, consultancy firms and refined through web searches. As presented in the map (Fig. 7.), as many as 166 offshoring units divided by four sectors (business, financial ICT and R&D services), concentrated into 32 different locations, were collected.¹⁶

Obviously, the capital cities were the most important locations with the largest service centre concentration in Budapest, followed by Warsaw and Prague. Although this does not mirror the county level ranking as Poland ranked first (45 per cent) in terms of the number of projects, followed by the Czech Republic, Hungary and Romania with 25, 22 and 8.4 per cent, respectively. Examining the sectoral profiles Czech Republic shows a relatively stronger specialization in IT services which verified by the above average Czech share in ICT service trade. Numerous second tier cities, particularly in Poland, Czech Republic and Romania are emerging as popular offshoring destinations particularly in Finance & Accounting sourcing for the European market. Kraków is the frontrunner in this field and some of the other cities in the CEE that are prime locations for FAO are Bratislava, Prague, Budapest and Bucharest.¹⁷ Accenture, Hewitt, IBM, Diageo and others have their European services centres in these cities (McKINSEY, 2003).

Poland, with the largest potential supply of skilled labour and the availability of untapped provincial locations has developed the most extensive network of offshoring locations. Poland has not only larger labour force (with nearly half a million graduates annually) but also has more urban centres that can support large-scale operations and longer-term prospect, more so than any other countries in the region¹⁸. Besides Warsaw, Kraków and Wrocław the already established hotspots, Łódź, Poznań, Katowice and Gdańsk are among the emerging ones. Not only nations but cities also have an opportunity to promote their locations. Łódź, in Poland, among others, has undertaken such an investor promoter initiative, which has been helping to make the city a booming Business Process Outsourcing (BPO) hub (CAPIK, 2008). While second tier Polish cities have been attracting BPO investments from the late 1990s, BPO work has only recently found its way to the provincial locations in the Czech Republic. Cheaper regional university centres such as Pardubice, Hradec Kralove and Ostrava with higher unemployment and ready supply of lower cost graduates have started to attract cost-conscious call centres migrating out of Prague. Brno succeeded in establishing its own location brand even for core services (PTACEK, 2009).

Fig. 7. Geographical and sectoral breakdown of the major offshoring services sites in Central and Eastern Europe, 2007

However, Hungary once a forerunner in the establishment of service centres, opening its first location in 1999 has lost its leading position. Contrary to Poland, most of the projects have concentrated into the capital city of Budapest and government agency failed to channel most of the new investments towards the midsize cities. While service centres investment selected by the Polish and Czech agencies as a priority, the Hungarian agency received criticism concerning its marketing activity. As in other spheres of economic activity in Hungary Budapest dominates the offshorable service sectors. Apart from the traditional dominance of Budapest the underdeveloped office markets in the provincial cities is one of the main hindering factors. Companies do investigate provincial locations but invariably return to Budapest due to the lack of suitable offices.¹⁹ Alternative options to costly Budapest

tend to be crossborder, such as Bucharest or even Kyiv rather than Miskolc, Pécs or Debrecen. Most of the few provincial service centres are located nearby the eastern borders of Hungary taking the operators' intention for their future cross border expansion and easier labour hire into account²⁰.

In high-demand countries such as the Czech Republic, Poland and in a smaller scale in Hungary many outsourcing vendors are setting up smaller centres with less than 500 employees to avoid the risk associated with the maintenance of a large workforce. Additionally, a smaller workforce is more aligned to the smaller labour supply in tier-2 cities, which has the added benefits of lower labour and facilities costs that can more than offset any benefits of economics of scale in capital cities. More vendors maintain operations in both the capital city and secondary cities, as capital cities leveraged for higher-value work, while lower level processing accomplished in secondary locations that offer much lower costs and extremely low attrition sites (*Outsourcing in Poland*, 2006).

Cities with the right combination of location factors will be the winners in the future waves of offshorable service investments. Certain locations suffer from structural problems such as low labour supply, higher wages, lack of suitable office space or weaker language and technical skills, but companies are more likely to choose another location rather than leave the entire region. The challenge for individual cities will be to build their attractiveness and competitiveness by investing into their ICT infrastructure, education and business environment.

