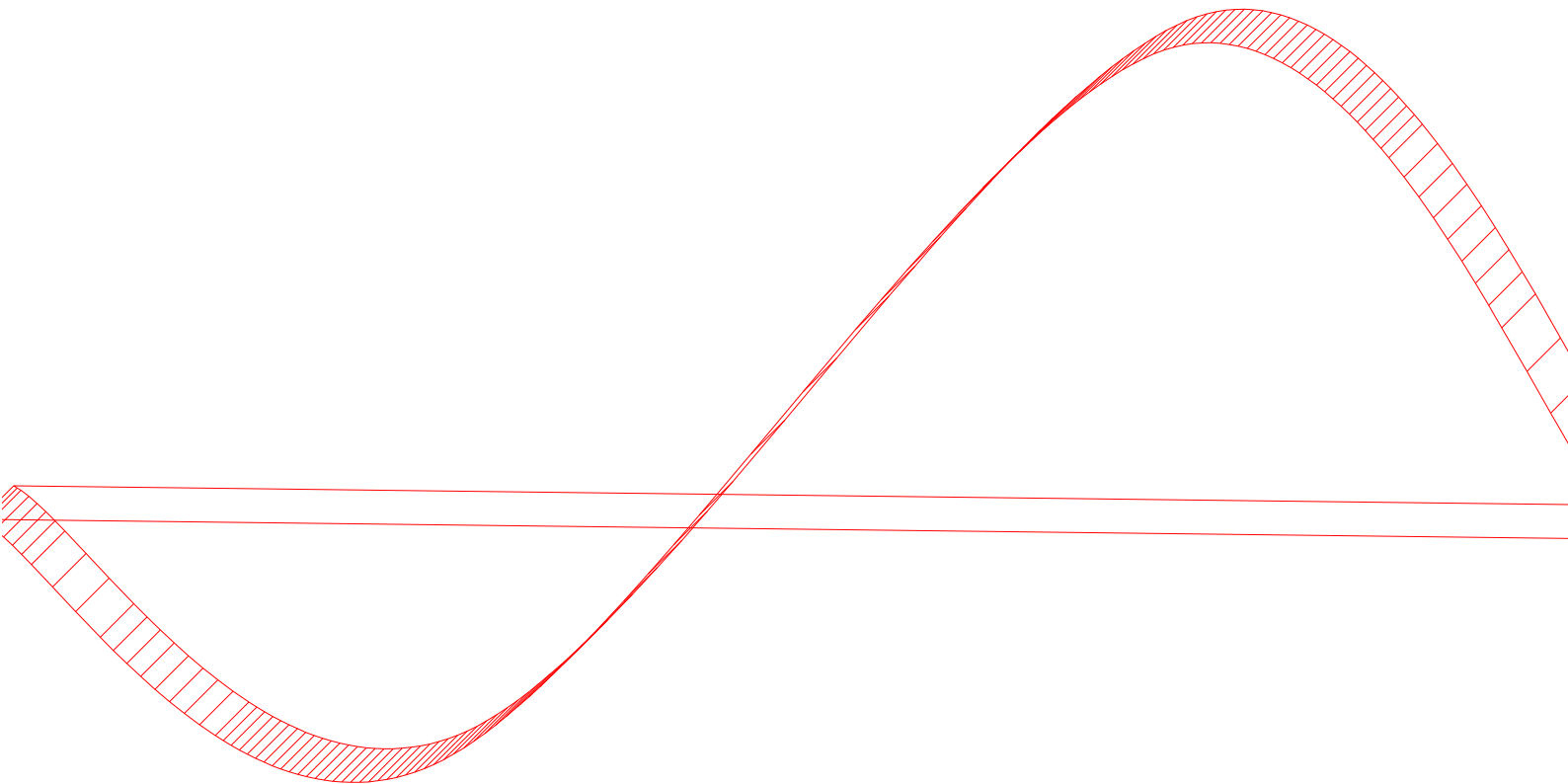


# IT-Offshoring to India

A driver for efficiency or a high-risk bubble?



A whitepaper from Globals Inc.

