

Market Overview of China-Centric Pure-Play Application Service Providers

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China is a highly analyzed global sourcing destination. It is often compared with India as the next bastion of offshore or nearshore resources for IT services and outsourcing. Given the demand for more information about key outsourcing options in China, this research addresses one of the many frequently asked questions about the potential IT services provider options using Chinese resources for the delivery of offshore or nearshore services. This research provides a high-level profile for many emerging China-centric pure-play application service providers.

Key Findings

- China has most of the crucial ingredients necessary to succeed as a destination for outsourcing. However, it's still maturing, and more-credible vendors with credible offerings and proven track records are in high demand.
- The lack of extensive English-speaking skills, the relatively higher level of risk for security and Internet Protocol issues, and relatively lower process maturity are a few of the areas that need to improve in China. Emerging vendors must be able to demonstrate the ability to address all these areas.
- Involvement in China from larger, traditional multinational service providers and Indian-based providers is accelerating the credibility of the vendor landscape and increasing the process maturity for services delivered from China.

Recommendations

- Clients refreshing their sourcing strategies should use this market overview to determine potential opportunities. It is important to monitor progress and maturity with regard to the use of China-centric pure-play service providers.
- Because China as an offshore sourcing destination is still in its infancy, enterprises must confirm their willingness, risk tolerance and internal capacity for change management to source from China.
- Execute on pilot projects using China-centric pure-play application service providers to determine your acceptable levels of risk and conduct a more-rigorous due diligence on emerging vendors.

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1.0 Introduction

China is rapidly evolving in the IT services and sourcing arena. Based on various sources, including the Chinese Government and the China Council for International Investment Promotion, it is estimated that the amount of outsourcing from Chinese delivery centers ranges from \$1.5 billion to \$3 billion (in 2007). Based on consistently applied calculations, we estimated that annual growth was more than 50% from 2006 to 2007. Conservative estimates for growth rates are approximately 30% to 40% per year throughout the next two to three years, resulting in estimated levels that will exceed \$7 billion by 2010.

In this research, we examine the China-centric supply side (that is, vendor landscape) for application services (which includes consulting, system integration and outsourcing in all areas of application design, development, deployment, maintenance and management). A large number of providers have some type of delivery capacity in China. We detail four categories of providers in the next section of this research. In summary, providers include large, traditional global (multinational) providers, India pure-play providers, native Chinese product-led vendors with IT services practices and China-centric emerging providers, which Gartner refers to as China-centric pure-play application service providers. This last category of providers is the focus of this research.

China-centric pure-play application service providers are comprised of emerging vendors that are relatively smaller in size, do not have well-known brands and are still in growth mode. They are interesting and important because they are reminiscent of well-known Indian vendors that less than seven years ago had all the same characteristics. Circa 2000, the Indian vendors were important emerging providers to watch. Individually, they did not represent a big threat, but collectively they changed the market and redefined long-held norms in the industry. As a result, this research is focused on analyzing a new set of emerging providers whose main common denominator is that China is the epicenter of their delivery center structure. Some are headquartered in China and some in the U.S. Regardless of the headquarters, the majority of their head count and the core source of the IT services creation is in China to export to the U.S. or Europe for client consumption. Thus, we have named this category of IT services providers as China-centric pure-play application service providers (or China pure plays). All these IT services providers have a primary focus on application services. This research does not evaluate business process outsourcing (BPO) or infrastructure providers.

2.0 Background on Market Structure

As clients approach, develop or refresh their sourcing strategies and need to conduct market scans of the IT services provider landscape, one way to begin the process is to look at the various categories of the IT services provider landscape based on their heritage. Here, we provide a high-level overview of the four broad categories of vendors that make up the IT services provider landscape for application services.

2.1 Large, Traditional, Global IT Services Providers

Many large, traditional, global IT services providers — such as Accenture, EDS, Fujitsu and IBM — are pursuing global delivery strategies in China. Each of these service providers (among others) has established facilities in one or more locations in China. All these investments represent a significant indicator of their strategies to capitalize on the growth of China-centric global delivery models (GDMs). These investments also signal that this shift in the use of the

GDM for sourcing beyond India is material, because "megavendors," such as Accenture, EDS and IBM, have the clout, influence and clients to change the market structure.

