



[www.process-alliance.org](http://www.process-alliance.org)

## ***Market Situation and Guidelines for Near- and Offshoring***

***Armin Heinzl, Michael Heym***

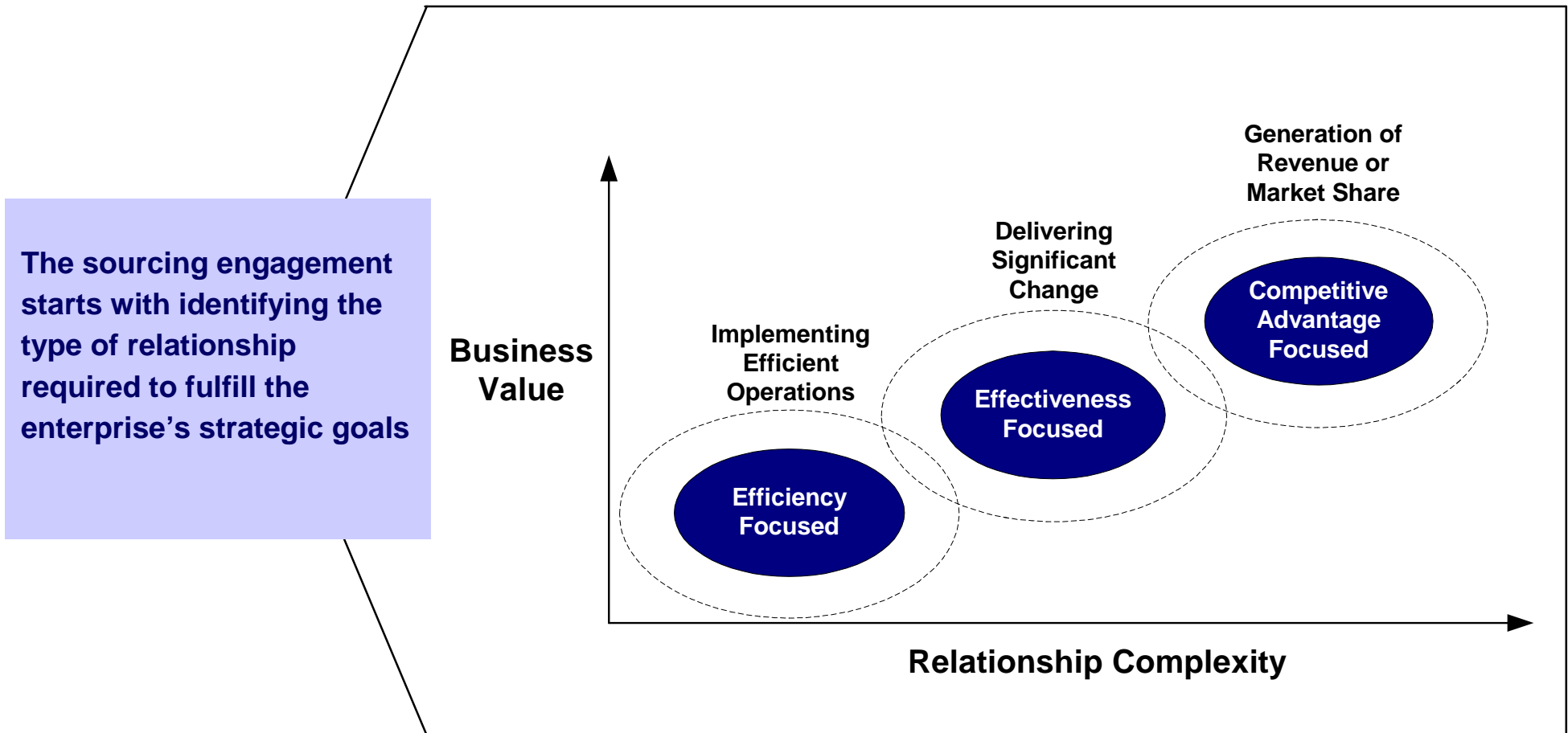
***PAI Foundation Meeting  
26<sup>th</sup>/27<sup>th</sup> of January 2005  
Hotel Louis C. Jacob, Hamburg***

