LOCATION STRATEGIES

COVID-19 and beyond

OFFICES

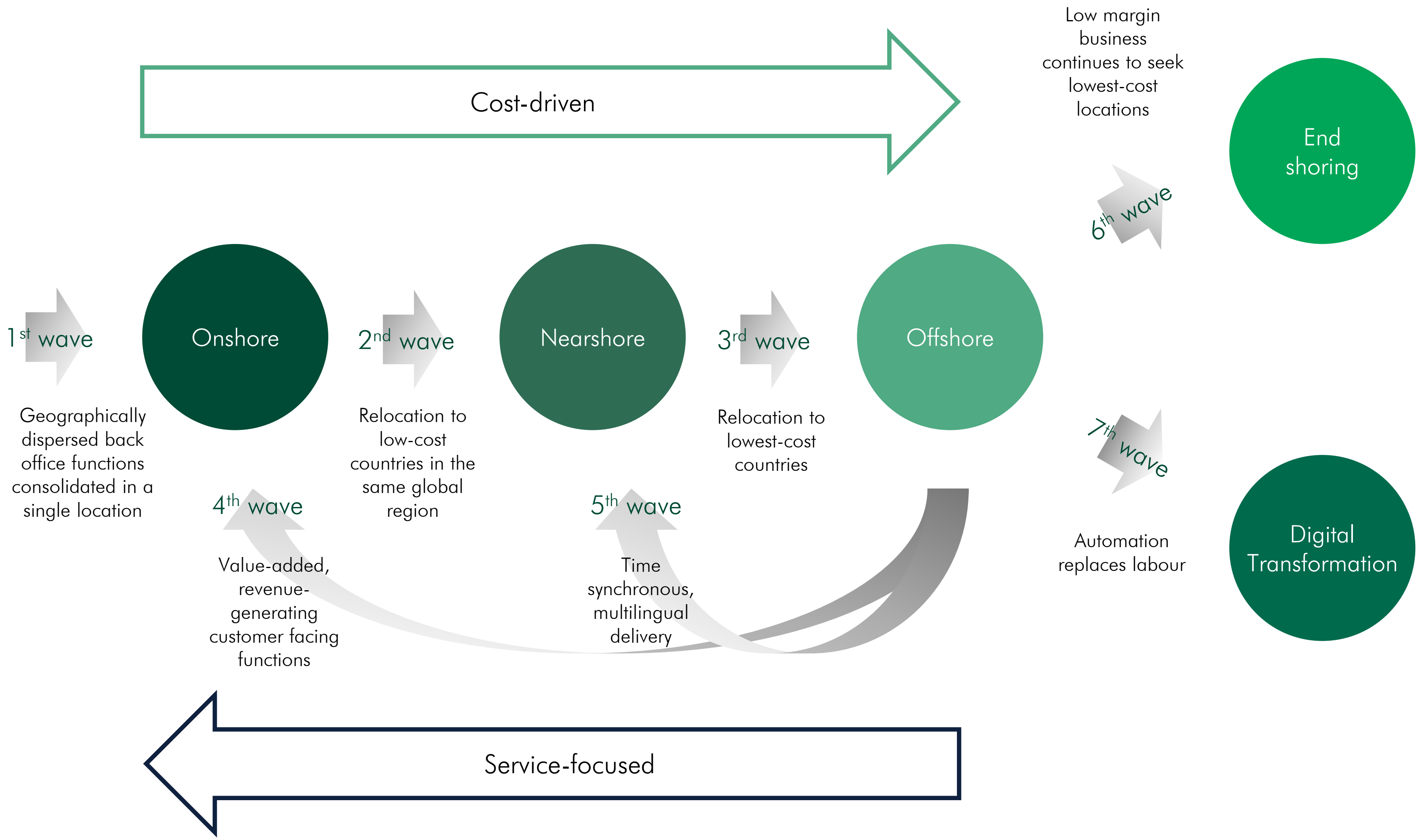
CBRE

Covid-19 has been a catalyst for many companies to begin reviewing their location strategies, or to move them to the top of the corporate agenda.

Cost-driven location strategies tend to lead to concentration risk. Reversing them to reduce risk may not necessarily mean giving up cost advantages.

FROM COST-DRIVEN TO SERVICE-FOCUSED

Evolution of location strategies



FROM COST-DRIVEN TO SERVICE-FOCUSED

Evolution of location strategies

Cost-driven

1ST WAVE, ONSHORE

Companies achieve economies of scale by consolidating several functions in a single new location, enabled by technology and business process reengineering.

The choice of location is not an important consideration at this stage, and consolidation often occurs within an existing corporate location to assess and monitor the operating model.

