Looking for new outsourcing opportunities? Enter Germany

Is outsourcing just about savings in expenses? Are shared services just about labor and rental costs? In fact, much more is at stake in the global insourcing and outsourcing game…

India, China and Malaysia being on the top… India and Philippines controlling about 50 percent of the global outsourcing market… India as a top BPO destination for overseas companies… – These are the statements we have been used to for many years. What about the other half of the globe? – We can summarize it in just one (short but very complex) sentence: It has been showing a huge dynamics over time and covers many (unexpected) issues.

Have you ever expected that a country with relative high labor costs can be one of the most attractive outsourcing destinations in the world? Probably not. But that really happens – France, Germany, Great Britain and the USA are listed in 2009 A.T. Kearney Global Services Location Index™ (GSLI), which shows 50 most attractive global outsourcing destinations.

Some high-cost countries rank even better than these perceived as low-cost ones.

How can that be explained? Labor costs are only one dimension a potential investor takes into consideration while looking for a destination they outsource (or insource) their operations to. Therefore they also consider such factors as people skills, their availability, and business environment. The expensive countries compensate the cost aspect by quality of workforce, good infrastructure and political stability. Let's analyze it, having a short look at the already mentioned 2009 A.T. Kearney Global Services Location Index™ (GSLI). Perceiving the three dimensions considered (financial attractiveness, quality and availability of human capital and business environment), Germany has received 4.91 as the total score, comparing with 6.91 of

India. Table 1. *Germany's comparison with the top three global outsourcing destinations* delivers a comparison between the top global outsourcing destinations and Germany.

Table 1. Germany's comparison with the top three global outsourcing destinations

Country	Financial attractiveness	People skills and availability	Business environment	Total score
India	3.13	2.48	1.3	6.91
China	2.59	2.33	1.37	6.29
Malaysia	2.76	1.24	1.97	5.98
Germany	**0.42**	**2.1**	**2.4**	**4.91**

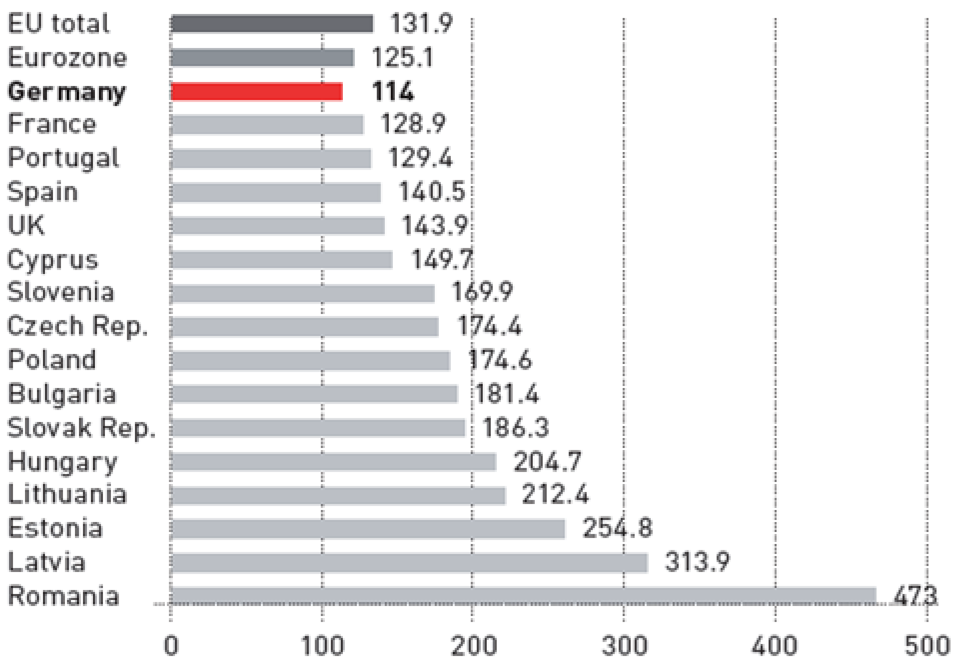
Source: 2009 A.T. Kearney Global Services Location Index™ (GSLI)

Also other studies confirm this tendency. According to the findings of one of the latest studies "Reinventing European Growth" (2009) undertaken by Ernst & Young, Germany receives high marks in terms of infrastructure (both telecommunications and logistics), social climate, qualifications of workforce, and quality of life. And the relative high labor costs can be reduced even by 40 percent thanks to special collective agreements signed with the trade unions. Except of that the level of wages and salaries remains stable in Germany comparing with other countries, which will be shown in the further part of this article. As Germany Trade & Invest, a foreign trade and inward investment agency of Germany reports, the annual growth in the BPO sector amounts to 9 per cent. The value of BPO market volume in Germany is estimated at EUR 16 billion by 2012.