**NAVISCO | AG**  
Sourcing Professionals

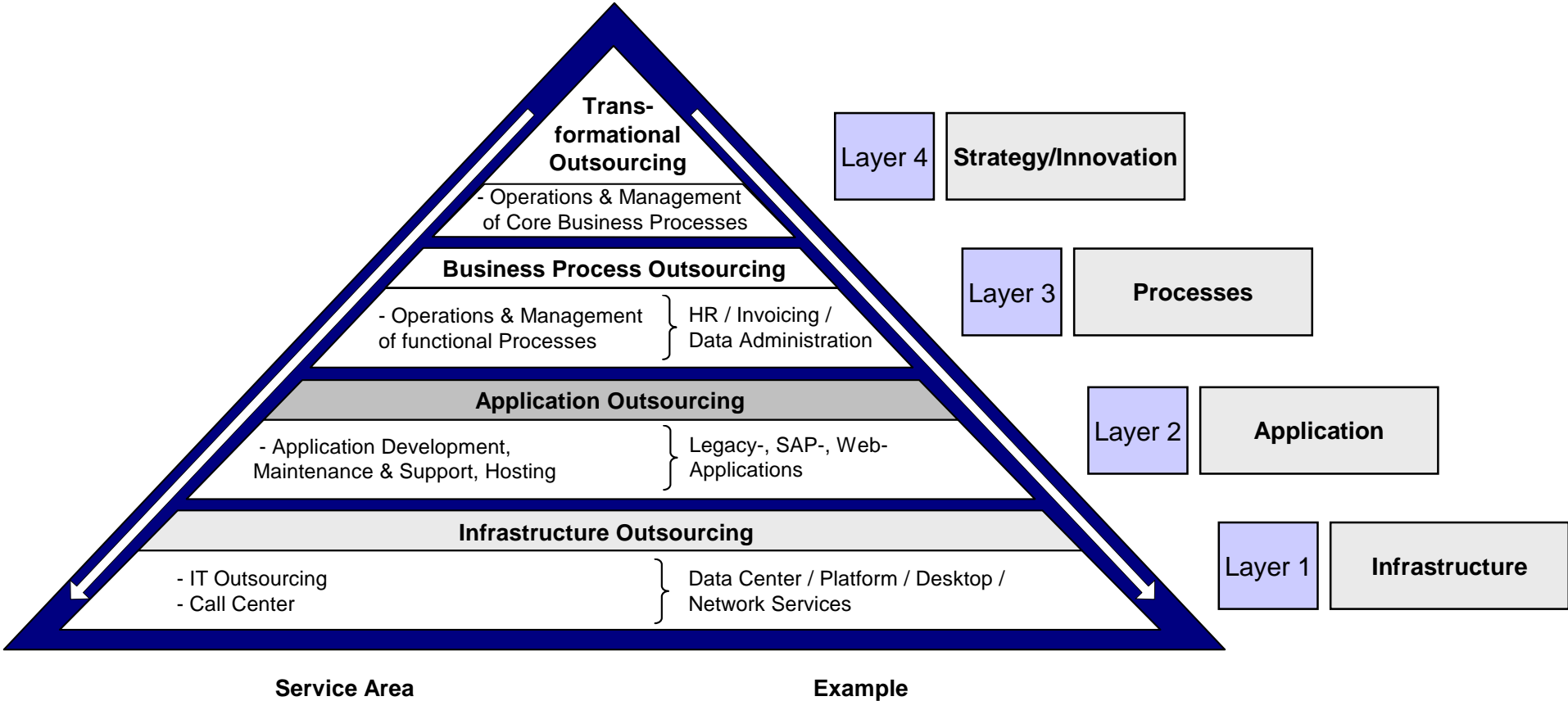
## Structure of Study

- n **Introduction**
- n **Market Situation Near- and Offshoring in Europe**
- n **Survey Results**
- n **Evaluation and Guidelines**
- n **Discussions**