2ND WAVE, NEARSHORE

Having established that the business model works, companies achieve further cost savings by relocating to nearshore locations in a low-labour-cost country in the same global region.

3RD WAVE, OFFSHORE

Companies seek further cost savings by relocating the function to the lowest-labour-cost country, irrespective of its location relative to their core operations.

Some companies will move straight to this phase following onshoring, often those who have a diverse global footprint.

In each phase, companies will often increase the headcount within the new location as more functions and geographies are served remotely. This will often be done through a single centre, increasing concentration risk as well as exposure to macroeconomic factors such as inflation and foreign currency movements.

Service-driven

4TH WAVE, OFFSHORE TO ONSHORE

Customer-facing, revenue-generating voice work returns onshore as customers find dealing with accented language a challenge and companies recognise the value in local delivery. Whilst labour cost increases, so does customer satisfaction and revenue.

5TH WAVE, OFFSHORE TO NEARSHORE

Offshore service delivery becomes less efficient as linguistic and time zone coverage becomes challenging. Competition for language skills increases as higher skilled multilingual jobs become available and working antisocial hours to serve remote markets requires companies to pay shift premiums.

Where next?

6TH WAVE, ENDSHORING

Low-margin businesses, often providing highly competitive outsourced services, continue to seek the lowest-cost locations.

However, the world is running out of viable, stable countries with a ready-made workforce and infrastructure that are cheaper than India or the Philippines.

7TH WAVE, DIGITAL TRANSFORMATION

Driven by changes in channel preferences from voice to online and the challenge of reducing labour costs further, companies begin to replace labour with capital, enabled by RPA and other technologies. In some cases, the labour is displaced from high-cost locations, rather than the offshore or nearshore location which continues to grow.

The functions that companies first sought to relocate to low-labour-cost countries are increasingly being automated. However, those employees are being upskilled and delivering higher value-added services remotely.

So which countries have benefitted from the movement from onshore to offshore?

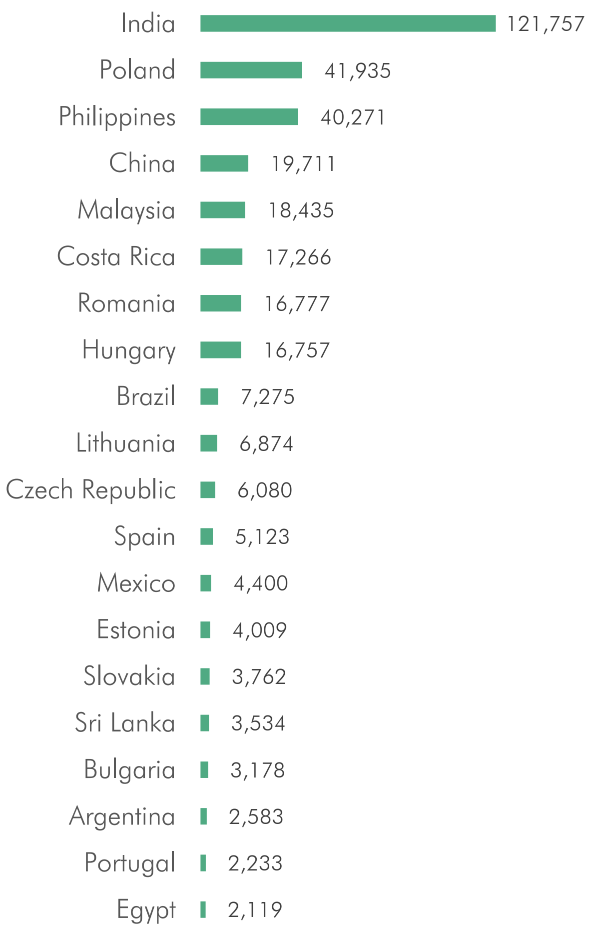
And which ones are starting to experience saturation of labour pools?