According to the statistics provided by Ernst & Young, FDI investment announcements in Europe in 2008 amounted to 3,718, of which more than 10 percent covers Germany. 11,397 jobs could be created in this country in 2008 thanks to FDIs while in 2007 there were "just" 5,972 jobs created. Germany overperforms the rest of Europe in terms of attracting of BPO activities and job creation due to them, as Europe as the whole recorded a decline in job creation between 2007 and 2008 by 16 percent. The decline affected almost all European countries except of the above mentioned Germany, Bulgaria and Ireland.

One of the reason for declining the FDI operations is obviously the global crisis. The other one can be directly connected with the explosion of labor costs. Long-term investors consider the development of wages and salaries, too. Diagram 1. *Development of labor costs (year 2000 = 100)* illustrates the development of gross wages in salaries in European comparison, showing that German labor costs remain stable in the middle- and long-term perspective comparing with other countries and that the cheap ones of today are mostly the expensive ones of tomorrow.

Diagram 1. Development of labor costs (year 2000 = 100)

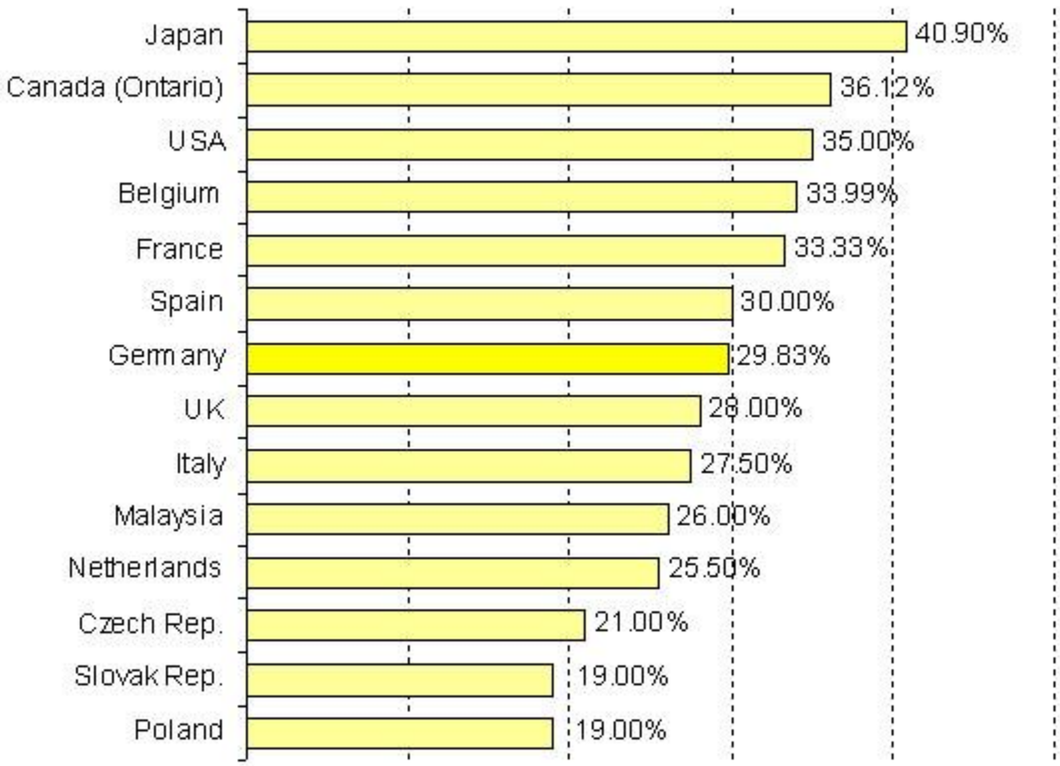


Source: Eurostat online, Germany Trade & Invest

There are also many incentives for investors willing to establish their operations in Germany, in form of cash incentives, interest reduced loans, public guarantees, labor-related incentives and R&D incentives.