CONCLUSION

Offshoring became a key globalisation force and because of its strong geographical implication has been challenging the traditional division of territorial labour. Offshoring has been also a stimulus to develop CEE as an important destination for offshoring services. Several findings of the paper supported the view of consultancy estimates, which view CEE as an attractive region for offshoring even in a global context. Calculations based on trade statistics support the assumption that an expanding export in other business and ICT services has been associated with offshoring services in the new member states. Offshoring services has not only generated trade in services but also impinge on the positive effects on the dynamic growth of higher value-added 'offshorable services'. However, the share of the region in the global service trade associated with offshoring is still lower than is hinted by the media and superficial estimates.

The other question was whether these locations might stand as a challenge for the overwhelmingly dominant global position of India and the other East Asian countries or only offer complementary offshoring bases for the continental European companies preferring to relocate their services nearby. India will maintain its stronghold as a primary offshore

destination, although Central and Eastern Europe cannot compete with India in volumes and IT specialisation, it will remain also a preferred sourcing location for Western European companies in particular. The region seems to have the right ingredients, at the right time, to make for its attractiveness and transnational companies are ready to reap the benefits of these nearshoring locations. Central and Eastern Europe offers five primary advantages in which India cannot compete: cultural and geographical proximity to Western Europe, still competitive wages (especially if one can consider India's wage inflation), good educational standards reflected by the higher rate of graduates' suitability, low risk profile and reliable infrastructure. "What is unusual about Eastern and Central Europe is that their most advanced cities offer a potent mix of attributes that even Bangalore cannot rival: a highly educated, multilingual pool of talent in an increasingly affluent consumer market — all barely a stone's throw from its prime clients" (*The New York Times*, 30 April 2007).

Empirical findings suggest that offshoring services has a significant impact on location. The paper reveals the role of offshoring activities in the metropolitan transformation and its growing significance in local and regional development. The expansion towards the second and third tier city locations also gives further potential for offshoring expansion beyond the saturated and more expensive locations of capital cities. Offshoring also implies an important local and regional dimension, and individual cities facing challenges to strengthen their attractiveness by investing into their IT infrastructure, higher education and business environment. Adequate state promotion and local initiatives are required to encourage the spread of service provision centres across the regions, and in provincial cities, in particular.

Despite the fact that the service industry is the most promising opportunity for the CEE economies there are few threats concerning the region's future prospects as a major offshoring hub. It is not just steadily raising cost. The size of the talent pool is still limited in CEE and compared to India and the majority of the workforce still consists of young and inexperienced graduates. Another aspect of the problem is based simply on size. The population of the six largest Central European metropolitan areas is only equal to the population of the single Indian city of Mumbai. On the corporate side, local providers in CEE failed to establish their global presence on the map, because of their smaller size and fragmentation, and they are more attached to the local market instead of seeking out the global market. Another problem is the bureaucratic environment. However, the pressure to stay competitive is slowly forcing governments to remove bureaucratic barriers.

The question can be raised as to whether competitiveness can be sustained for a longer-term by proximity of the CEE to its customers. In fact, offshoring success is a somewhat temporary phenomenon. Comparative advantages currently enjoyed by an offshore destination may not predict the future. Wages tend to rise as countries climb up the development ladder, which erode the very reason for offshoring. Further growth may be influenced by worsening global and local macro-conditions due to the global slump and

future prospect of the region depends largely on government incentives and on the success of exploiting talent pools offered by provincial cities.

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Table 1. Offshoring is not a new phenomenon: the first and the second global shifts

First global shift (relocation of manufacturing jobs)	Second global shift (relocation of service tasks)
First wave in the 1980-90s	Since the Millennium: new wave
Blue collar jobs	White-collar jobs
Impacts by industry – manufacturing	Across sectors and across nations –service occupations
Transportation enabled	Internet enabled
Driven by wages	Driven by wages, new business concept, language, skills,

	technical training
High capital investment required	Lower capital requirement (proceeding faster)
Limited to particular manufacturing sectors	Potentially affects firms in all sectors
Geographically more embedded: stronger links to local suppliers	Geographically more footloose

Source: Edited by the author.

