

OUTSOURCING IN KOREA AND FUTURE PROSPECTS

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Expanding Since the Late 1980s

Outsourcing is a strategic restructuring tool to strengthen core competences by cutting some operational affairs which were previously essential, but have now become unnecessary from an overall strategic viewpoint. Its previous concept was simply a transactional activity between assembler and suppliers, such as procuring and supplying some resources (i.e., general parts and simple services) from suppliers outside the firm-frontier.

The typical strategic outsourcing nowadays emerged from the wide diffusion and the successful utilization of information technology (IT) as means of re-engineering. In 1989, Eastman Kodak outsourced its information systems to IBM to be more cost-competitive. Recently, branches of outsourcing are becoming wider and more varied: from management of factory and buildings, transportation and professional services to administrative affairs (which was traditionally an essential insourcing affair), development, operation and maintenance of information systems, R&D, engineering and design, manufacturing, and marketing, among others. In light of this trend, the outsourcing market is widening.

Current Status of Outsourcing in Korea

The economic conditions in Korea under the IMF program have been bad for businesses, but good for the outsourcing market. There have been four main factors that have recently

influenced the market trend in Korea.

First, the law has been changed to support the magnification of the outsourcing market. For example, an act providing increased labor flexibility was passed by the National Assembly and became effective from July 1998. This will certainly help firms to utilize outsourcing more easily in the labor market.

Second, some functions of the public sector (67 functions under 24 ministries and departments) will be transferred to private sector within 1999 to fulfill the reform of the government sector. For example, reception and guides at the Ministry of Government Administration, and security and operation of museums in the Ministry of Culture & Tourism will be open to bidding among the private sector.

Third, private firms are increasingly resorting to outsourcing to complement their efforts to restructure themselves by downsizing and spin-offs. They are striving to strengthen their core competences with various professional services supplied by outsourcers. A typical example of outsourcing in 1998 was the move by large firms such as SK and Korean Air to outsource to IBM the implementation, operation and maintenance of their information systems for 5~10 years.

Last, the growing need for outsourcing is creating new suppliers in a specific outsourcing realms. New and specialized young firms are emerging in areas such as labor supply, design, general operators, public relations, R&D, and others. Most of these are small and in the infant stages, although there are many large companies in some outsourcing service industries as system integration, security and advertising.

The demand for outsourcing has increased greatly in the private sector as well as the public sector since late 1997, and many new suppliers are emerging following this demand, but many are still not attractive enough to domestic users.

Opportunity for Suppliers in Korean Outsourcing Market

According to a survey of 177 firms in November 1998 by HRI, about 40% of Korean firms outsource specific services and operation from independent suppliers. This is much lower than the levels found in the U.S. (90%) and Japan (77%). But conversely this means that there is vast room for expansion of the outsourcing market in Korea. Experienced foreign suppliers will have much opportunity to service Korean outsourcing customers, because there are few competitive suppliers in

most service industries.

As of yet, there is no outsourcing association to define, survey a market, and collect data in Korea, unlike the U.S., and there are no available accurate statistics to show the exact size of the outsourcing market. HRI has tried to define and infer the market size in Korea by looking at not the outsourcing market itself but the "outsourcing-related" market (which may different is size than the actual outsourcing market).¹⁾ According to HRI's findings, the market size was 19.5 trillion won (about \$17.7 billion) in 1996, and it will grow to 100.5 trillion won (\$90.0 billion) in 2001.

HRI predicts that in the near future, the need for outsourcing will increase the most in the areas of information systems and labor supply. In the future, the outsourcing market will expand in traditionally in-company areas such as training, human resources, and administrative affairs as well. **VIP**

<Outsourcing-Related Market and Its Prospects in Korea>

	1990	1993	1996	2001(e)
establishments(No., %)	24,386	35,531(13.4)	50,575(12.5)	92,770(12.9)
workers(person, %)	192,843	311,018(17.3)	833,721(38.9)	4,310,542(27.6)
annual sale(trillion won, %)	4.0	7.3(22.2)	19.5(38.8)	100.5(30.2)

Source: National Statistical Office (ROK), *Report on Census of Service Industries, 1991 · 1994 · 1998*

note: 1) Outsourcing-related industries refer to categories 841, 842, 843, 844 under the Korean Standard Industrial Classification (KSIC) codes as of 1990 and categories 72 and 74 under the revised KSICs as of 1993 and 1996.

2) The figures in parentheses () refer to average increase rate per year

3) HRI estimates

1) "Outsourcing-related" industries refer to categories 841 (legal, accounting, and other clerical services), 842 (architectural, engineering and technical testing services), 843 (survey information related services), and 844 (other business services, except machinery and equipment rental and leasing) under the Korean Standard Industry Classification (KSIC) codes as of 1990 and categories 72 (computer and related activities) and 74 (other business activities) under the revised KSICs as of 1993 and 1996.