Regarding the corporate tax, Germany with its almost 30% tax rate is still not the lowest-tax country but this corporate tax rate is also not the highest one. It ranks somewhere in the middle comparing with other countries, as Diagram 2. *International comparison of the average corporate tax burden (2008)* presents.

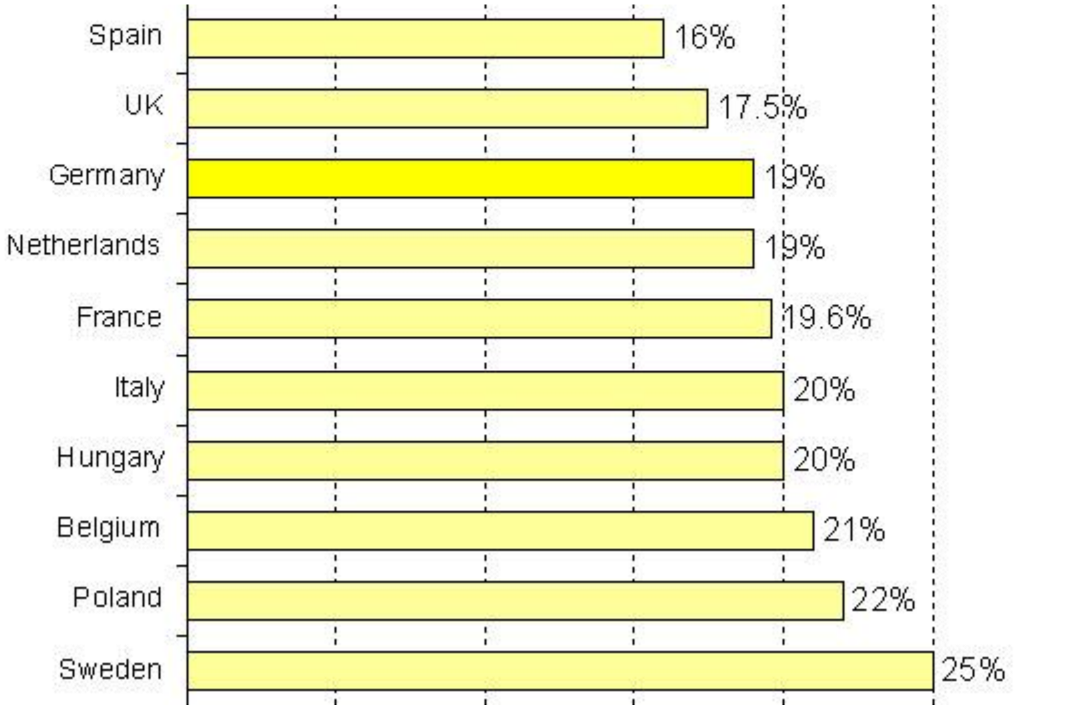
Diagram 2. International comparison of the average corporate tax burden (2008)



Source: German Federal Ministry of Finance, Germany Trade & Invest

However, the value added tax (VAT) rate amounting to 19% in Germany is one of the lowest ones in comparison with other countries, which is summarized in Diagram 3. *Comparison of European VAT rates (2008)*.

Diagram 3. Comparison of European VAT rates (2008)



Source: European Commission, Germany Trade & Invest

While for many years a significant number of German companies have been doing business abroad, now foreign companies are following their example investing in Germany. The process in which the outsourcer of today becomes the "outsourcee" of tomorrow is also called "reverse outsourcing". Val Stella, professor from Kansas University describes the phenomenon of reverse outsourcing as follows: "The world is 'flat' in all directions. The water doesn't only flow to India and China. There is flow back to this country: They need the things that we do well, and we can use the things that they do well." And more: "We tend to think of it only as a one-way street, but it isn't that way."