Table 2. Offshore environments: India versus Central and Eastern Europe

	Central & Eastern Europe	India
Advantages	Value player	Volume player
	Proximity to the European customers (nearshore locations)	Large global vendors
	Language skills in European languages	Proficiency in English, wide skills, experience
	Untapped locations choices	Large cities/talent pools
	Motivated, more suitable talent pool	Very low salaries
	Acceptance, common cultural understanding	Flexibility, determination
	CEE has a good potential for further growth	Strong IT specialisation
	Captive dominance	Strong third party vendors
	Specialisation in BPO and KPO (R&D)	Primary specialisation in IT
Disadvantages	Developing infrastructure	Poor infrastructure
	Higher labour cost	Wage escalation
	Government incentives	High attrition rate
	Innovativeness, flexibility	Languages, accent, cultural barriers
	Office availability	Office availability
	Smaller local vendors (with no global presence)	Far-shore, additional cost
	Bureaucratic environment	India is close to its peak (saturation)

Source: edited by the author

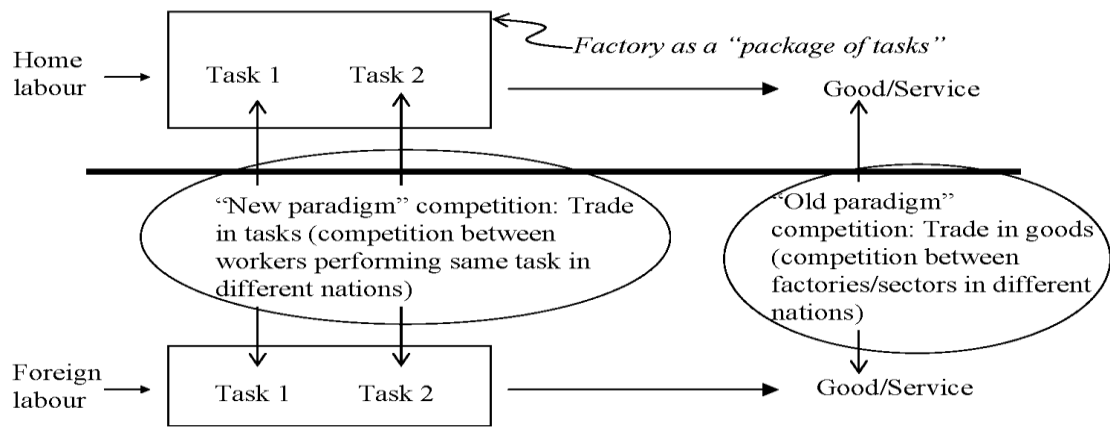


Fig. 1. *Tasks trade: Grossman and Rossi –Hansberg theorem*

Source: BALDWIN (2006)

Fig 2

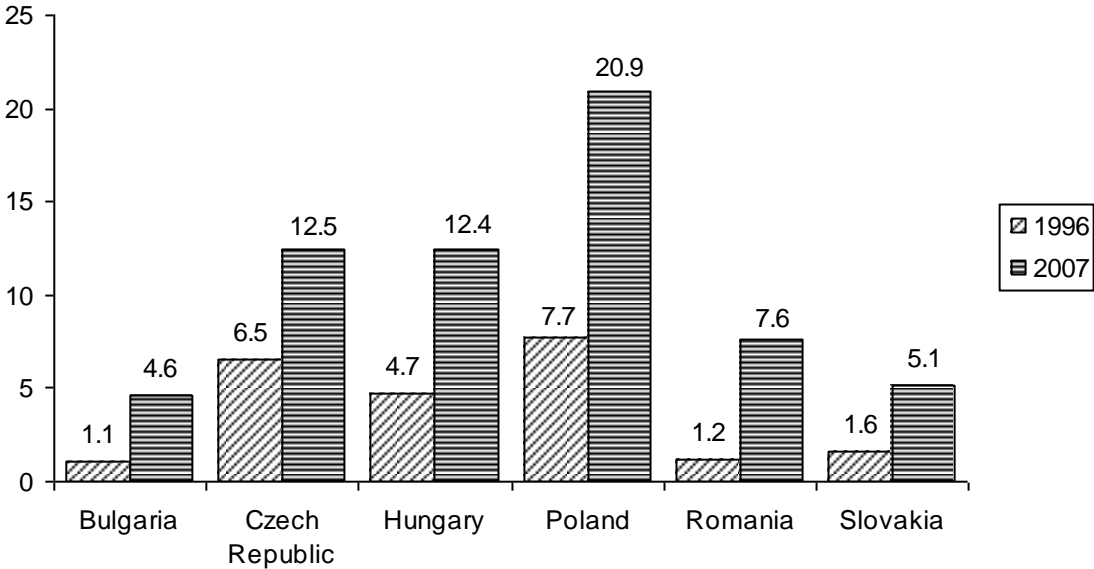


Fig. 2. Exports of services in the NMS-6 in 1996 and 2007 (EUR Bn)