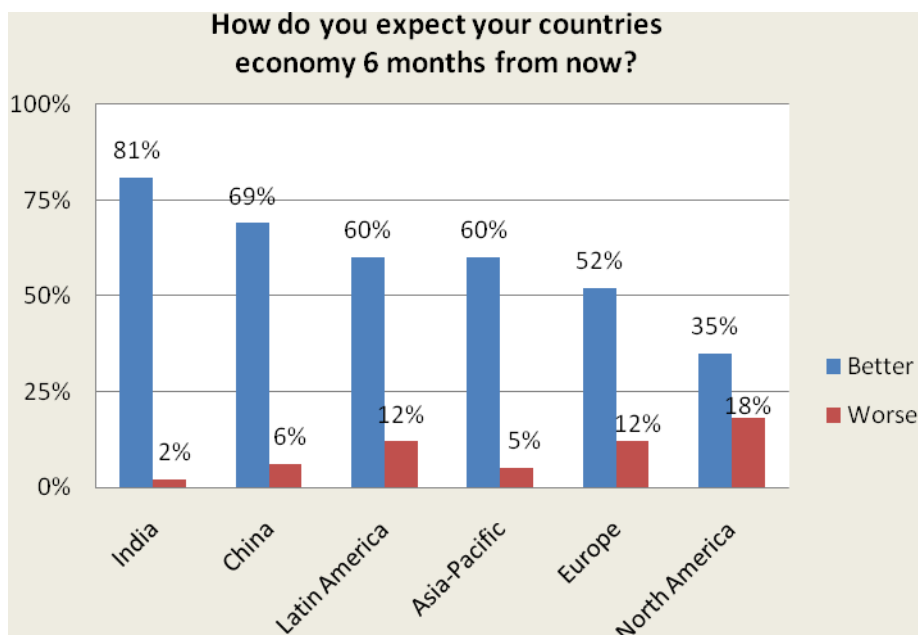


## The emergence of a true global economy

The rate at which companies lose their leadership positions doubled from the mid-'70s to the mid-'90s.<sup>1</sup> Additionally to that a lot of markets become global in various ways. The growing competition, the demand of the emerging countries, economical liberalization and growing importance of capital markets, new communication technologies and efficient logistic systems drives the numbers of interconnections worldwide.

The traditional value-chains are deconstructed by network-based business-models, supranational markets and higher competition.<sup>2</sup> The emerging countries, like Brazil, Russia, India and China (BRIC) are the new powerhouses of global growth and are transforming from cheap production sites to more and more innovative competitors.<sup>3</sup>

Since the beginning of significant global sourcing activities in the late 1980s India is a front-runner of globalization. The biggest democracy of the world is still preferred by investors because of its high-educated English-speaking workforce, its process maturity, its political stability and its investor-friendly atmosphere.



Top Executive Survey, June 2007. Source: McKinsey.

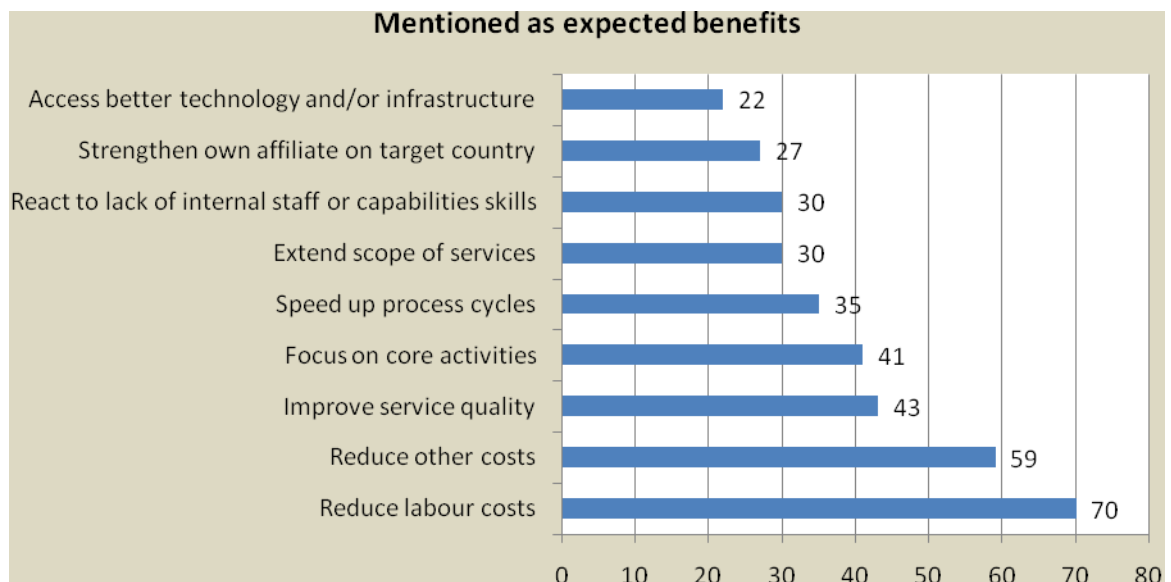
<sup>1</sup> McKinsey 2006.