Many German towns, as Frankfurt, Munich, Berlin, and other were ranked among best cities to locate a business today, ranking 34 European cities and prepared by Cushman & Wakefield in form of European Cities Monitor 2009. Frankfurt was ranked 3 – and that for 20 years now (after London and Paris), Munich – 7, Berlin – 9. The main criteria taken into consideration to prepare this ranking were as follows:

- Easy access to markets and customers,
- Availability of qualified staff,
- Quality of telecommunications,
- Transport links with other cities and internationally.

The above mentioned towns will be further discussed in terms of their attractiveness.

Frankfurt am Main has the population of 670,000 citizens and is the fifth biggest town in Germany following Berlin, Hamburg, Munich and Cologne.

Frankfurt belongs to the richest and high-productive European metropolises. That can be seen perceiving the high number of international companies located in Frankfurt, representing different sectors, as banking, accounting and professional services, management consulting, law, electronic communication, chemicals, software development and call centers. Frankfurt is famous as one of the leading financial centers in Europe. Except of the headquarters of the leading German banks, the European Central Bank, one of the world's most important central banks, responsible for monetary policy of the Eurozone, is also located in Frankfurt. Moreover, this town has the second largest stock exchange in Europe following the London Stock Exchange and being the largest stock exchange in Germany. And Frankfurt possesses the third-largest exhibition site in the world, too.

Due to high level of wages and salaries, Frankfurt attracts many high-qualified professionals from other regions. This city has also very good educational infrastructure, consisting of two universities and several specialist schools preparing candidates for the challenges of the labor market.

Business, education and transport infrastructure – these are the characteristics Frankfurt has. The Airport of Frankfurt ranks among the world's top ten airports and is the biggest cargo airport in Europe. Except of that, Frankfurt is a traffic hub of the German Autobahn system. The Frankfurt Central Station is the largest train station in Germany by number of platforms and railway traffic. Public transportation system consists of two underground systems (U-Bahn and S-Bahn), trams and buses.

Munich has the population of about 1.4 million citizens and the motto of this town is "Munich loves you". Let's explain, why you can love Munich as well.

Munich is a leading location for science and research having a long list of Nobel Prize laureates for many years now. It is a town of many universities, colleges and other scientific centers. This city is the strongest economy in Germany, having the lowest unemployment rate comparing with other German locations.

Munich is a global city. Headquarters of many global players, as Siemens, BMW, Allianz or MAN are located here. Such industries as: electronics, automotive, engineering, insurance, banking, software development, professional services, biotechnology are represented here. Munich is also known as the largest publishing city in Europe.

Regarding transport, the Franz Josef Strauss International Airport, the second-largest airport in Germany, after the above mentioned International Airport of Frankfurt, is located in Munich. Munich can be proud of its most comprehensive and very punctual public transportation system in the world. It includes two underground systems (U-Bahn and S-Bahn), trams and buses.

Munich is an integral part of the motorway network of southern Germany. However, traffic in and around Munich is often heavy and traffic jams are commonplace. Therefore cycling is recognized as a good alternative to motorised transport.

Berlin is the capital city of Germany with population amounting to 3.4 million. This city offers highly educated, flexible, and competitive workforce. Wages and salaries in Berlin are 10 to 20 percent below those of Germany's other major cities. There are over 131,000 students attending Berlin's four universities, three colleges of art, eight technical colleges, and ten professional schools and academies.

Berlin has a very good transport infrastructure and is easy to reach by plane, train, and automobile. The city currently has three airports. All of them can be reached via public transportation. Starting in 2011, the new BBI Berlin-Brandenburg International Airport will further develop the city's links to Central and Eastern Europe and Asia. Berlin has ten major train routes which make the city an important meeting point for rail transportation. Also the efficient network of motorways makes Berlin easily accessible from many national and international directions.

Regarding telecommunications, Berlin is equipped with very good digital infrastructure including 1.8 million conventional telephone connections, over 600,000 DSL connections, and over 200,000 kilometres of fiber optic cable. The city also boasts the first fully-digitalized ISDN network and the first complete broadband network in Germany. More than 1.4 million households and over 90 percent of all Berlin companies are connected to the broadband cable network. Berlin is on the top of the list of wireless LAN locations in Germany.

High-qualified workforce and good infrastructure pay back: About one-third of the world's 50 largest companies are active in the Berlin region.