## There exist three Types of Sourcing Relationships



# Outsourcing Services are focusing on four Levels

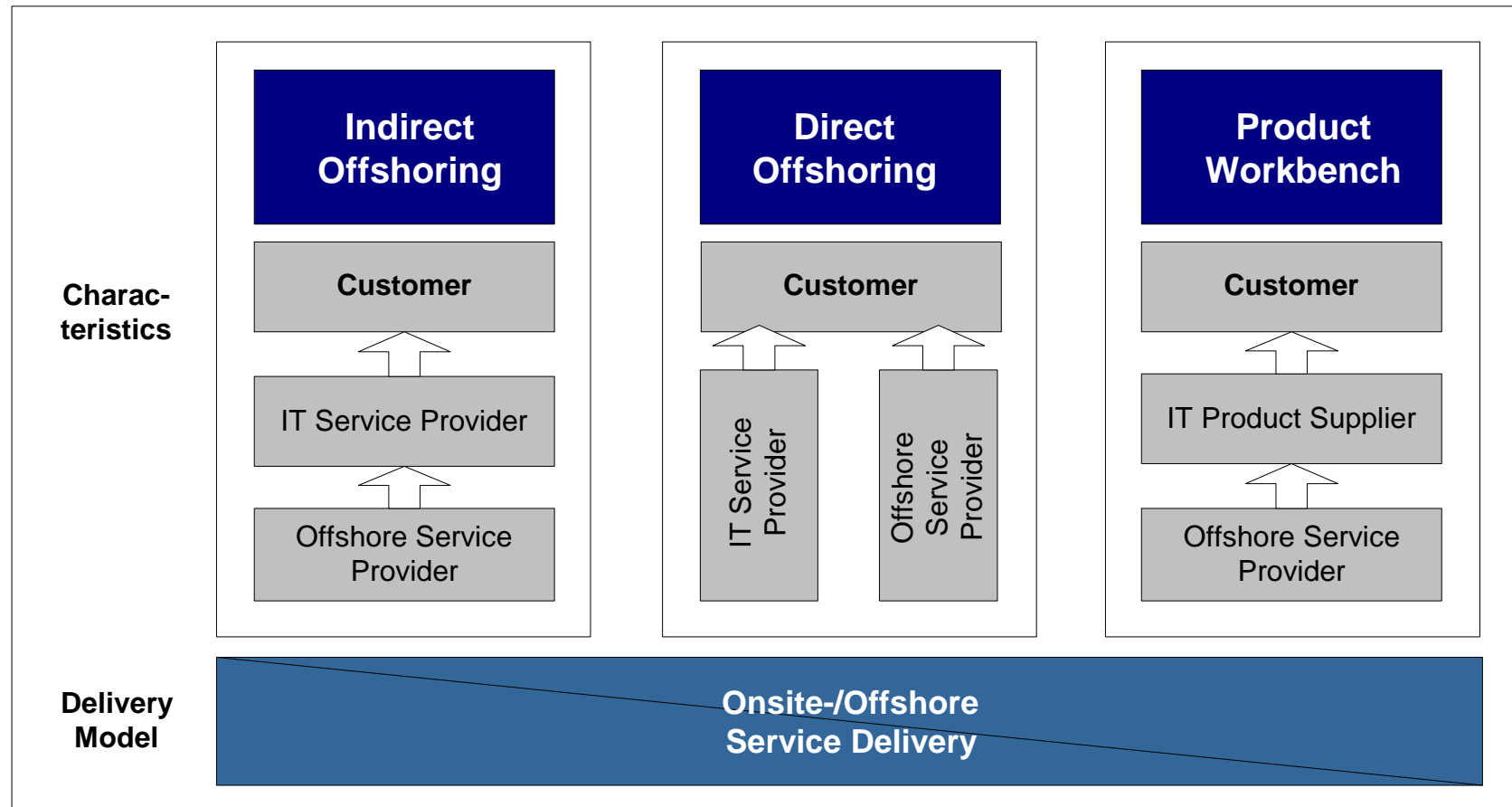


## Cost Savings by Application Offshoring varied between 10% and 35% depending on the maturity of the relationship



- n Evaluation of daily blended rates for application Offshoring including expenses for travel, living, and the onsite / offshore ratio shows savings from 500,- to 800,- € between traditional ESP and offshore proposals
- n Additional costs will arise for management, quality assurance and adapting the own organization
- n Depending on the duration and maturity of the partnership the savings increase from 10% up to 35% for application development, maintenance and support