2.2 India Pure-Play Vendors

This category of service providers is made up of companies that are headquartered in India or defined by a disproportionately large India-centric workforce — for example, Tata Consultancy Services, Infosys Technologies, Wipro Technologies, Cognizant, Satyam and HCL Technologies. These service providers (among others) have established facilities in one or more locations in China. The biggest assets that these organizations have are their methodologies and their competencies to execute a GDM. The challenges include being able to replicate and localize the GDM to China, establishing their brands to attract customers and employees, and establishing front-end relationships with Japanese, Korean and other multinational clients in their domestic markets.

It is also important to note that an increasing number of market forces are demanding that many of these providers move beyond a predominately India-centric model to other destinations, such as China. Some of the market forces contributing to this change include, but are not limited to:

- Rising labor costs in India
- Short-term fiscal benefits of labor arbitrage
- Attrition ratios
- Continual issues on human capital demands, including hiring and retention
- Middle management scarcity in India
- Rupee exchange rate

2.3 Local, Native-Chinese, Product-Led (Hardware or Software) IT Providers

This category of service providers (headquartered in China) is made up of large companies whose primary revenue stream is derived from the sale of software and/or hardware, but they provide support services and system integration for those products, and extend their service portfolios to outsourcing (for example, Digital China, Huawei, Lenovo and Tsinghua Tongfang). Most of the top 10 companies, as ranked by revenue, are relatively larger (more than \$200 million in overall revenue) and have an established customer base. Beyond this initial top tier (as defined by revenue size), many of the other providers are fragmented and vary in revenue size. The advantages they bring are a significant number of local customer accounts and relationships, knowledge of the local market, cultural similarities and a local presence. Challenges include the need to build an understanding and set of business processes and IT service offerings in the consulting and outsourcing arena. This entails huge investments in portfolio strategies, a go-to-market approach, personnel, competency building and methodologies, and other operational requirements.

2.4 China-Centric Pure-Play Application Service Providers

This category of service providers is made up of companies where the majority of the revenue stream is derived from business process and IT services (primarily application services) delivered in a GDM structure. The majority of the IT services are created in China as the primary low-cost destination and exported for client consumption in other markets, such as the U.S., Europe, Japan or any non-China location. The vendors are headquartered in China, or their prime and/or largest delivery centers are in China. Many of these companies are relatively small (revenue is

often below \$100 million or less than IT services revenue). The clear advantage that these providers bring is knowledge of the local Chinese operations, business practices, culture and local presence.

3.0 Service Provider Selection Process

Because this research is focused on China-centric pure-play application service providers that are emerging in the market, we made every attempt to create an extensive list with an array of providers. The list is not meant to be exhaustive because the market is moving quickly and constantly changing, making it a moving target. With this in mind, we used the following general criteria to select the providers appearing on the list:

1. The prime delivery center and/or majority of head count of the emerging providers depicted are in China. Some of the providers are headquartered in China, and others are headquartered in the U.S. or other countries (there is one vendor from Mexico). We did not find any vendors that are headquartered in Europe. We did not exclude any companies based on the location of their headquarters.
2. The primary business focus of the IT services provider strategies was to target nearshore or offshore services as the majority of their portfolio of business. Most of the IT services are created in China as the primary low-cost destination and exported for client consumption in other markets, such as the U.S., Europe, Japan, Korea or any non-China location.
3. Employee head count was generally above 250 full-time equivalents (FTEs). Most of the providers ranged between 500 and 2,000 employees in their China delivery centers. Some providers have reached levels above 4,000 FTEs.
4. The service provider is actively marketing and promoting its IT services with a dominant focus on application services. Application services include consulting, system integration and outsourcing in all areas of application design, development, deployment, maintenance and management.
5. Based on enterprise client inquiries, there is overall market interest and visibility, as determined by serious consideration for evaluation and selections for application services.

3.1 Service Provider Overview Profiles

Depicted in Table 1 is an overview of all the service providers that we profiled in this research. The vendors are listed in alphabetical order, so there is no ranking or rating of the providers. One of the key areas to focus on in the table includes distinguishing between global delivery centers (GDCs) where information was available, as opposed to locations which are primarily used as sales offices. In addition, we have separated the number of personnel located in China-based delivery centers and the total worldwide head count for the specific provider. The head count numbers in China are defined as employees dedicated to IT services work for export to non-China locations. These key items are important in distinguishing providers' capabilities. Table 1 can be used as a starting point for identifying a long list of service providers for potential evaluation and further due diligence. It can be combined with options from the other categories of providers, as well as offshore options from other country destinations. The key evaluation criteria defined by the enterprise organization will be the determinants of the providers for evaluation.

