How Chile can win from offshoring

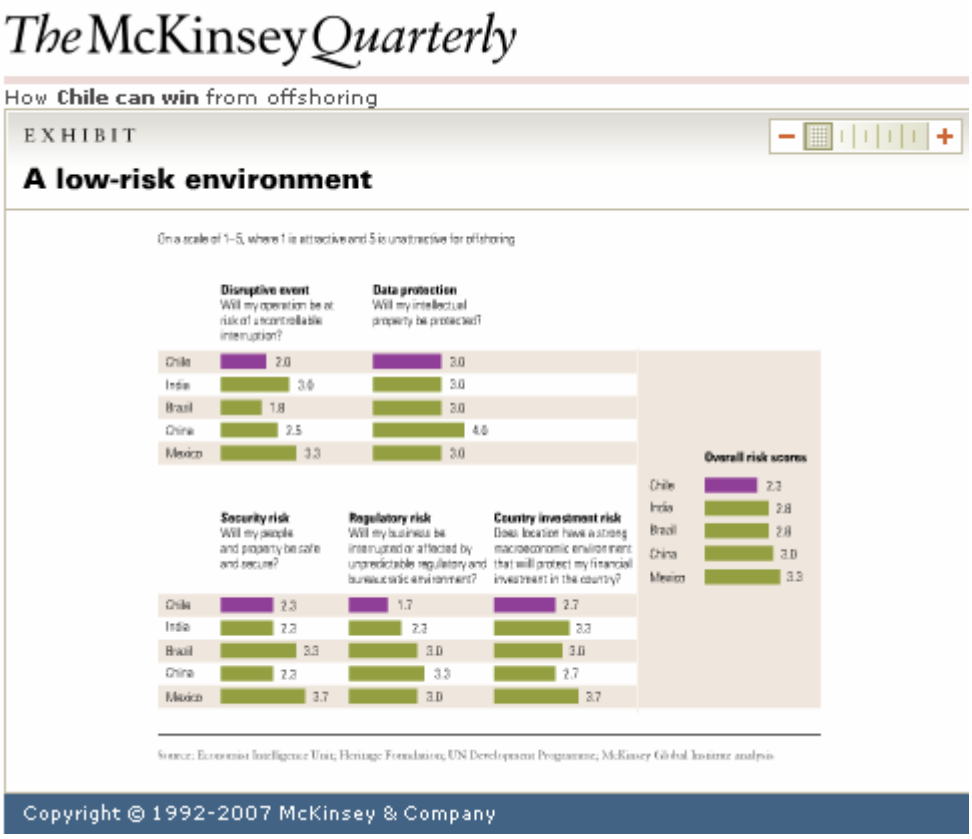
Roshni Jain, Martha A. Laboissière, and Gonzalo Larraguibel

The country has already attracted the attention of multinationals; now it must address its shortcomings to reach its offshoring potential.

Chile has attracted considerable attention from foreign companies as an offshoring location, given its first-rate regulatory and living environment, attractive risk profile, low infrastructure costs, and openness to trade1 (see "What executives are asking about Latin America"). Analysis by the McKinsey Global Institute (MGI), however, finds that Chile's limited potential as a domestic market lowers its appeal to multinational companies interested in establishing captive centers, while its small base of IT vendors lowers its appeal to companies seeking to outsource services.

MGI examined Chile's position relative to ten other low-wage countries2 along six dimensions that companies consider when choosing an offshore location: costs (including labor costs), market potential, the vendor landscape, risk profiles, the overall environment, and the quality of infrastructure. (The full report, The Emerging Global Labor Market, Part II—The Supply of Offshore Talent in Services, is available free of charge online.)

We found that Chile's risk profile, which is better than that of both China and India, is the most attractive among all of the Latin American countries we studied (exhibit). Chile scores especially well on regulatory risk: the regulatory frame-work is transparent, with little bureaucracy, and the legal environment is stable.



Chile's overall environment (a measure that includes a country's business and living environments, as well as its accessibility3) and level of government support are among the best of any low-wage country we studied—second only to those in Hungary and tied with the Czech Republic's. Chile's score is buoyed by quality-of-life ratings comparable to those of developed countries, low levels of corruption, and government policies that appeal to foreign investors. Indeed, when measured by the general level of government support,4 Chile scored better than Germany and nearly twice as high as Brazil.

Moreover, the cost of electric power in Chile is among the lowest in the world—comparable to rates in Canada and the United States—in part because of regulatory reform in the 1980s.5 Chile also boasts one of the world's lowest corporate tax rates, at 17 percent, and highly competitive real-estate costs. While Chile's labor costs are higher than Mexico's, they are similar to those in Brazil.6 This was also the case for total costs (a weighted average of the quality of labor and infrastructure, as well as the corporate tax rate).

But Chile faces challenges, given its small base of IT vendors. Despite an educated workforce, the number of employees in IT services is small—and so is Chile's market for offshore IT services and business process outsourcing. (Together, these activities represented around $500 million in 2005, compared with more than $6 billion for IT services alone in Brazil.) The market is small partly because of Chile's small population—around 16 million, compared with 184 million in Brazil—which also explains the limited size of its talent pool.

Chile's market potential is also hampered by the relatively small size of its economy and those of its neighbors. This factor is important because some companies may offshore activities to a given location in order to support domestic expansion there, as well as in neighboring countries where they also operate. Moreover, the long travel times from key markets in Asia and Europe could make companies thinking of establishing large-scale operations in Chile hesitate.

To be sure, Chile is already an appealing offshoring location for multinationals. In 2002 Citigroup and Unilever established operations in Santiago to handle software development and back-office services, respectively. Just last year, Yahoo! opened a Web research lab in the country. Still, Chile should establish a long-term strategy to compensate for its shortcomings and help the offshoring sector capitalize fully on its potential.

For example, Chile should increase the collaboration among the government, companies, and local universities to ensure that students acquire the level of skills that multinationals expect. In our view, the curriculums in disciplines such as engineering need to be more practical and flexible so that young engineers can adapt better to changing market demands. To transfer knowledge and best practices, Chile should also consider educational-exchange programs with engineering schools in developed countries. Such moves would help Chile increase its attractiveness to foreign companies and put the country in a better position to thrive as offshoring grows in Latin America.

Disponível em: <http://www.mckinseyquarterly.com>. Acesso em 9/4/2007.