# Different Offshoring Delivery Models



# Structure of Study



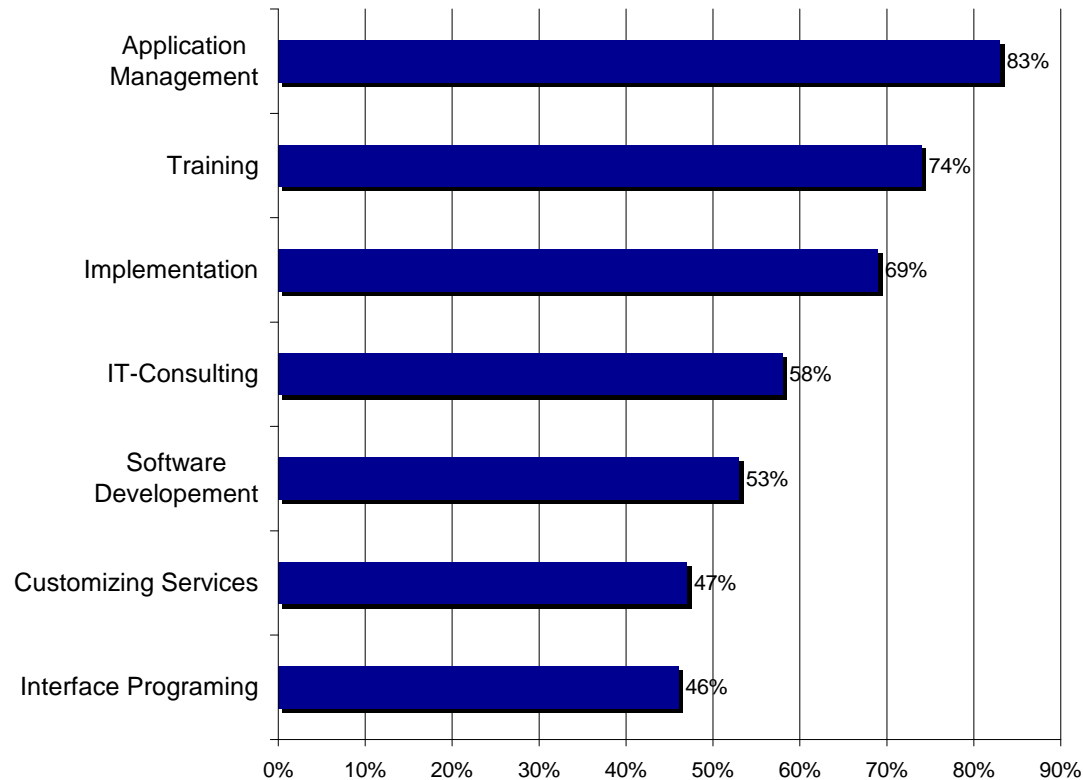
- n Introduction
- n **Market Situation Near- and Offshoring in Europe**
- n Survey Results
- n Evaluation and Guidelines
- n Discussions

## Europe follows the leading US Market with an share of about 15% to 20% from the Total Offshoring Market



- n The US market is the strongest and experienced market (70%-80%)
- n Finance sector, telecommunication, technology and production represent 75% of the total offshore volume worldwide
- n Germany is the largest IT market in Europe with the services of about 30 billion €
- n Offshore providers rate the German market as the most attractive one regarding market growth
- n According to a Deloitte & Touche study 71% of the respondents are investigating or already in conducting offshoring
- n The German IT Outsourcing market has a volume of 10 billion €  
4% of this volume are offshoring services

## Application Management Services dominate still the current Offshore Services in Germany



Multiple answers possible. Base: 151 German companies

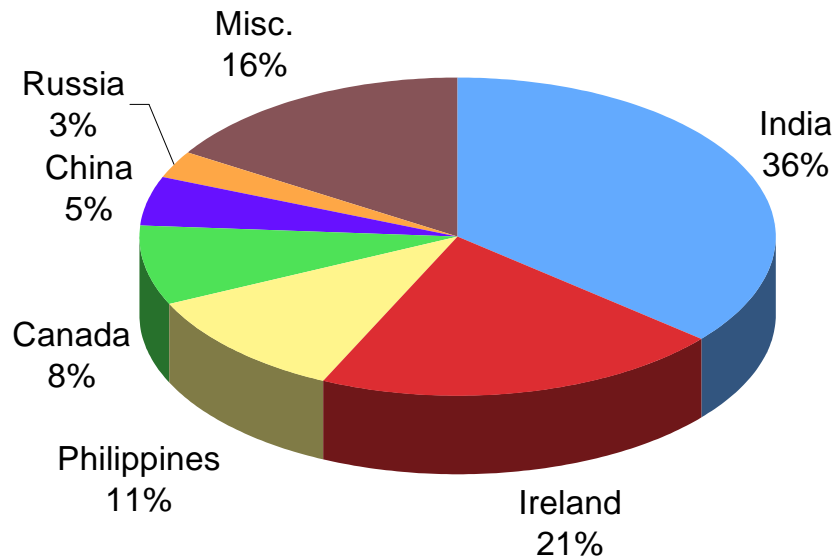
Source: Metagroup 2004

- n Application management and software development represent the highest export share of Indian Offshore service provider
- n In comparison to European prices, the Indian offshore services are based on daily rates between 140,- and 200,- €
- n Offshore providers focus on consulting and business process services to achieve higher value for their customers