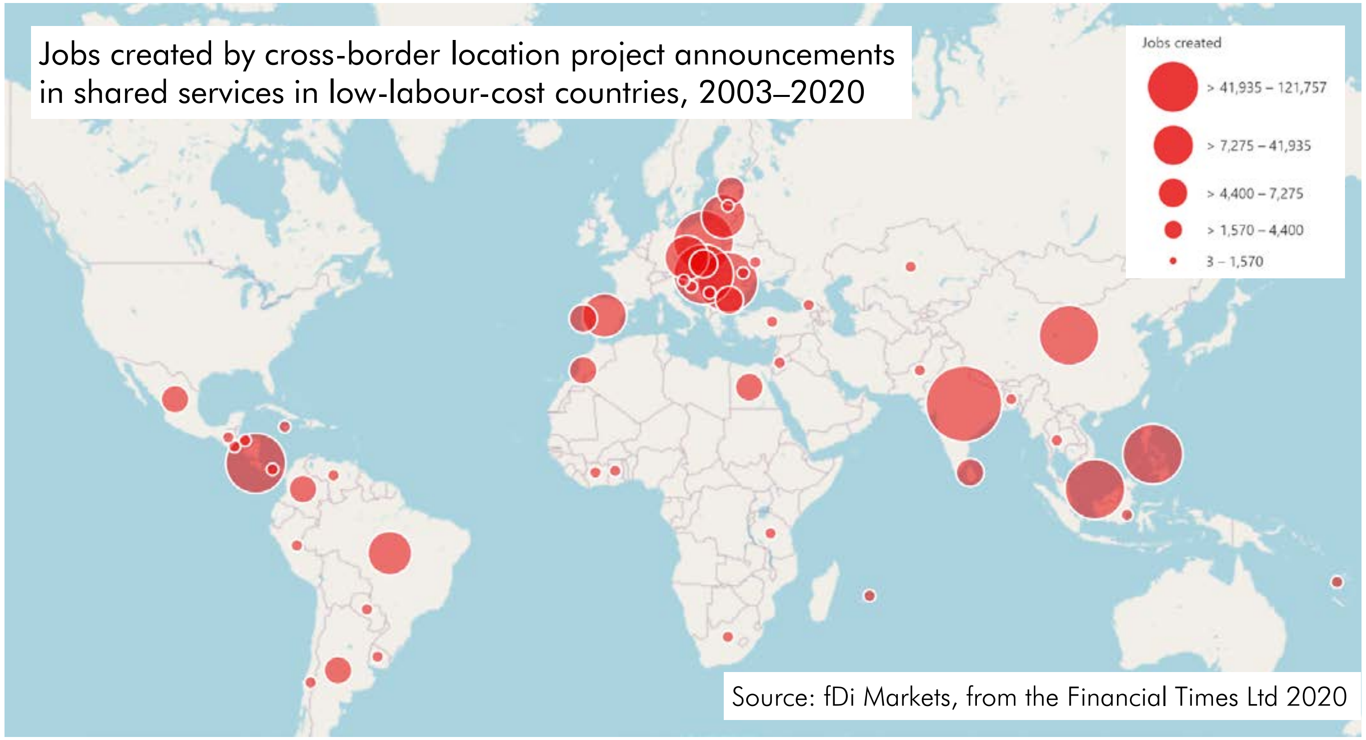
Concentration risk is often accompanied by increased competition for labour as companies adopt the same cost-driven location strategies and land in the same countries.

LOW-COST DESTINATIONS

Low-cost nearshore and offshore locations

Top 20 countries by jobs created





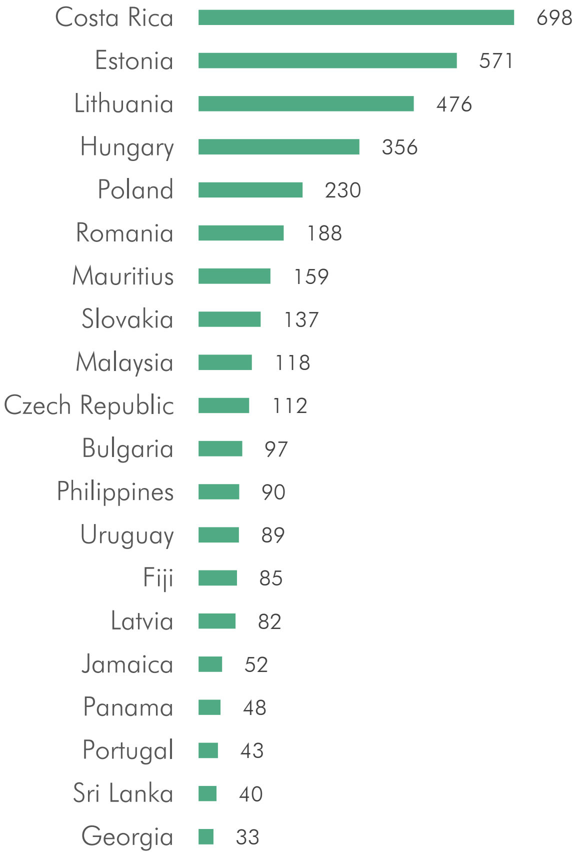
APAC The APAC region continues to draw traction as a nearshore and offshore hub driven by low labour costs, the emergence of secondary cities and the availability of a fluent English-speaking workforce

EMEA Central and Eastern Europe has been the go-to destination for many companies seeking low-cost labour in Europe. However, Spain and Portugal now compete on cost.