Table 1. Market Overview of China-Centric Pure-Play Application Service Providers

Company, Headquarters (Web Site)	Delivery Center Locations	Sales Offices	Annual Revenue Range in U.S. Dollars (Depicted as Range Because Many Providers Are Private)	Revenue by Service Category	Revenue by Geography	Calendar-Year 2007 Employees (Global)	Calendar-Year 2007 Employees (China)	Planned for Year End (2008)	Attrition Ratio
Achievo, San Ramon, California (www.achievo.com)	China: Beijing, Dalian, Guangzhou, Shanghai, Shenzhen, Wuxi Germany: Böblingen, Dresden, Ingolstadt Japan: Tokyo Canada: Toronto U.S.: San Ramon, California	China: Beijing, Hong Kong, Shanghai, Shenzhen Germany: Böblingen, Frankfurt, Freiburg, Ingolstadt, Munich, Wolfsburg Japan: Tokyo, Nagoya Canada: Toronto U.S.: San Ramon, California	\$50 Million to \$100 Million	App. Dev. (AD): 80% IT Service Mgmt.: 20%	North America and Europe: 43% Japan: 51% Rest of the World: 6%	1,800	1,400	2,400	7%

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Augmentum, Shanghai, China (www.augmentum.com)	China: Shanghai, Beijing, Wuhan U.S.: Foster City, California	China: Shanghai, Beijing U.S.: Foster City, California	\$30 Million to \$50 Million	Software Product and AD Services: 50% Quality Assurance (QA) and Test: 20% Sustaining Engineer.: 10% Embedded Software Dev: 20%	U.S.: 75% China: 25%	1,250	1,200	1,600	16%

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Beyondsoft, Beijing, China (www.beyondsoft.com)	China: Beijing, Shanghai, Wuhan, Tianjin, Dalian, Chengdu, Chongqing Japan: Tokyo India Delhi, Mumbai U.S.: Seattle, Washington; Denver, Colorado; Vancouver, Washington	China: Beijing, Shanghai U.S.: New Jersey; San Francisco, California Tokyo: Singapore	\$50 Million to \$100 Million	R&D Services: 54% AD: 12% Enterprise Apps. (ERP): 32% BPO: 2 %	U.S.: 59% Europe: 1% Japan: 7% China: 24% Others: 9%	2,500	2,050	4,000	12%
Bleum, Shanghai, China (www.bleum.com)	China: Shanghai, Chengdu, Wuhan China	China: Shanghai U.S.: California, New Jersey	Less Than \$30 Million	AD: 50% App. Outsourcing: 35% R&D: 15%	U.S.: 80% Europe: 20%	347	340	600	11%

Company, Headquarters (Web Site)	Delivery Center Locations	Sales Offices	Annual Revenue Range in U.S. Dollars (Depicted as Range Because Many Providers Are Private)	Revenue by Service Category	Revenue by Geography	Calendar-Year 2007 Employees (Global)	Calendar-Year 2007 Employees (China)	Planned for Year End (2008)	Attrition Ratio
Chinasoft International, Beijing, China (www.chinasofti.com)	China: Beijing, Shanghai, Dalian, Guangzhou, Shenzhen, Changsha, Wuhan, Kunming, Wuxi, Chongqing, Xiamen Japan: Tokyo U.S.: Seattle, Washington; Princeton, New Jersey	China: Beijing, Shanghai, Dalian, Guangzhou, Shenzhen, Changsha, Wuhan, Kunming, Xiamen Japan: Tokyo U.S.: Seattle, Washington; Princeton, New Jersey	\$50 Million to \$100 Million	Staffing: 38.2% AD: 18.7% Indepen. Testing Service: 14.1% BPO: 14.1% Computer-Aided Design: 8.8% Others: 5.9%	U.S.: 70.4% Japan: 22% Europe: 7.6%	Total: 4,600 Outsourcing: 3,500	Total: 4,480 Outsourcing: 3,380	5,000	22%
Dalian Hi-Think Computer Technology, Corp. (DHC), Dalian, China (www.dhc.com.cn)	China: Jinan, Beijing, Tianjin, Shenzhen Japan: Tokyo	China: Beijing Japan: Tokyo	\$50 Million to \$100 Million	Software Dev.: 92.4% Software Services: 4.9% System Integration: 2.7%	Domestic: 19% Overseas: 81%	2,917	2,802	4,000	12%