# India is still the leading country with most relevant Offshoring experiences and providers



**Offshore market share**  
(International comparison)



Source: Metagroup 2004

- n Strong government support evolved the software industry at an early stage
- n The US Green Card program enormously affected the success of the providers
- n IT services have a share of 49% of the Indian GDP
- n India as the only country has worldwide operating, financially strong and listed service providers
- n An increasing demand leads to a shortage of resources in India with attempts to move delivery units to China
- n 45% of the German offshore volume can be assigned to Indian providers

## Major Indian Service Providers with global Presence

Name	Total Revenue (2003 in Billion US\$)	Employee (in 2003)
Tata Consultancy Services	1.560	ca. 24.000
Infosys	754	ca. 21.000
Wipro Technologies	617	ca. 13.000
Satyam	572	ca. 9.750
iGate Global Solutions	394	ca. 3.150
HCL Technologies	388	ca. 8.750
Convansys (US based)	382	ca. 4.860
Cognizant Technology Solutions (US based)	230	ca. 6.500
Patni Computer Systems	188 (2002)	ca. 5.600
MBT	165	ca. 3.600
Syntel (US based)	164	ca. 2.790

# China and the Central East European (CEE) countries offer potentials for Near- and Offshoring



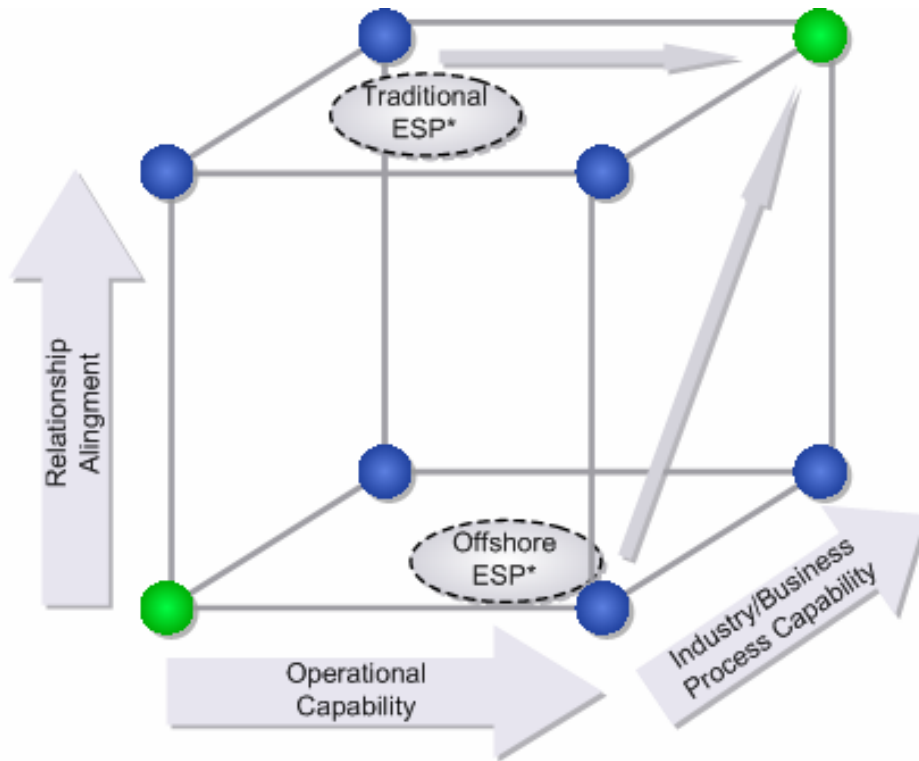
## China:

- n Lower labor costs compared to India by ca. -15%
- n High internal need of skilled IT resources for their own growing economy
- n Starting support by the government like building technology centres for software development will strengthen the future evolution
- n Foreign providers are allured by tax incentives and good infrastructure in a growing domestic market
- n Education and missing English skill are hampering the further growth
- n There is no global player with presence in Europe

## East European countries:

- n Nearshore providers from CEE countries are important to Europe
- n Language, culture and the geographical nearness support business process services
- n The service provider market is strongly fragmented with no global player
- n The entry to the EU and the stabilised legal system sustain the market growth of estimated 15% to 35%
- n Poland and Czech Republic are rated as the most attractive Nearshore countries