AMERICA Within the Americas, LATAM continues to gain jobs from U.S. companies seeking low-cost, Spanish- and English-speaking talent. Tech skills primarily remain in U.S. markets, but strong opportunities are emerging in Canada.

Labour market saturation of low-cost countries

Top 20 countries by labour market saturation
(jobs per 100k labour force)



Jobs created by cross-border location project announcements in shared services, 2003-2020 per 100k of countries' labour force

Source: World Bank World Development Indicators, fDi Markets, from the Financial Times Ltd 2020

APAC A large working-population base coupled with a younger demographic in countries such as India and the Philippines keep the region attractive. However, most Tier-1 cities in these markets are facing issues of congestion, pressure on city's infrastructure and rising cost of living

EMEA The most popular city destinations in Central and Eastern Europe have experienced significant competition for talent, so companies are now looking to second and third tier cities, as well as other countries in the region.

AMERICA The most mature offshoring markets in LATAM (Costa Rica, Panama, Mexico) have experienced high levels of saturation, creating talent shortages for certain skills. However, more emerging markets like Uruguay, Paraguay and parts of Colombia represent strong labour opportunities for pioneering companies.

So how much does it cost to mitigate concentration risk?

Initial reluctance can be driven by the inevitable increase in real estate cost and duplication.

However, labour is on average 90% of total office operating costs, with real estate less than 10%.

Companies need to establish whether consolidating business functions in a single city or single country is within their tolerance for risk.

