Developing Mexico's offshoring opportunity

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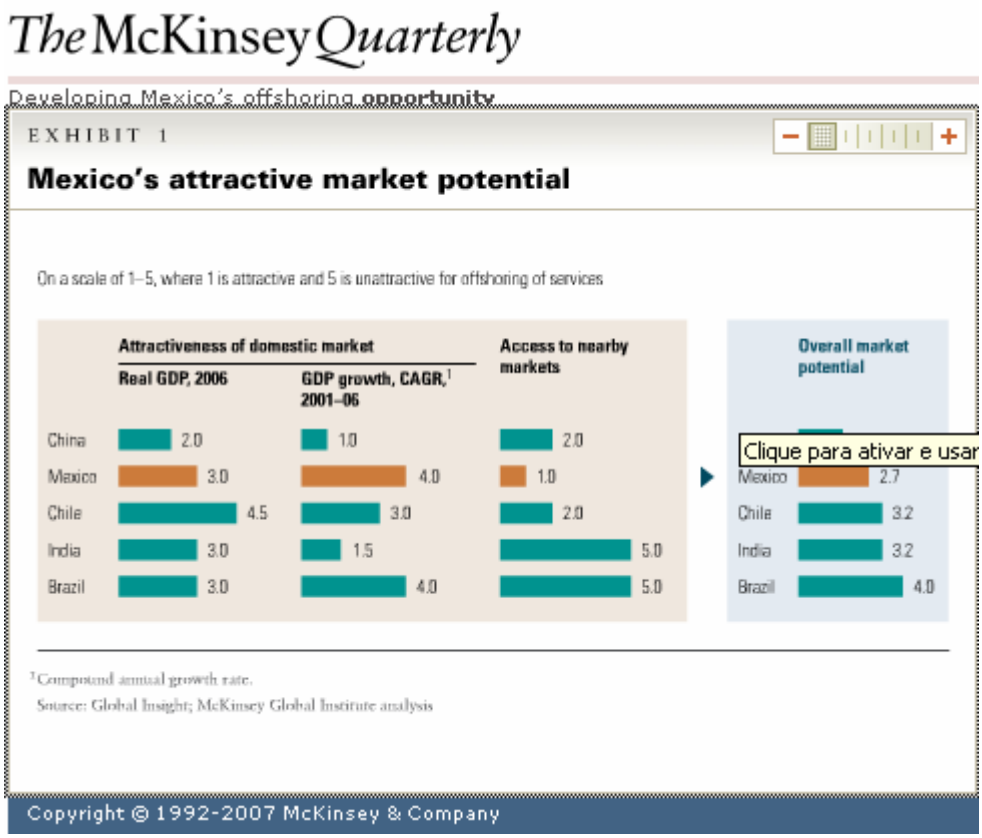
To take advantage of the growing global market for offshored services, the country must do more to improve the suitability of its workforce.

Mexico holds great potential as a supplier of offshored services, given its low costs, proximity to the United States, fast-growing pool of university graduates, and promising domestic market. But research by the McKinsey Global Institute (MGI) finds that a dearth of IT vendors, a costly infrastructure, and a talent pool with limited suitability for multinational positions are among the factors preventing Mexico from realizing the considerable opportunity created by globalization.

Mexico's advantages start with low labor costs, which, at around one-quarter of US levels, were the fifth lowest among the 28 low-wage countries we studied.1 (The full report, The Emerging Global Labor Market, Part II—The Supply of Offshore Talent in Services, is available free of charge online.) Even after accounting for the relatively high cost of electric power, Mexico is a less expensive offshoring location than low-wage centers in Eastern Europe. Indeed, for a company motivated primarily by cost, Mexico holds the most attractive position among the Latin American countries we studied.2