After having analyzed the most attractive towns in Germany, no wonder that Germany is a popular country where big multinational corporations establish their shared service centers (for example: Allianz, BASF, Bayer, GMAC, IKEA, Merck, Parexel and many more).

Parexel has three regional financial shared service centers: in den USA (Lowell, Massachusetts), Great Britain (Uxbridge) und Germany (Berlin). The Berlin shared service center delivers services to Parexel subsidiaries located in 15 European countries. The advantages of the German capital are as follows: language skills, low employee turnover rates and relative low rental costs.

Also BASF has decided to establish their European shared service center in Germany, in Berlin as well. This entity was founded in 2005 and delivers finance and accounting, and HR services to 100 subsidiaries of the BASF Group located in 25 European countries.

IKEA Deutschland decided to centralize their personnel administration in form of a HR service center in Potsdam close to Berlin. This shared service center is specialized in payroll, system support and recruitment. The customers of this shared service center are over 40 IKEA stores located in Germany, employing around 16,000 staff.

Lately MAN has decided to outsource their IT and telecommunications infrastructure to T-Systems and IBM starting 01 July 2009. It is going on outsourcing of networks, data processing centers, decentralized services and PCs. Until now, MAN IT shared service center, MAN IT Services GmbH, located in Karlsfeld, Germany has delivered these services. The employees of MAN IT Services GmbH, amounting to 320 persons, have been given the choice: to stay with MAN or to change to the new service provider.

The objective of this decision was to focus on key business and to be served by providers who are more experienced in the IT and telecommunications area than MAN. Cost reductions and reduction of future risks are expected as the future investments have been transferred to the new business partners.

The above mentioned and other companies are around 75 percent of the top German companies which have already implemented the shared services concept. About 25 percent of them are going to outsource their shared service center to a third party. 70 percent of German companies want to establish further shared service centers, located in Germany. Key drivers of this decision are: the availability of qualified personnel, labor costs, and the increased significance of labor turnover rates.

Well, we are talking about outsourcing to Germany and about shared service organisations operating in Germany – what are actually the both concepts about? What is the difference between them? Let's explain it just in one sentence: While **outsourcing** is about letting things done by a **third party**, **shared services** – also known as insourcing – are about the concentration of company resources in form of an **internal entity** providing back-office functions to multiple internal partners.

Shared service centers (as insourcing) and outsourcing solution – if properly implemented – bring the following advantages to corporations using them:

- Improvement in customer service,
- Sharing best practices,
- Utilizing technology,
- Processes simplification,
- Increase in efficiency.

Germany to the rest of the world, the rest of the world to Germany… – who is actually outsourcing and insourcing their operations to whom? It is not as clear any more in today's globalized world. Nevertheless, one thing remains truth: The above mentioned and many other advantages from outsourcing and insourcing can be very likely achieved in Germany – a country of 82 million inhabitants with Berlin as the capital, a home land of famous philosophers, like: Kant, Leibniz, Hegel, Schopenhauer, Heidegger, a country of technology and automotive sector: the home land of Siemens, SAP, Bosch, MAN, Porsche, BMW, and a country of football (Franz Beckenbauer, Gerd Müller, Jürgen Klinsmann, Lothar Matthäus, Oliver Kahn, Lukas Podolski… – you know them, don't you?), and of course motorsports with the famous name of Michael Schumacher. A country having open society where over 7 million people from other countries have decided to make their home of. Germany is now becoming a new face: As a country of BPO and shared service operations – being very successful in this area as well.

Our short investment trip through Germany nears the end now. It is a good time to make some conclusions. We have started with the cost aspect and then analyzed other aspects which make a certain location attractive for investors. Therefore: Conclusion 1: Shared services and outsourcing are not just about costs, although the cost aspect is still one of important factors affecting the investment decision. Except of the cost aspect, investors take risk management dimension (stability, predictability) and quality (infrastructure, human capital) into consideration – not just quantity but also quality is at stake. And following the best in class, here is Conclusion 2: Allianz, BASF, Bayer, GMAC, IKEA, Merck, Parexel and many other have already decided – what about you?

By the way, did you know that there are about 1,500 German companies being global market leaders in their sector? What about the BPO and shared service sector in Germany in this context – can we expect that it also will be the leading one in a couple-year-time?

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