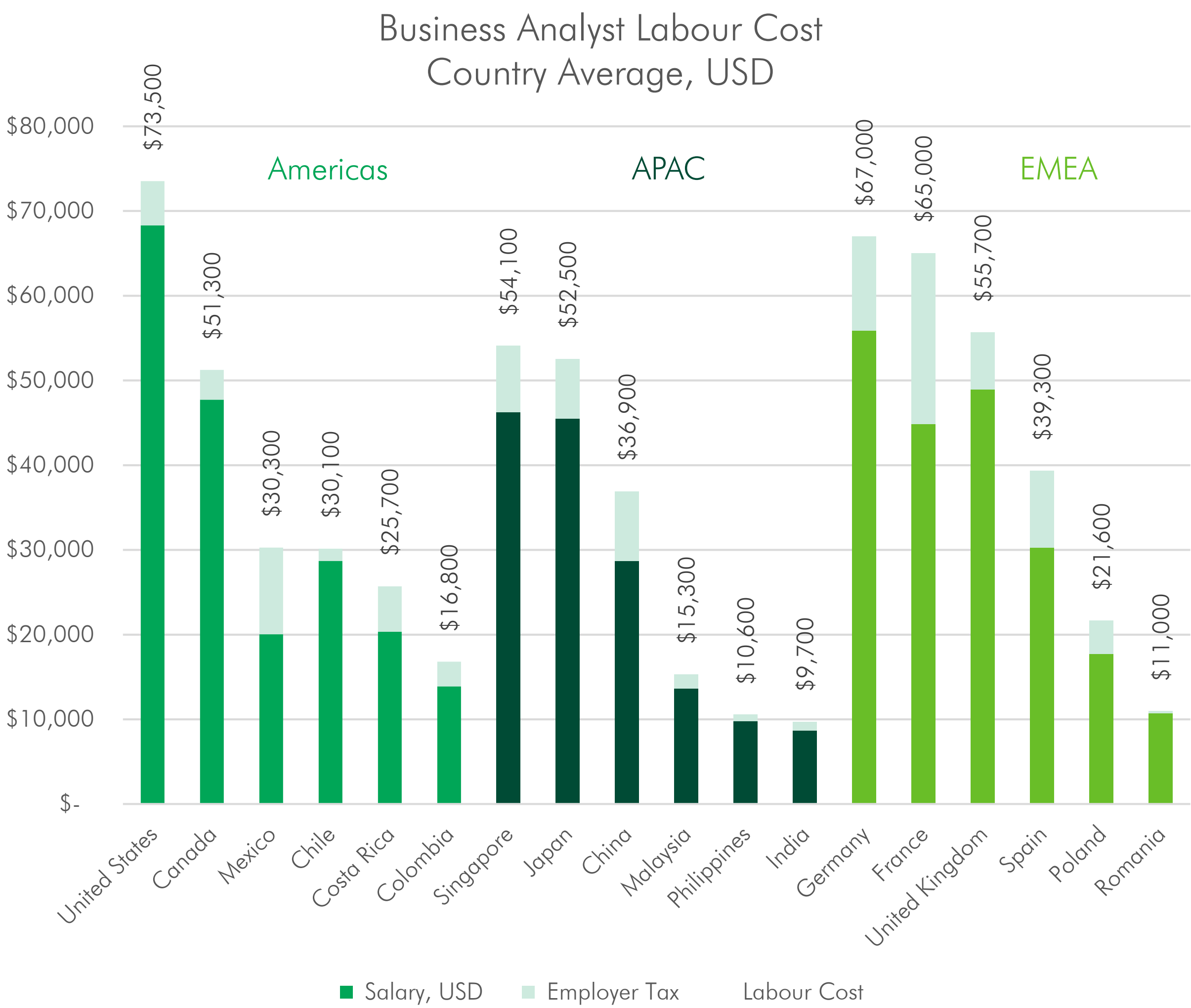
Labour cost arbitrage

The chart shows two high-cost and three low-cost-labour countries in each global region.

The cost data is the average salary for a business analyst, plus employer tax.

The range in each region is broadly the same, with labour cost in the higher cost countries between $50k-$70k per year and falling to $10k-$20k per annum in the lowest-cost countries.

So labour cost savings of 80%-90% are achievable.



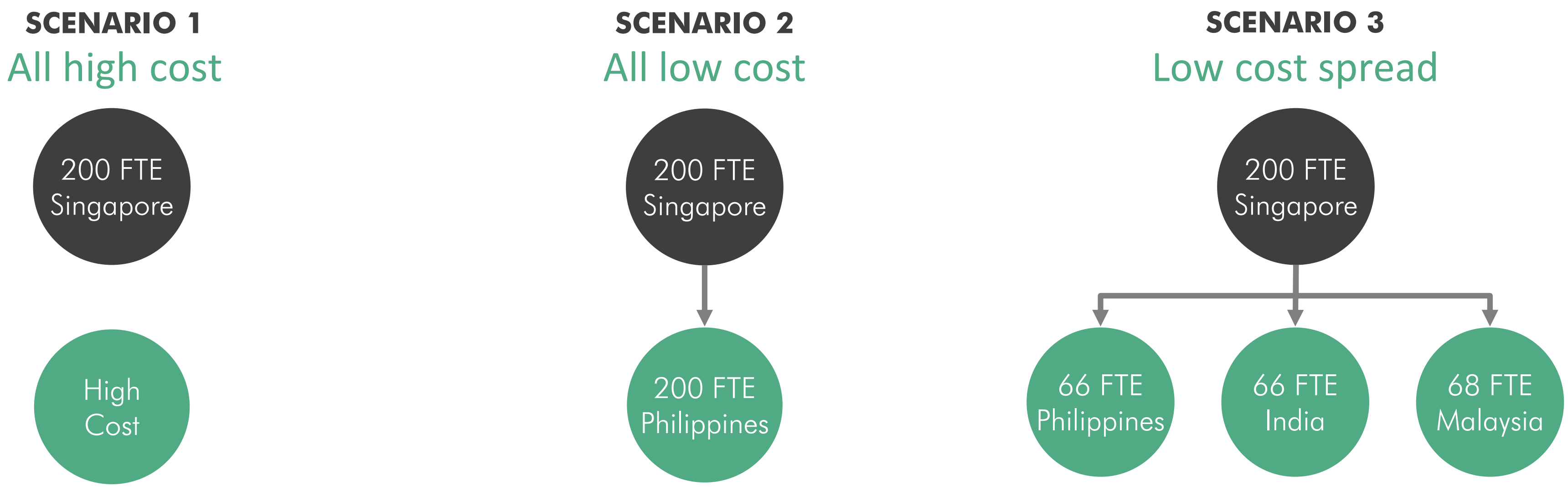
COST OF DE-RISKING

The cost of mitigating concentration risk

We've created three scenarios in each region to show the labour cost impact of mitigating concentration risk, based on reconfiguring 200 business analysts using the salary data and countries shown on the previous page.

- **SCENARIO 1** – all employees are located in the highest-cost country in each region
- **SCENARIO 2**– all employees are located in the lowest-cost country in each region
- **SCENARIO 3**– employees are spread between the three lowest-cost countries (from the previous page) in each region

The graphic below shows how this works for APAC.