# Traditional ESPs and Offshore ESP develop Global Delivery Models from different starting situations



\*ESP: External Service Provider

- n Comparable range of services in the areas application management, BPO (e.g. service center, HR, finance) or infrastructure services
- n Strengths of the traditional providers can be found in the relationship management and the business / industry knowledge
- n Offshore providers have developed since years processes and skills for an onshore / offshore delivery model with strongest certifications on CMM Level 5, CMMI, ISO, SPICE, Six Sigma

# Current Strategies of the Offshore Providers to address the Restrictions in the German speaking Market



1

Nearshore providers from the CEE countries like Poland or Czech Republic will pursue the delivery of value added services benefiting from the cultural and geographical nearness to the German speaking market.

2

Experiences in project management and software development processes will be the base for extending the range of services by the Indian players. BPO of labor intensive work will offer high cost advantages.

3

Therefore traditional Offshore providers pursue the strategy to establish own subsidiaries in Western or CE Europe partly by acquisition or partnership with local companies (e.g. NIIT / AD-Solution).

4

Traditional Offshore build up locate value added services at delivery centers in Nearshore regions, especially for BPO services like HR or finance administration.

## Structure of Study

- n Introduction
- n Market Situation Near- and Offshoring in Europe
- n **Survey Results**
- n Evaluation and Guidelines
- n Discussions

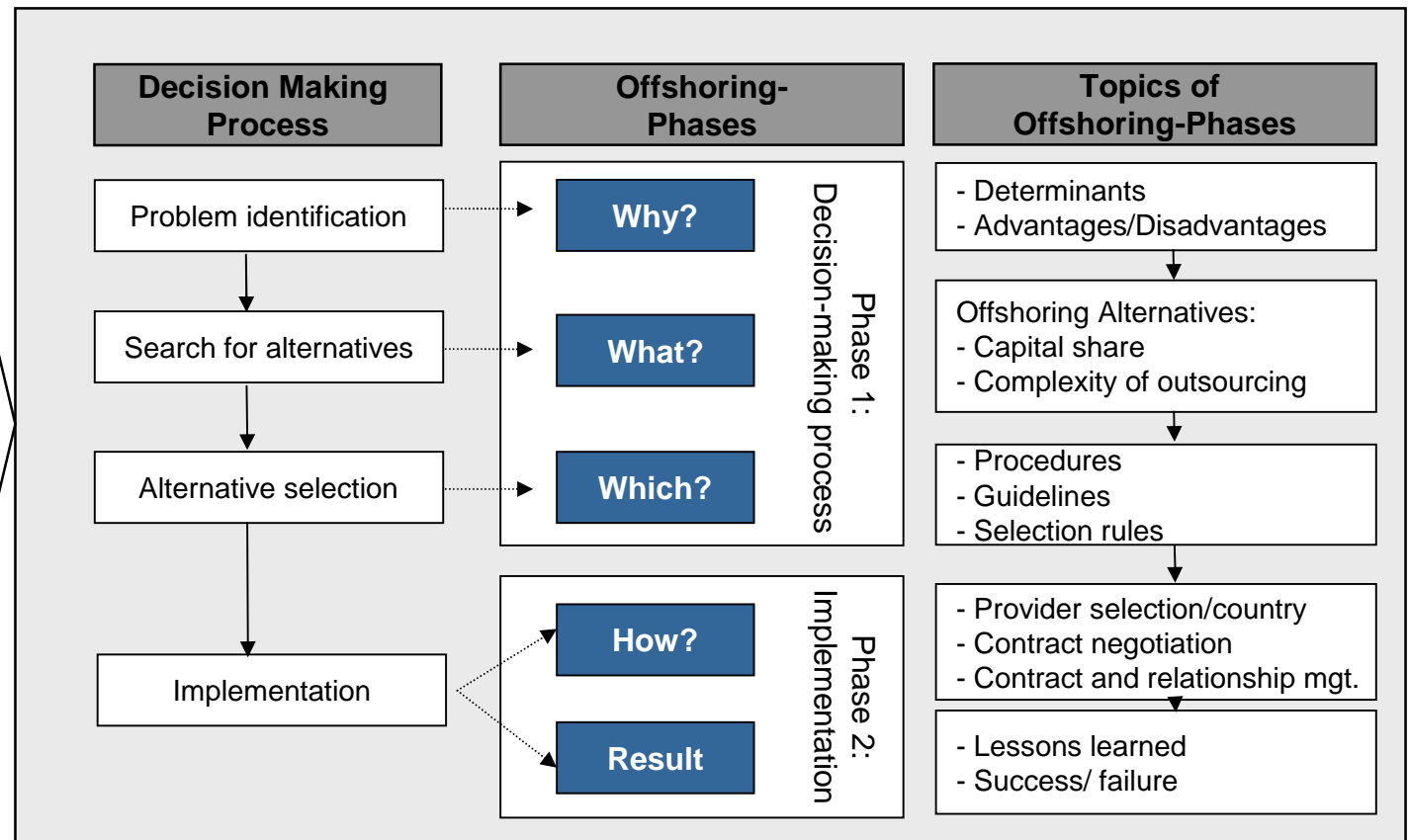
# Seven out of the fourteen interviewed Survey Participants are using Offshoring Services already