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Dextrys, Wakefield, Massachusetts (www.dextrys.com)	China: Suzhou, Shanghai Key China Office: Hong Kong Key U.S. Office: Wakefield, Massachusetts	U.S.: Los Angeles, California; New York, New York; Atlanta, Georgia; Brookfield, Connecticut	\$50 Million to \$100 Million	AD and Implemen.: 60% Product Engineering and R&D: 40%	U.S.: 75% China: 25%	1,200	800	1,400	Not Disclosed
Freeborders, San Francisco, California (www.freeborders.com)	China: Shenzhen, Guangzhou, Wuxi U.S.: San Francisco, California; New York, New York	U.S.: San Francisco, California; New York, New York; Boston, Massachusetts; Cleveland, Ohio; Atlanta, Georgia; Seattle, Washington; Greensboro, North Carolina	Less Than \$30 Million	AD: 30% App. Outsourcing: 30% Application Testing: 20% Business Intelligence: 10% AS/400 Support: 10%	U.S.: 96% All others in Asia/Pacific: 4%	500	450	750	19%

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iSoftStone Information Service Corporation, Beijing, China; Boston, Massachusetts, U.S.; Tokyo, Japan (www.isoftstone.com)	China: Beijing, Shanghai, Wuhan, Dalian, Wuxi, Tianjin, Shenzhen, Nanjing, Guangzhou Japan: Tokyo, Kyushu U.S.: Seattle, Washington	China: Beijing, Shanghai, Shenzhen, Gusngzhou, Tianjin Japan: Tokyo Korea: Seoul U.S.: Boston, Massachusetts; Seattle, Washington	\$50 Million to \$100 Million	Consulting and Solutions: 35% AD, Maint. and ERP: 50% Testing: 10% BPO and Others: 5%	China: 38% U.S. and Europe: 37% Japan and Korea: 25%	3,500	3,300	5,000	13.7%
Longtop International, Xiamen, China (www.longtopinternational.com and www.longtop.com)	China: Shanghai, Beijing, Chengdu, Guangzhou North America: Seattle, Washington; Toronto, Canada	North America: Seattle, Washington; Princeton, New Jersey; Toronto, Canada China: Shanghai, Beijing, Xiamen, Chengdu	\$100 Million to \$250 Million	Not Disclosed	China: 60% to 70% U.S.: 25% to 30% Canada: 3% to 5% Europe and Middle East: 1% to 2%	1,600	1,400	2,000	10% to 12%

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Objectiva Software Solutions (business unit of EMC Corporation), Carlsbad, California (www.objectivasoftware.com)	China: Beijing and Xi'an	U.S.: Carlsbad, California; San Francisco, California China: Beijing	Less Than \$30 Million	R&D: 52% Enterprise Apps. (ERP): 48%	North America: 96% Europe: 2% All Others in Asia/Pacific: 2%	510	450	600	Not Disclosed
SinoCom Software Group, Beijing, China (www.sinocom.cn/enwww/index.htm and www.sinocom.jp)	China: Beijing, Shanghai, Hangzhou, Chengdu, Dalian, Jinan, Jiaxing Japan: Tokyo, Osaka	China: Beijing, Shanghai, Chengdu, Dalian Japan: Tokyo, Osaka Canada: Toronto	\$50 Million to \$100 Million	AD: 90% App. Outsourcing: 7% IT Support Services: 3%	Japan: 95% U.S.: 5%	3,300	3,000	3,700	12%