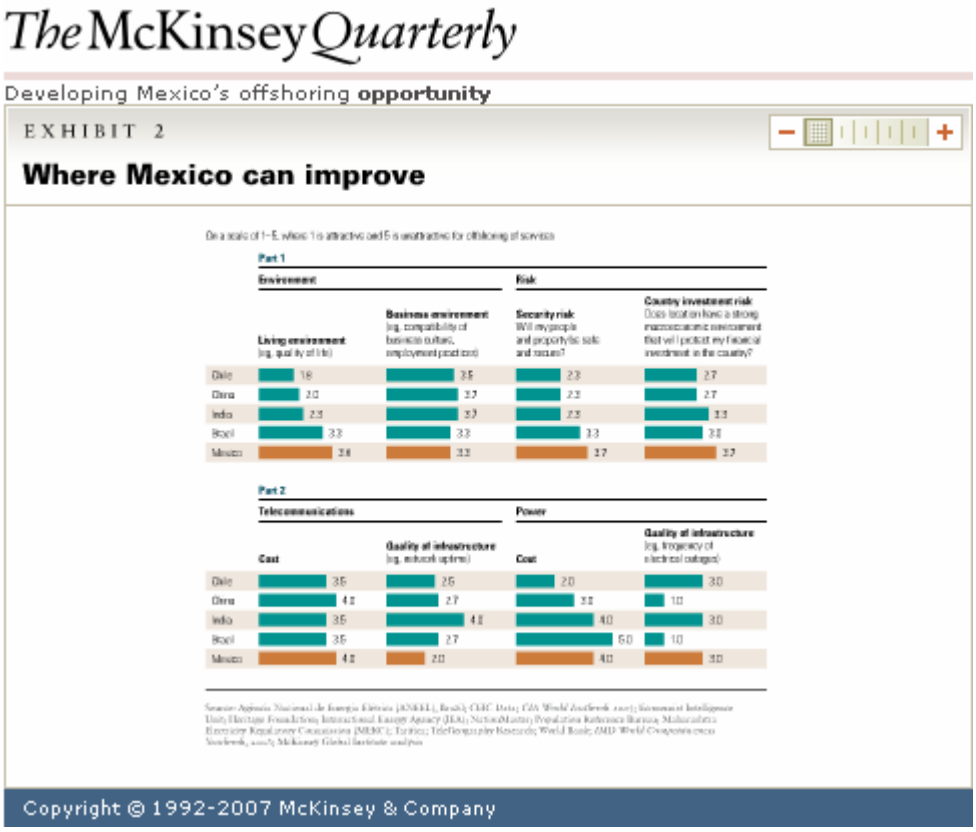
Mexico's other benefits include its cultural ties and physical proximity to the United States and Canada, including shared time zones and frequent flights with short travel times that make Mexico the most accessible low-wage market for North American companies. This proximity allows for high levels of support and collaboration between customers and service providers—positive factors that can outweigh negative ones such as higher costs. In addition, Mexico's market potential is promising: it placed second only to China among the developing countries we examined (Exhibit 1).



Mexico fared less well in other ways. The country's landscape for IT vendors, for instance, ranked second worst among the low-wage countries we studied, largely because of the low number of employees in IT services (around 15 percent of India's total) and a small local

market for IT services and business process outsourcing.3 The size of Mexico's market for these activities is comparable to that of Chile, which is much smaller.

The country also scored poorly when compared with other countries along such measures as risk and the living environment. It tied with the Philippines for the highest risk of disruptive events (say, business interruptions resulting from political unrest) and security problems (the safety of a company's people and property). On measures of the living environment4 Mexico's score was quite low—the result of a high crime rate and subpar scores for quality of life (Exhibit 2, part 1) in large cities. The costs and infrastructure of Mexico's telecommunications and power sectors also stack up rather poorly (Exhibit 2, part 2). Likewise, Mexico's rigid labor regulations make hiring and firing employees difficult.



We also found that despite the country's burgeoning population of university graduates (growing by some 7 percent a year since 2003), companies doing business in Mexico have trouble finding suitable talent—particularly for high-value-added jobs. Our interviews suggest5 that for positions in areas such as applications development, software design, and pharmaceutical R&D, a multinational company would hire perhaps only 20 percent of a given graduating class. (Such figures are in line with suitability levels in Asia and Brazil.) The low suitability rates among Mexican students can be explained largely by the shortcomings of the country's education system and the poor English-language skills of its graduates.

An underdeveloped recruiting industry (including headhunters and companies specializing in HR) exacerbates the situation by making recruiting more time consuming for companies. In an extreme case, a multinational had to screen 500 new graduates on its own to fill ten openings. Given India's suitability levels and recruiting industry, this company reckons it would have to screen no more than 50 candidates to fill the same positions in its office there. Such challenges make it difficult for companies operating in Mexico to grow. As one interviewee put it, "We set up an offshore center but couldn't expand [it] because we could not find the necessary people—ultimately, we ended up only doing low-value activities there."

Together, these factors leave Mexico in a bind. Although it has attracted major call center providers serving both the English- and Spanish-speaking markets, it isn't as cost competitive

for such jobs as Asian countries (for English-speaking centers) or Central American ones (for English- or Spanish-speaking centers) are. Identifying, attracting, and developing the necessary talent pool for higher-value jobs is more difficult in Mexico than elsewhere.

As the global market for offshored services grows, along with demand for offshoring capacity in Latin America, Mexico must continue to focus on the advantages conferred by its proximity to the United States. Mexico's government must also address talent shortages, as well as the regulatory, infrastructure, and living-environment issues that make the country less attractive to foreign companies. While these are large, time-consuming problems, efforts are under way to address them. Mexico's recently implemented national exams, for example, should make evaluating the qualifications of its talent base a more transparent process. Recent government efforts to combat crime are also laudable.

Another bright spot is Prosoft, a government initiative to upgrade Mexico's software industry by bolstering the training and education of its workforce (and thus attract companies that focus on higher-value-added activities) and by supporting improvements to Mexico's infrastructure and telecommunications networks, among other goals. In India such efforts, pioneered by the National Association of Software and Service Companies (Nasscom), helped to speed the development of the software sector and to prepare the country for emerging opportunities in areas like pharmaceutical R&D. Such efforts increase cross-border collaboration between companies—something that would help Mexico improve its already strong ties with companies in the United States.

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