Source: Author's calculation based on Eurostat and IMF BoP data

Fig 3

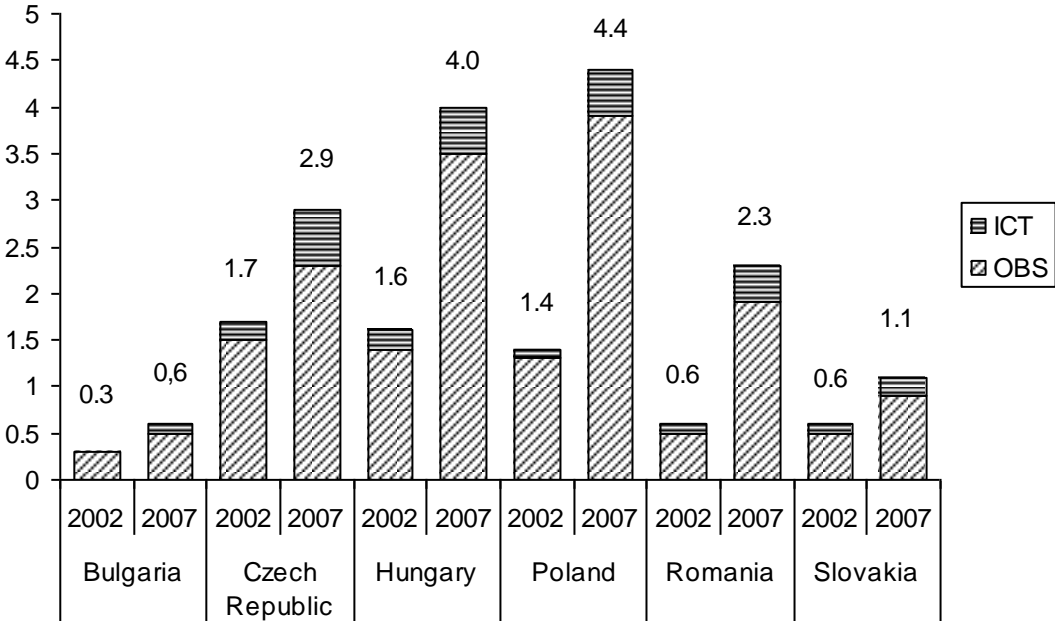


Fig.3. Exports of offshorable services and its sectoral composition in 2002 and 2007 (EUR Bn) ICT = Information and Communication Technology Services, OBS= Other Business Services

Source: Author's calculation based on Eurostat BoP data

Fig 4

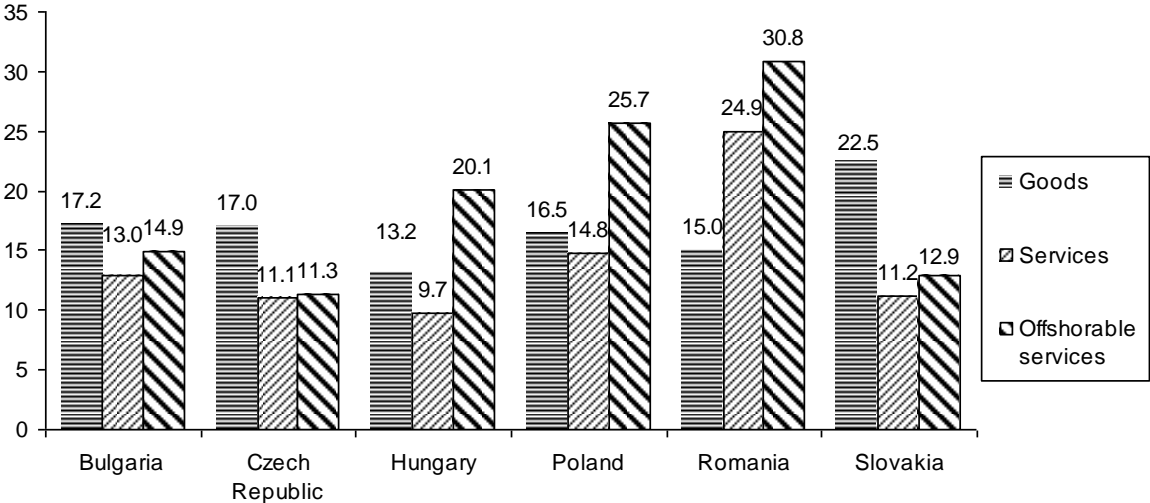


Fig. 4. Average annual growth rates of different export sectors in NMS-6, between 2002 and 2007 (%)