<sup>2</sup> The Boston Consulting Group 1998.

<sup>3</sup> The Boston Consulting Group 2007.

## Fascinating and dangerous at the same time – What makes offshoring successful?

The main advantage of offshoring seems to be the difference of cost of labor between the western and developing countries. But behind this obvious fact, there is a lot of more potential for organizations to get more competitive.



Top Executive Survey, 2004. Source: United Nations.

Although the advantages of offshoring seem to be evident, just 15 % of major companies are planning to offshore their activities to create higher value.<sup>4</sup> The same

*"The vendors say you can throw it over the wall and start saving money right away. As a result I've heard of CIOs who have tried to go the India or China route, and nine months later they pulled the plug because they weren't saving money. You have to build in up to a year for knowledge transfer and ironing out cultural differences."*

*Hank Zupnick, CIO of GE Real Estate,  
CIO Magazine 2003*

study figured out that 49% could not raise their prices because of low-cost competitors. If lean cost-structures are so essential, why offshoring is not their first choice?

Offshoring is not a miracle, but the result of well-defined strategy. Although the Indian market, is much more experienced compared to other BRIC markets, the choice of a reliable vendor with a transparent culture is

essential to profit from the advantages of offshoring. The most important factor is the communication between the vendor and the client across time-zones, cultural

<sup>4</sup> McKinsey 2007.

area, interests, expectations and experiences. A lot of the low-cost vendors are able to set their prices, due to lack of project management methods, measurable quality standards and high-skilled employees.

But also inexperienced clients do not calculate the efforts of contracting, troubleshooting, communication and preparation and underestimate the Total Costs of Offshoring (TCO).

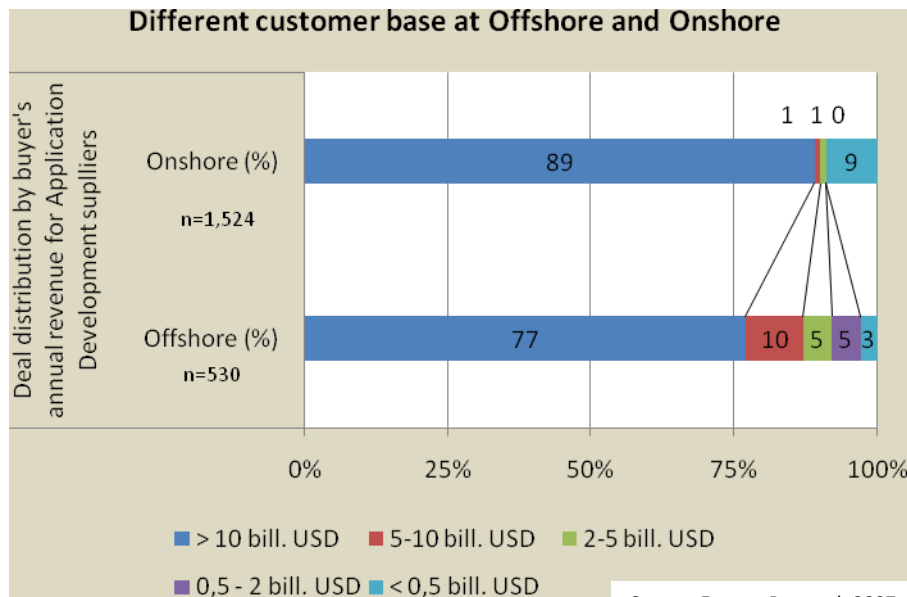
Hidden Costs	Best Case	Worst Case
Vendor selection	0,2%	2,0%
Transitioning the work	2,0%	3,0%
Layoffs and retention	3,0%	5,0%
Lost productivity/Cultural issues	3,0%	27,0%
Improving development processes	1,0%	10,0%
Managing the contract	6,0%	10,0%
<b>Total hidden costs</b>	<b>15,2%</b>	<b>57,0%</b>

Source: CIO Magazine 2003.