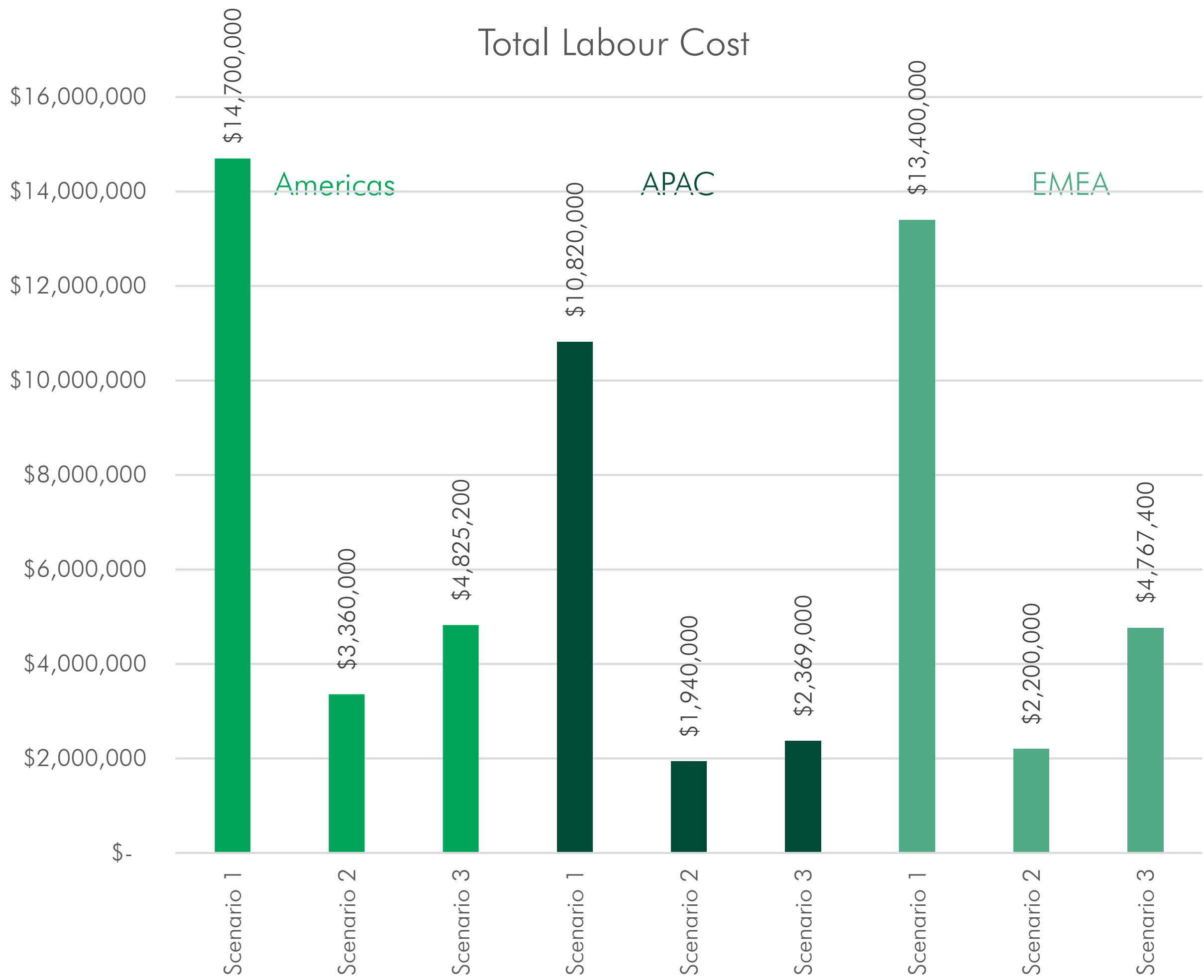
COST OF DE-RISKING

The cost of mitigating concentration risk

The savings delivered by moving all jobs from the highest-cost country to the lowest reduces labour cost by 80%.

So that's around $10m per year in savings but with concentration risk.

Mitigating that risk by spreading the jobs between three countries still delivers labour cost savings of 80% in Americas and APAC and 60% in EMEA.



Sources: Glassdoor (salary data), KPMG (employer tax rates), xe.com (exchange rates). All data May 2020

So what does this mean as companies embark on digital transformation strategies?

Nearshore and offshore locations have seen jobs in low value processes automated, but without necessarily displacing those jobs as employees—often overqualified for those original roles—are upskilled.

So the key to remote delivery is rightshoring, determining which business functions and roles are mobile, and whether they need to remain in high-cost global cities.