Source: Author's calculation based on Eurostat BoP data

Fig 5

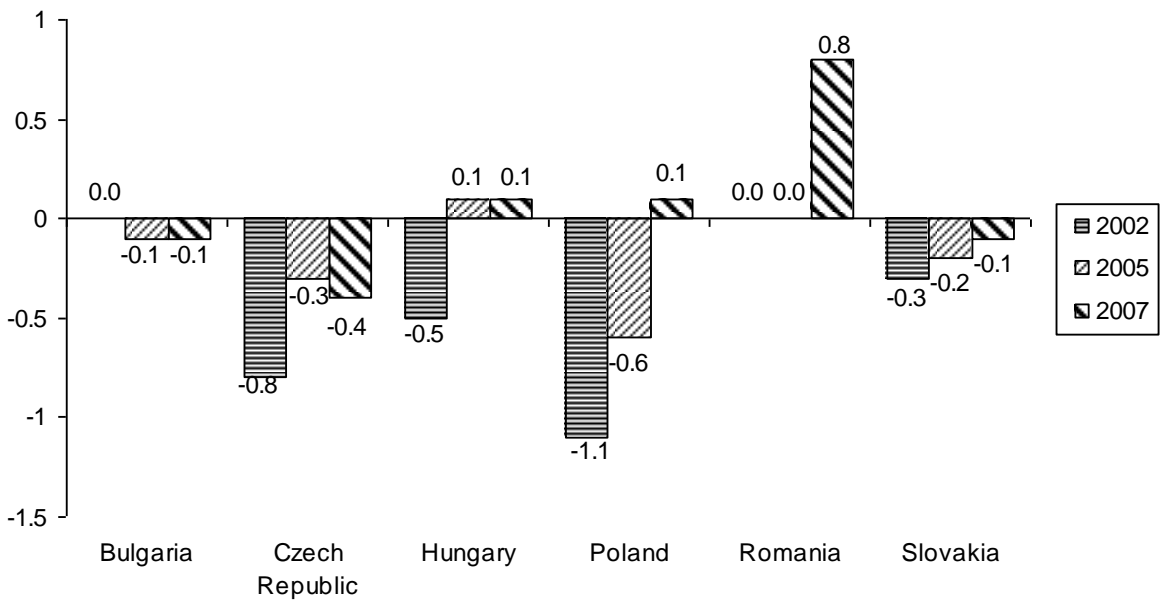


Fig. 5. Net trade in offshorable services in the NMS-6 in 2007 versus 2005 and 2002 (EUR Bn)