Actually Offshoring is mainly driven by enterprises and less by small and medium sized businesses (SMB). The main reason is that the vendors are focused on enterprises following their ,penetrate and radiate'-strategy.<sup>5</sup> Another important factor is the missing understanding of business needs, corporate culture and organizational structure of SMBs.

Especially medium-sized businesses see Offshoring as a valuable option to compete in international as well as national markets. This dynamic is especially rooted in the relative higher share IT takes in the cost structure of SMBs compared to enterprise on the one hand and the high cost of outsourcing in their homeland on the other hand. The small-sized businesses are still under represented in the IT-Offshore market, although they could significantly grow if they would use Offshoring.

<sup>5</sup> Everest Research 2007.



But only some vendors are reacting on the special needs of this segment and offers simplified high-quality Offshoring solutions. The customers value this supply by significant growth rates over the last years.

Finally it hardly depends on the vendor and the model if Offshoring becomes a success story for an organization. Additionally, the structural advantages are not only still true, but often not fully recognized by the competition.

## Why an Offshoring Development Center is more than just doing Outsourcing abroad

Contrary to the normal models an Offshoring Development Center (ODC) works like an expansion of the client organization. The whole team is staffed according to the specific requirements of the client and is fully committed to his needs. The long-term engagement style of ODC reduces a lot of the risks and hidden costs. Current studies figured out that an ODC saves more than 15% compared to a captive Offshoring engagement.<sup>6</sup> The main reason is that the vendors are closer to the market as a foreign company. A main advantage, which is often ignored, is that western companies are able to improve the expertise of your company by an ODC despite the lack of talents at their home labor markets. Actually the emerging economies have 33 million university-educated young professionals, this more than twice as much as at the devel-

<sup>6</sup> CIO Magazine 2007.

oped countries.<sup>7</sup> Additionally to that the development process of new products becomes much faster, if an ODC is enforcing the clients' development team. This model creates a virtually 24/7 development using the time-zone differences and smart shift-management. R&D based business models, which use this time advantage will be much more competitive in modern ICT markets with their short life-time cycles and fast moving technologies.

Since the idea emerged in 2003 a lot of different ODC-models are being offered, but the clients buying center needs a clear idea about ODC as well as the own claims and resources to make the right choice. To get the full advantages of an ODC it is essential to make sure:

- ✓ That communication, which the most critical factor in cooperation, is embedded in well-defined and proven processes.
- ✓ That a Total Quality Management is installed not only at the ODC, but also at the vendors firm.
- ✓ That the vendor has experience with the mentality of the client cultural sphere and with comparable products and industries.
- ✓ That a professional project management and engineering philosophy is established.
- ✓ That a fair and transparent legal framework is offered.
- ✓ That intellectual property is protected by international laws.
- ✓ That the OCD infrastructure is independent from power breakdowns and has an industrial standard bandwidth.
- ✓ That the vendor is not only focused on costs, but also has an ambitious internal talent management.

Excellent experts are rare, especially at the booming Indian market. The education and industry standards are not same as in western economies. A lower productivity level can have a huge impact on the efficiency of an offshore investment. The competition among the OCD suppliers is big enough to create an unreliable low-cost segment. Some vendors are offering standards, which are a priori impossible, like chang-

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<sup>7</sup> McKinsey 2006.

ing objectives at every time of the project or improve quality, save time and reduce

*It's not a cheap proposition in terms of set-up costs either. (...) It took a year to recoup those costs, but David Wood, Otis's director of systems development, says it was worth every penny for the efficiency, cost-effectiveness and productivity gains. "For us, it's just a better way to do things," Wood says.*