Industry	Outsourcing Volume (% of total IT budget)	Offshoring Volume (% of outsourcing volume)	Offshoring since	Service Area
Industry	10-20%	10%	2004	Application Support SAP
Telecommunication	70%	1%	2003	Application Development
Transportation	30-40%	10%	2003	Application Development and Maintenance
Airline	60%	1-2%	2002	Application Development
Travel	60%	10%	2005	BPO with large IT part
Transportation	90%	3-4%	1999/2001	Application Development and Maintenance
Insurance	50%	70%	2001	Application Development, Maintenance & Support

# Interview Guideline Structure

- 14 companies were interviewed
- Contact persons were CIOs, Heads of IT or dedicated Outsourcing Project Managers
- Goal of the Interviews was to get information concerning the **Outsourcing Decision Making Process**



## Interview Results: Motivation for Offshoring

Cost Reduction	Increased Flexibility	Availability of Resources	Internal Reorganization
<ul style="list-style-type: none"> <li>§ A major motivation for Offshoring is cost reduction regarding the contracted function/area</li> <li>§ Cost reduction is a requirement to stay competitive in an international environment</li> <li>§ For some, cost reduction is the only driver for Offshoring</li> </ul>	<ul style="list-style-type: none"> <li>§ Offshoring is seen as a means to increase the flexibility of a project regarding time, costs and quality</li> <li>§ In general, Offshoring provides access to a large pool of highly qualified and critical resources</li> </ul>	<ul style="list-style-type: none"> <li>§ Through Offshoring, companies face an increasing availability of critical and well-qualified resources</li> <li>§ This also implies getting access to specialized processes and leading-edge technologies</li> </ul>	<ul style="list-style-type: none"> <li>§ The cooperation with an Offshoring service provider can foster internal reorganization</li> <li>§ Service levels agreements and process requirements will push the own organization to higher professionalism</li> </ul>



**Motivation for Offshoring**

# Success Factors for Offshoring



## Lessons Learned for Implementing Offshoring

### Country and Provider

- § India is the most designated Offshore country in the survey
- § The provider selection is mostly based on a well-structured selection process
- § Important selection criteria are: experience, industry know-how, skills, certification and strategic scope

### Contract

- § Contract negotiation takes overall two to six months until closure
- § Application Offshoring contracts are agreed for three to five years
- § Support by experienced and well-qualified internal or external resources is important for Offshoring success

### Governance

- § SLAs and KPIs management is crucial
- § Established communication procedures (e.g. Steering Board meetings, Onsite-/Offshore coordinators)
- § Established survey for feedback

## Structure of Study

- n Introduction
- n Market Situation Near- and Offshoring in Europe
- n Survey Results
- n **Evaluation and Guidelines**
- n Discussions

## The Study shows three major Findings

### Offshoring Findings

n The discussions of the pros and cons has been concluded. Today, Offshoring should be an inherent part of the **corporate sourcing strategy** with different delivery models

n The success of offshore projects depends on **service characteristics** and **maturity** of the own organisation

n **Best practice** in offshoring shows how to establish successful partnerships and how to reduce risks

# Today, Offshoring should be an inherent part of the corporate sourcing strategy with different delivery models



1

Offshoring with established service provider has a **proven stability** with advantages in strong cost saving, short time to market, high quality and flexible access to critical resources and know-how.

2

Due to high costs for communication and for adjustment of the organisation offshoring should be implemented as a **long term partnership** instead of a single initiative.