Source: Author's calculation based on Eurostat and IMF BoP data

Fig 6a

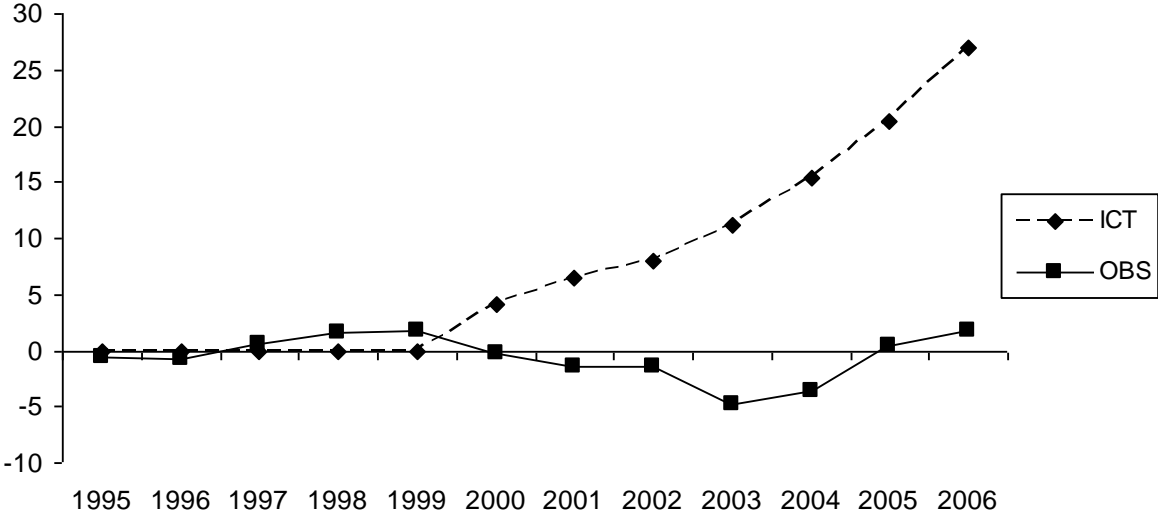


Fig. 6a. Net trade in other business services and ICT services in India in 1995-2006 (USD Bn)

Source: Author's calculation based on IMF BoP data

Fig 6b

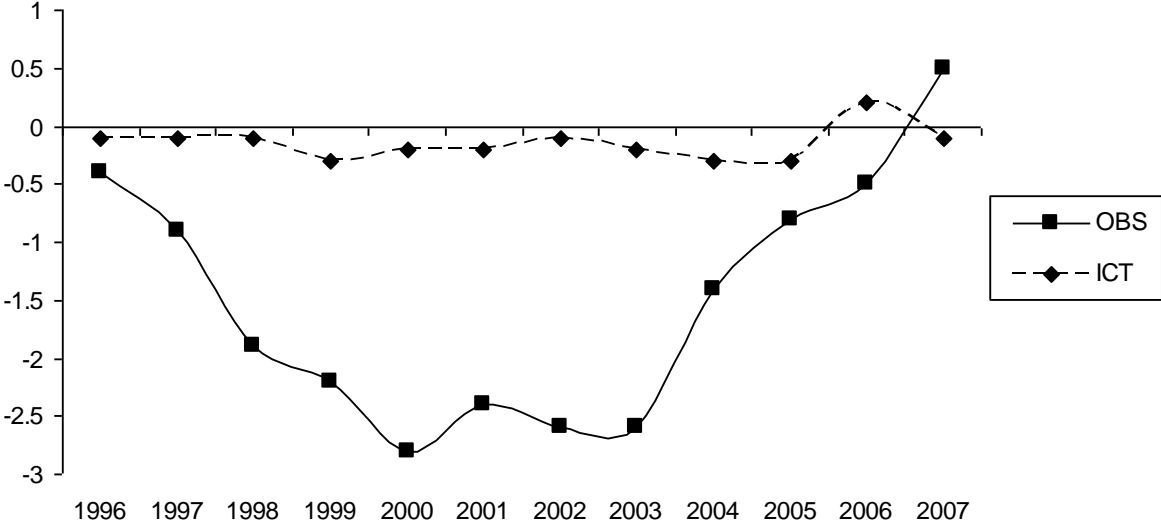
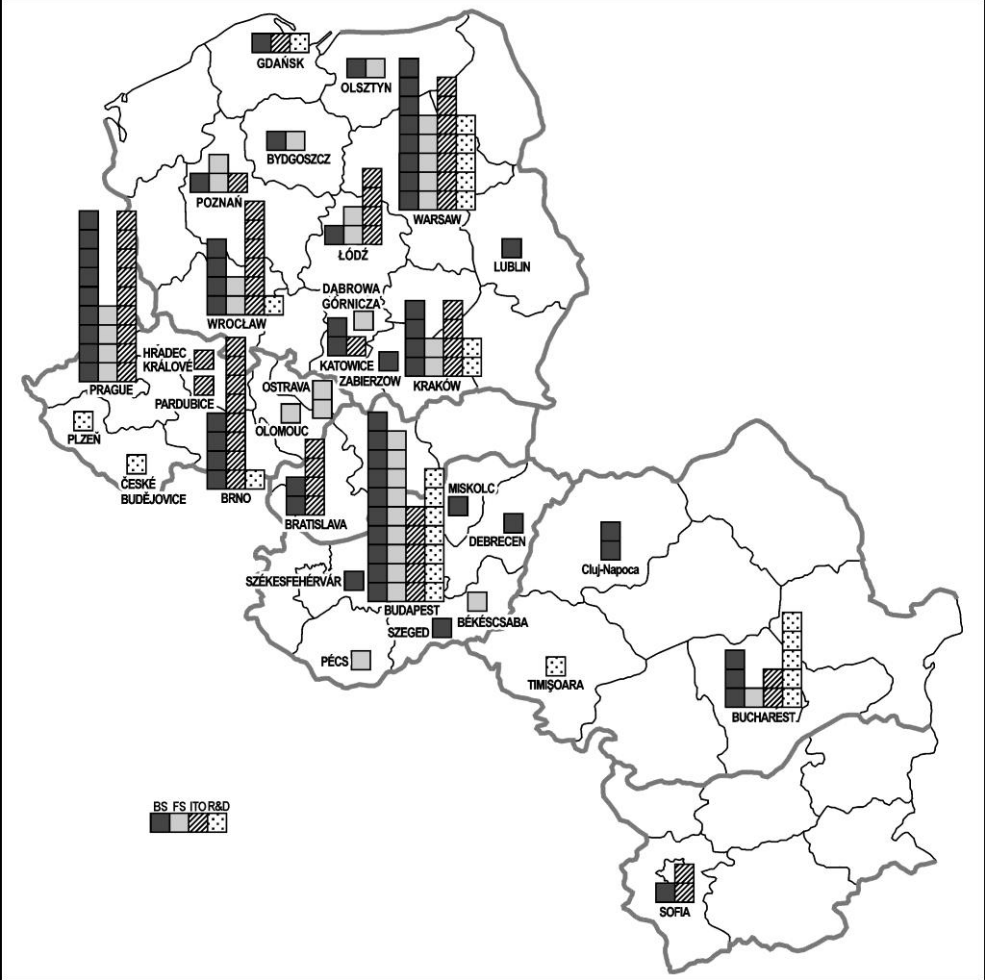