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Softtek (China-based legal entity is Softtek Asia, which was formerly known as IT United), Worldwide headquarters: Monterrey, Mexico; Softtek Asia headquarters: Beijing, China (www.softtek.com)	China: Nonglobal Delivery Locations Are in Xian and Shanghai Worldwide GDCs: Mexico: Aguascalientes, Monterrey, Mexico City, Ensenada Brazil: Sao Paulo, Sao Leopoldo Spain: A Coruna China: Beijing Argentina: La Plata	China: Beijing, Shanghai Global Sales Offices Span More Than 20 Countries	Softtek Global: \$250 Million to \$500 Million Softtek Asia: Less Than \$30 Million	AD: 50% App. Outsourcing: 30% Infra. Outsourcing : 20%	Softtek Asia 90%: China 10%: Rest of Asia/Pacific	6,000	250	Worldwide: 6,900 Resources 300 (in China)	Worldwide: 17%

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Symbio Group, Beijing, China (www.symbio-group.com)	China: Beijing, Chengdu, Hangzhou, Shanghai, Taipei U.S.: Silicon Valley, California; San Jose, California	Asia: Tokyo U.S.: Boston, Massachusetts; Chicago, Illinois; Dallas, Texas; Los Angeles, California; San Jose, California; Seattle, Washington; Washington DC	\$30 Million to \$50 Million	Develop: 40% QA: 40% Technical Support: 10% Globalization: 10%	U.S.: 85% Europe: 5% Asia: 10%	850	750	1,500	17%

Company, Headquarters (Web Site)	Delivery Center Locations	Sales Offices	Annual Revenue Range in U.S. Dollars (Depicted as Range Because Many Providers Are Private)	Revenue by Service Category	Revenue by Geography	Calendar-Year 2007 Employees (Global)	Calendar-Year 2007 Employees (China)	Planned for Year End (2008)	Attrition Ratio
VanceInfo, Beijing, China (www.vanceinfo.com)	China: Beijing, Shanghai, Shenzhen, Wuhan, Chengdu, Tianjin, Dalian, Hong Kong, Nanjing, Hangzhou Japan: Tokyo U.S.: Seattle, Washington; San Francisco, California; San Diego, California	China: Beijing, Shanghai, Shenzhen, Hongkong Japan: Tokyo U.S.: San Francisco, California; New York, New York; Seattle, Washington	\$50 Million to \$100 Million	R&D: 57% AD: 18% App. Outsourcing : 8% Enterprise Apps. (ERP): 15% BPO: 2 %	U.S.: 63% Europe: 12% Japan: 12% China: 13%	3,750	3,700	5,100	14%

Source: Gartner (October 2008)

Depicted in Table 2 are several other vendors that qualify as China-centric pure-play application service providers that Gartner has analyzed and interviewed in China. However, at the time of publication, Gartner was unable to reach these vendors to factually confirm their information. Thus, the data in the table represents Gartner estimates, combined with data available on the vendors' Web sites.

Table 2. Gartner Estimates of Other Vendors That Were Not Able to Confirm Their Data at the Time of Publication

Company, Headquarters (Web Site)	Delivery Center Locations	Sales Offices	Annual Revenue Range in U.S. Dollars (Depicted as Range Because Many Providers Are Private)	Revenue by Service Category	Revenue by Geography	Calendar-Year 2007 Employees (Global)	Calendar-Year 2007 Employees (China)	Planned for Year End (2008)	Attrition Ratio
Bamboo Networks (www.bamboonetworks.com)			\$30 Million to \$50 Million						
Baosight Software (www.baosight.com)			\$50 Million to \$100 Million			3,200			
BroadenGate, Shanghai, China (www.broadengate.com.cn)	Telecom ODC: Shenzhen, Nanjing ERP System Service ODC: Beijing Japanese Project ODC: Shanghai.	Shenzhen, Nanjing, Shanghai, Wuhan, Beijing	30 Million to 50 Million			750			
hiSoft Technology International, Dalian China (www.hisoft.com)			\$50 Million to \$100 Million			3,300			
Neusoft (www.neusoft.com)			\$250 Million to \$500 Million			13,000			

Source: Gartner (October 2008)

RECOMMENDED READING

"Dataquest Insight: Profile of 10 China-Based Pure-Play Application Service Providers"

"Analysis of China as an Offshore Services Location"

"Market Overview: IT Services Providers, China, 2007"

"Dataquest Insight: China's Software Offshore Service Market Environment of Four Key Cities"

"The Emerging Buyer and Seller Dynamics for IT Services in China"

"Dataquest Insight: Progress in China's Export Services Industry Creates Opportunities"

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