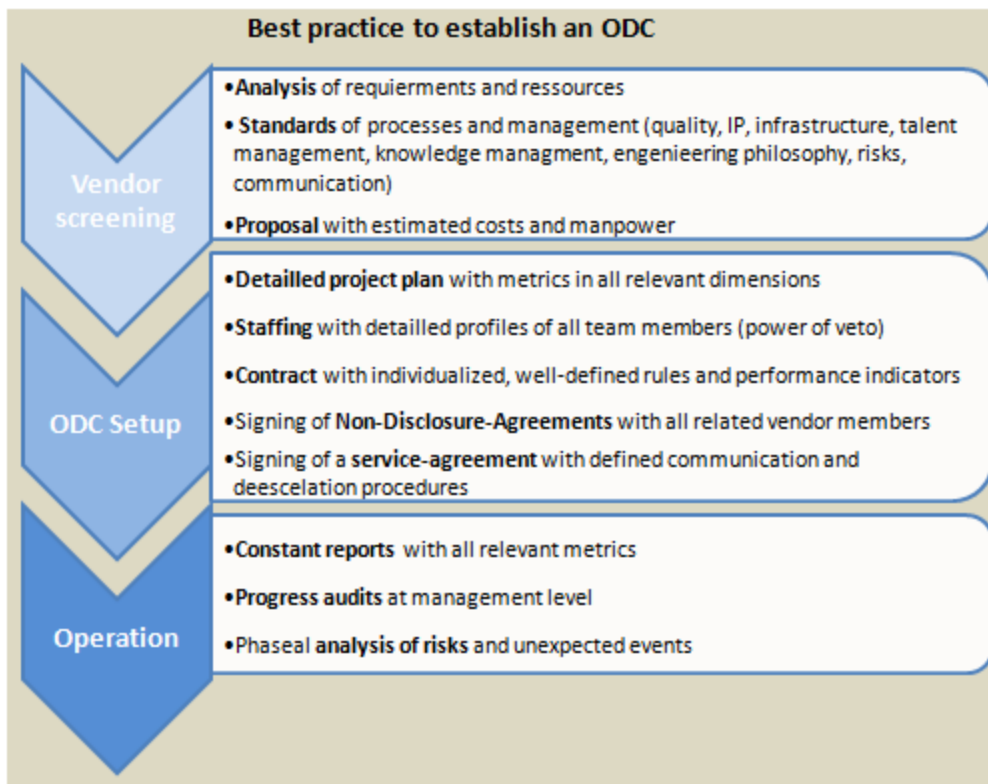
*CIO Magazine 2003*

costs at the same time. Some companies made the mistake to work with the low-cost segment and had a cruel hang-over as they woke up.

If an ODC is finally installed the process of vendor management still continues as shown in the figure below. Clients should not make the mistake and think industrial services are like car-washing. A high-quality product needs a lot of interaction, because of the high complexity