DIGITAL TRANSFORMATION

Rightshoring of IT and software engineering

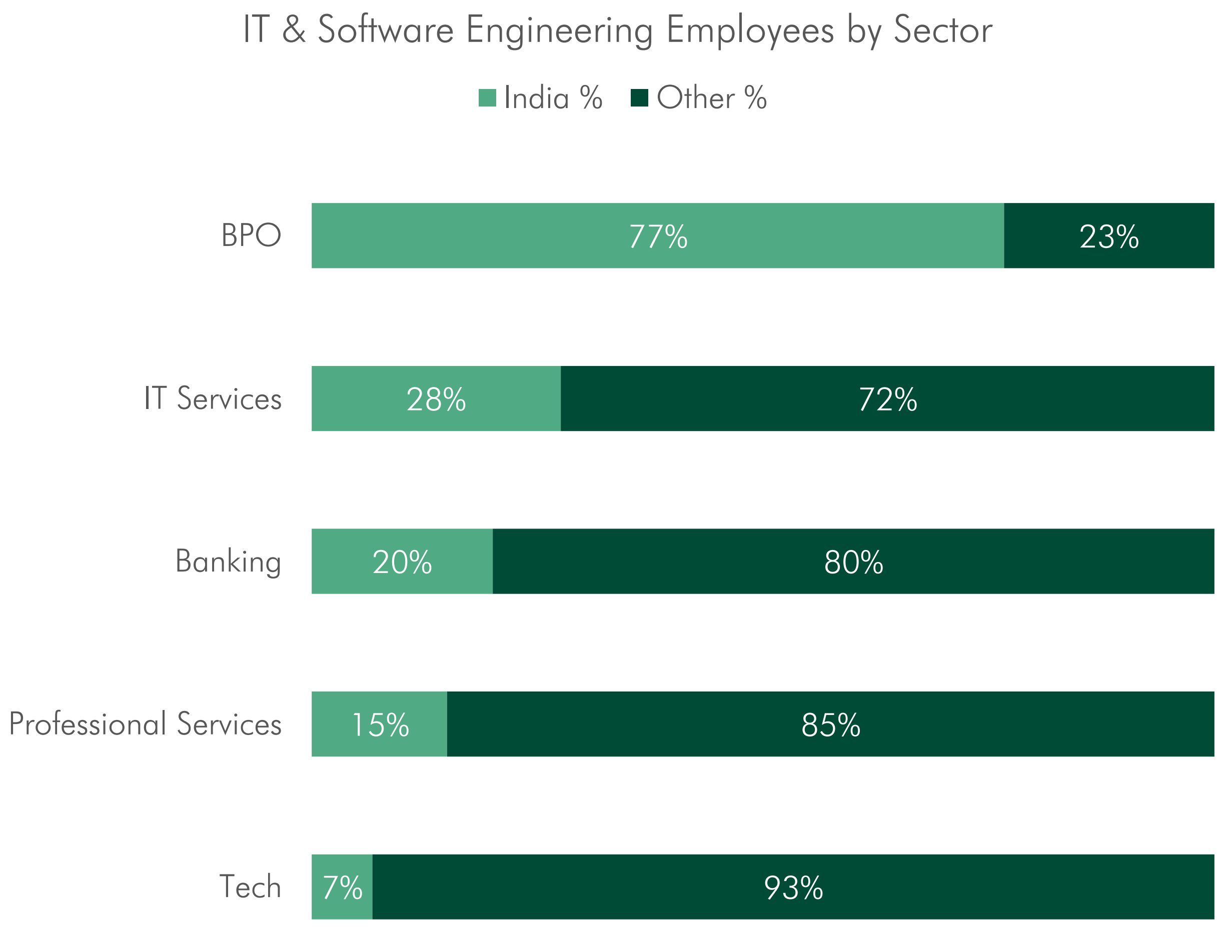
The chart shows how different sectors have developed very different strategies for rightshoring tech talent.

Sectors where margins are tight and controlling cost is critical have tended more toward offshore locations.

The key differentiator here is whether they service a cost centre or generate revenue. That line is becoming increasingly blurred, as basic processes are robotised and offshore workers upskilled.

Whilst the tech companies do have a significant presence in offshore locations, it is not as significant, since the focus is on revenue generation.

This will be true for companies entering digital transformation programmes who need engineering, data science and analytics skills.



Source: Selected companies' annual reports

So how can CBRE help?

An initial global footprint diagnostic can highlight the split of talent between high- and low-cost countries by individual business functions or skills and demonstrate opportunities to rightshore based on peer company examples.

Developing a global location strategy that tests scenarios based on mobility of functions to demonstrate labour cost savings or depth of talent.

Finally, location selection identifies labour cost savings or sustainable talent pools.

How CBRE can help

Global Footprint Diagnostic

Independent desktop study to:

- Identify concentration risk
- Quantify potential labour cost savings

The diagnostic breaks down opportunities by business function and analyses peer companies to benchmark performance.

Global Location Strategy

More detailed analysis overlaying your company's data with labour market data.

Working with you to develop potential configuration options to mitigate concentration risk and reduce cost.