Fig. 6b. Net trade in other business services and ICT services in the NMS-6 as a group in 1996-2007 (ECU/EUR Bn)

Source: Author's calculation based on Eurostat and IMF BoP data

Fig.7.



Legend: BS=business services; FS= financial services; ITO= Information Technology outsourcing; R&D=Research and development, Knowledge process outsourcing; One box is equal with one offshoring unit (project).

Fig. 7. Geographical and sectoral breakdown of the major services offshoring sites in Central and Eastern Europe, 2007

Source: data collected by the author based on data of PAIiZ, Czechinvest, ITD-Hungary, DTZ and Deloitte (2007).

¹ Offshoring reflects the tradability revolution of services. Traditionally, most services were non-tradable and had even stronger proximity requirement regarding the geographical position of sellers and buyers. The original precondition of tradability is the use of ICT which allows knowledge to be standardised and digitized, allowing more and more services to fragment their different tasks into smaller components that can be located elsewhere to take the cost, quality and scale economies advantages of the particular location.

² Offshoring and outsourcing are often used as an interchangeable phenomenon, but they are different. While outsourcing is delegating an internal business process to an external company, offshoring means the geographical spread and decentralization of production of exchange through the transfer of activities from one site to another across national borders. Although offshoring can occur in combination with outsourcing (offshore outsourcing), this need not be the case (captive offshoring).

³ LEAMER AND STORPER's (2001) theorem has a strong implication for offshoring as only those services can be relocated which are based on routine cognitive processes, have high information content, are internet-enabled, require no face-to-face contacts and easy to set-up even in remote locations and easy to manage cross-nationally. Nevertheless, most personal services cannot be performed from a distance, while impersonal services such as the core tasks of financial services are liable to offshoring.

⁴ GROTE and TÄUBE's (2006, 2007) argue that outsourcing becomes an option only when organizational proximity is not necessary. When organizational proximity is needed, relocated units have to be fully owned subsidiaries. Moreover, the content of the processes to be outsourced ought not to be strategic to the outsourcing company. Offshoring of complex tasks

is also possible for parts of the value chain that do not require cultural and spatial proximity and where professional proximity ensures sufficient common background for communication.

⁵ The outsourcing market is close to 300 billion USD of which only 80 billion USD is subject to offshoring (XMG Report, 2007). With the current US\$1.2 trillion spend in outsourcing, only 6%, amounting to US\$77 billion, is being offshored and executed from global low cost geographies (THOLONS, Trends in Services Globalization 2008)

⁶ There is a considerable heterogeneity respecting the actual meaning of “offshoring”. It can be used simply to cover anything from ‘outside of country boundaries’ or ‘not domestic or not a border country’ to ‘remote lower cost locations’ or ‘outside of the continent’. In a more widely used interpretation, it refers to developing low cost countries that are located outside the First World (JAHNS et al., 2006). The geographic dimension of service locations refers to onsite (on the premises of the local company) and offsite (off the premises but in the same country) together forming the onshore alternatives, as well as nearshore (relocation of services abroad within a shorter distance, often in the same continent) and, finally, offshore or farshore (developing and emerging countries) options.