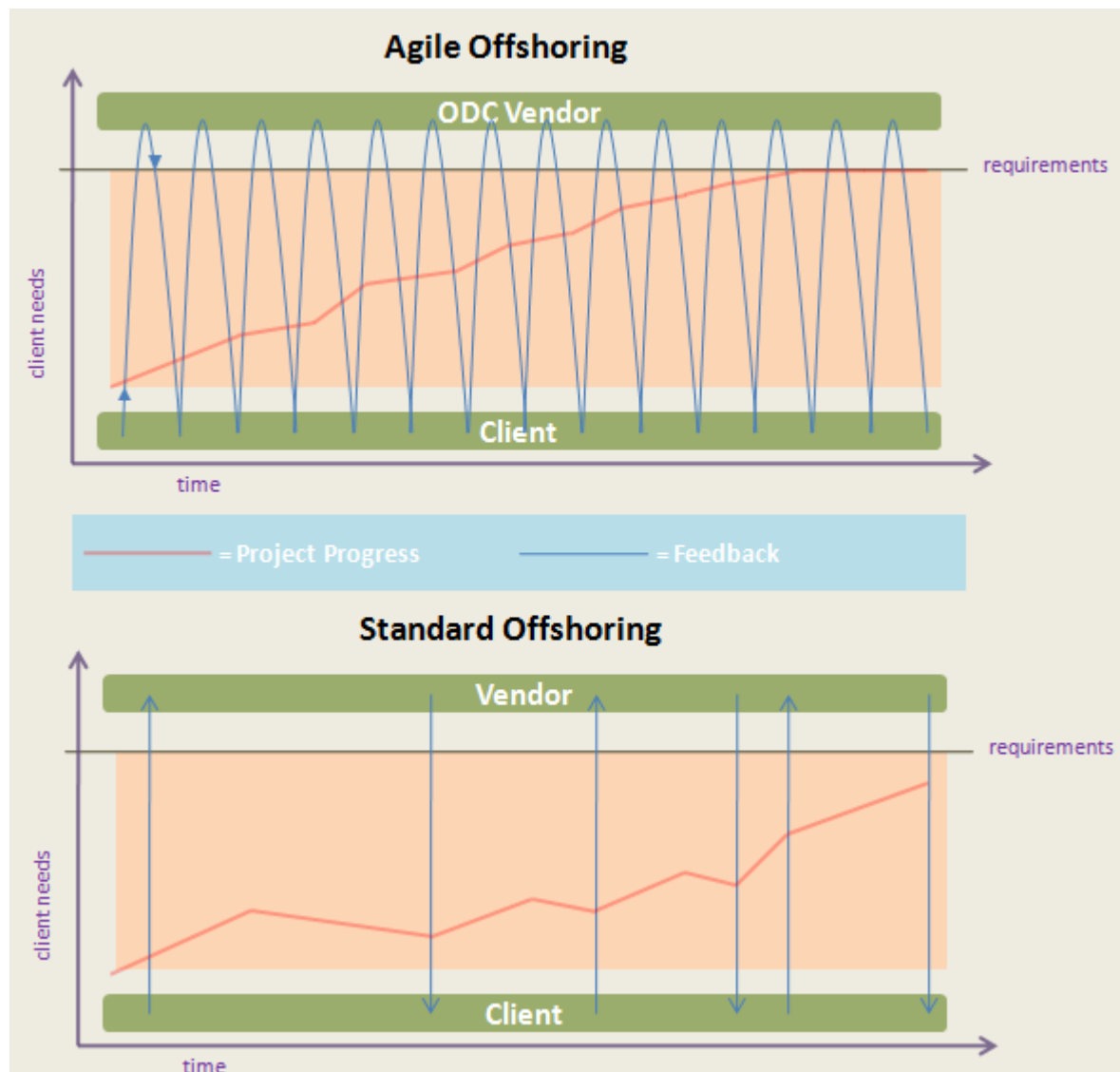
of sophisticated, interconnected requirements and these products have their prices, although they are still much lower as in the G8 countries.

Our experience and our research help us to develop an ODC model, which minimize the risk by using well-defined and proven processes and standards.



## Agile Offshoring – The client centered way

As we mentioned above, communication is the key to success in Offshoring. The dedication of an own development team managed by an experienced vendor like in our best-practice-model is the best design. But there is also the other side of the coin: The mechanics behind the design. We find out that using the principles of agile development and extreme programming is the most efficient and effective way to manage the relation between client and vendor. To put in a nutshell: It is the philosophy of communication based iterative work with a high degree of commitment.



The combination of the ODC in the design dimension and the Agile Offshoring in the workflow dimension enable the vendor and the client to minimize the risks as well as the related hidden costs of Offshoring and give them full access to the valuable advantages.

## About us

Globals Inc is a multinational company founded in the year 2000 by Mr. Suhas Gopinath at the age of 14 years at California, USA. Globals offers cost effective world class quality solutions in web, software, mobile and multimedia. Globals has established offices in more than 11 countries. Till date Globals has served more than 200 clients worldwide.

We have always placed quality over quantity, mind over machine and unity over uni-opinion. Our firm is one of the few places on the earth where egoistic thoughts are out of question. There is a lot of enthusiasm among the members to perform. This makes our work more streamlined and solutions meet the prescribed time boundary.

The focal point of the firm is to provide a global arena for the youngsters to perform at the corporate and the industry level giving emphasis to the skill sets of the individuals than their academic qualifications.

We believe in doing things through proper channels for optimum results. Nothing else would explain serving more than 200 clients worldwide. We at Globals understand we have miles to go before even looking back. Hence we do not rest on our prior laurels. Laurels come and go, progress is the only thing on our minds, and will be the same for the time to come.

In a nutshell we are Globals, setting the global trend.

## Contact us

Amruta Desai  
Vice President, Strategy & Marketing  
Globals Inc.

**Email:** [sales@globalsinc.com](mailto:sales@globalsinc.com) / [amruta@globalsinc.com](mailto:amruta@globalsinc.com)

**Web:** <http://www.globalsinc.com>

**Phone:** +91 80 4127 5853 / +1 650 209 4853