Benchmarking existing locations for talent availability and cost against potential new locations to establish whether your company is in the right locations.

Location Selection

Identify locations that:

- Reduce labour cost by 20-30% within country, or 70-90% through nearshoring or offshoring
- Maximise access to talent
- Are best placed to implement a new business process, such as digital transformation centres

We evaluate country and city level data to identify the best, not the obvious, locations that are sustainable.

REGIONAL SNAPSHOT

AMERICAS

Mark Seeley

Head of Labour Analytics, U.S.

mark.seeley@cbre.com

Yazmin Ramirez

Labour Analytics & Location Incentives, LATAM

yazmin.ramirez@cbre.com

Within the U.S., one of the dominant trends over the last five years has been the consolidation of workers into large regional hubs – often employing 2,000–5,000 people each. These corporate hubs typically employ many roles across large back-office functions like finance, technology, HR and service. Due to the large size of these hubs, only a limited number of markets other than the high-cost established markets of NY, LA, SF and Chicago can support them. The result has been hyper-competition—particularly for technology talent—in the short-list of "go-to" markets: Dallas, Atlanta, Austin, Denver, Nashville, Phoenix and others. Now, due to the massive disruptions to jobs caused by COVID-19, new location strategies are emerging, and new markets are likely to see corporate expansion activity. This next tier of markets includes cities like Kansas City, San Antonio, Albuquerque and Boise.

The most competitive jobs heading into the pandemic were tech-centric (i.e. software engineers, data analysts, business analysts, etc.), and this is expected to continue and possibly amplify once the virus abates. Canada is emerging as an excellent "release valve" where companies can source top tech talent with less competition at a 25% discount.

LATAM markets should remain strong options to those seeking low costs with strong Spanish-speaking capabilities and/or time zone alignment with U.S. customers. Emerging markets offering strong availability and an expanding skill base include Colombia, Uruguay, Argentina and Paraguay.

REGIONAL SNAPSHOT

APAC

Arpan Barua

Head of Labour Analytics, APAC
arpan.barua@cbre.com

Amy Ying

Labour Analytics, APAC
amy.ying@cbre.com

Udit Sabharwal

Labour Analytics, APAC
udit.sabharwal@cbre.com

The region continues to draw strong attention from international businesses driven by availability of skilled multi-lingual talent, competitive labour costs and the ability to support both 'follow the sun' and 24x7 operations.

Whilst unemployment rates across countries rose as a result of COVID-19 and country-wide lockdowns impacted business activities, there is optimism in sight for some sectors as countries gradually lessen restrictions.

In APAC, India and the Philippines traditionally have been the top two recipients of outsourcing jobs. But as major cities in these countries are reeling under pressures of rising labour costs, attrition, infrastructure and social security concerns, secondary cities are becoming interesting alternatives. Language availability, particularly English-speaking, remains a key consideration for the voice-based international call centre industry, and secondary city choices can pose limitations when looking to grow in scale.

We have also seen an increasing dialogue around digital transformation, with some BPOs considering deployment of virtual call-centre operations.

On the technology side of software development, sales and support, China and India remain leaders with a large and skilled workforce availability.

Looking ahead, for high-cost locations such as Singapore and Hong Kong, companies will continue to diversify their footprint to lower-cost markets. Malaysia, Vietnam and Thailand are regularly featured as potential contenders for the shared service centre industry.

REGIONAL SNAPSHOT

EMEA

Stephen Fleetwood

Head of Talent and Location Advisory, EMEA

stephen.fleetwood@cbre.com

Stephen Hetherington

stephen.hetherington@cbre.com

Joanna Foster

joanna.foster@cbre.com

Lisa Steffen

lisa.steffen@cbre.com

Central and Eastern Europe (CEE) has been the choice for many companies seeking low-cost labour in Europe, but the picture is changing.

The Czech Republic and Slovakia have higher labour costs and relatively few large cities, so competition for labour is fierce. Poland, Romania and Hungary remain popular, but labour markets in major cities are showing signs of overheating. Thus, companies are becoming more adventurous and looking at second and in some cases third tier cities to find new talent pools.

Bulgaria and Ukraine are the lowest-cost options in Europe, but each has challenges, with significant outflows of talent to better-paid jobs in other countries being just one.

Lithuania has attracted a number of shared services and remote delivery centres, and we would expect Latvia to follow suit.

Spain, Portugal and Greece are all now in a similar cost bracket to many CEE countries and are often on the shortlist alongside them for many office projects.

Labour costs in the established nearshore destinations in Africa, such as Morocco and Turkey, are now comparable to the lower-cost regions of CEE, so the search is likely to widen to those countries on the continent with sufficient business infrastructure and political stability.

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