⁷ Survey by UNCTAD of over 1,800 service export-oriented FDI projects in 2002 and 2003 not surprisingly revealed India with its 12 per cent share to be the largest single recipient of projects such as call centres, shared service centres and IT services, with Asia as a whole being the largest regional hub with its 40 per cent share. These data also reveal that most export-oriented service projects are still concentrated in developed countries (51 per cent), although lower-cost locations are rapidly catching up. In the case of shared service centres, developing countries and CEE economies attracted 65 per cent of all export-oriented FDI service projects in 2002-2003 (UNCTAD WORLD INVESTMENT REPORT, 2004).

⁸ However, in 2006 Romania already attracted over 40 per cent of total Business Process Outsourcing (BPO) projects in the regions, which was higher than the corresponding Polish figure.

⁹ SASS (2009) explores several methodological problems related to the exact quantification of offshoring services, and stresses the difficulties in grouping those particular service categories which are affected by offshoring, partially because the NACE classification packs together offshorable and non-offshorable service categories..

¹⁰ As GHIBUTIU and POLADIAN (2008) pointed out, it is difficult to distinguish between offshorable and offshored service parts because not all service trade is related to offshoring, nor it is possible distinguish between affiliated and unaffiliated trade, or differentiate between captive and independent providers respectively.

¹¹ SASS (2009) expresses constraints of FDI data lie not only in their unreliability but also in their limited size in services compared to manufacturing investments. Moreover, the offshore outsourcing is usually less connected to FDI than to trade.

¹² Bulgaria, Czech Republic, Hungary, Poland, Romania, Slovakia

¹³ On country level some offshorable export shares increased even more between 2002 and 2007: Hungary from 20 per cent to 32 per cent, Romania from 24 per cent to 30 per cent and Poland from 13 per cent to 21 per cent.

¹⁴ In Eastern Europe, the share of German speaking graduates can be as high as the number of English speaking ones. (Nearly 40 per cent of schoolchildren learn German while 70 per cent of them English). Romania is particularly interesting destination for French companies as 85 per cent of schoolchildren learn French there.

¹⁵ An optional methodology to examine the attractiveness of an offshoring location is the employment in service centres. The lack of comprehensive data in this field requires further investigation. The talent pools of university graduates are one of the most important indicators of attractiveness of cities for offshorable services. One can find strong correlation between the

number of students and the relative share of employment in financial and other business services, which used as an approximate estimation of the availability of labour pool suitable for the service centres.

¹⁶ According to estimates about 1400-1500 service centres operate within Europe, of which 150-180 located in Central and Eastern Europe (SASS, 2008). In the early 2007, DTZ survey recorded 183 offshored service operations across CEE revealing that the three core countries, namely Poland, Czech Republic and Hungary, account for 77 per cent of total business offshoring services within the region. The shares by individual countries were the following: Poland (32 per cent), Czech Rep. (25.7 per cent), Hungary (18.5 per cent), Romania (12.5 per cent), Slovakia (5.4 per cent), and Bulgaria (5.4 per cent).

¹⁷ There are approximately 30,000 graduates in Krakow, of which about 21,000 are graduates in economics. Capgemini has its largest F&A and R&D offshoring centre in Krakow.

¹⁸ Labour supply can be tightened in provincial Poland too as cities in regional Poland, in particular, have seen large flux of emigration to the British Isles.

¹⁹ DELOITTE's Global Location Survey (2007) examined Hungary's untapped offshoring locations and selected 5 provincial cities (Debrecen, Kecskemét, Pécs, Székesfehérvár, and Szeged) which should be considered as so-called "under the radar" locations offering an attractive cost/quality ratio that can stand comparison with Budapest.

²⁰ The under-development of certain eastern regions of CEE lacking regional airports, motorways and international schools can deter expatriate manager staff from locating there. In terms of office markets in the smaller secondary locations, it can be difficult to beat the advantages of the capital cities or the larger regional centres (Brno, Kraków, Wrocław).