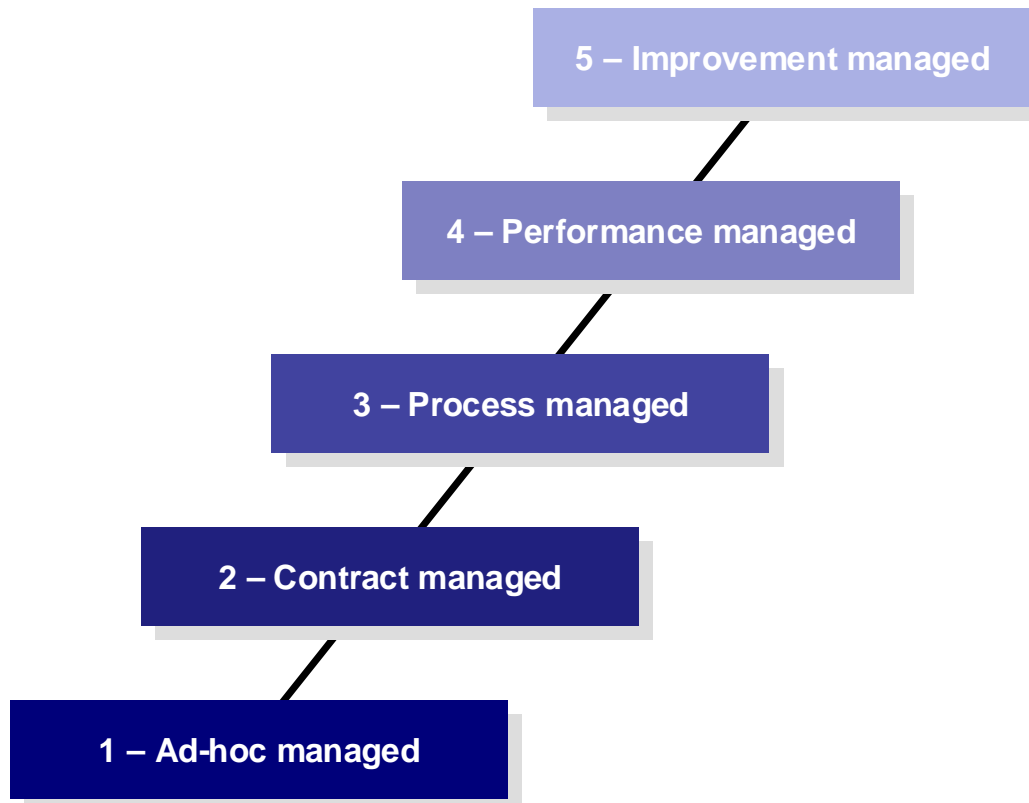
3

**India** is the **dominating country** for companies, looking for direct Offshoring with responsibility relocation and long term stability. International companies are currently evaluating to relocate Shared Service Centers to Offshore countries as an alternative.

4

For **individual and business critical** services as well as for companies with less international or outsourcing experience, Nearshoring at CEE countries is a good alternative.

# The Success of Offshoring depends on Service Characteristics and the Maturity of the own Organisation



## Service characteristics

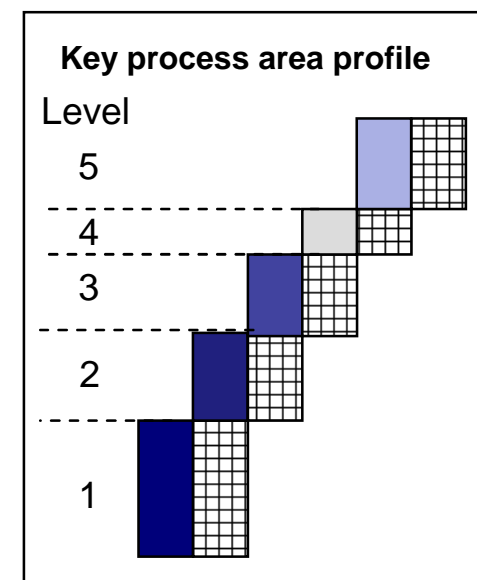
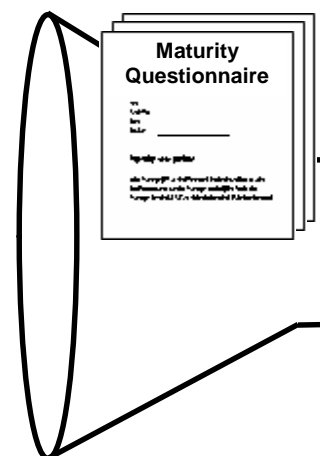
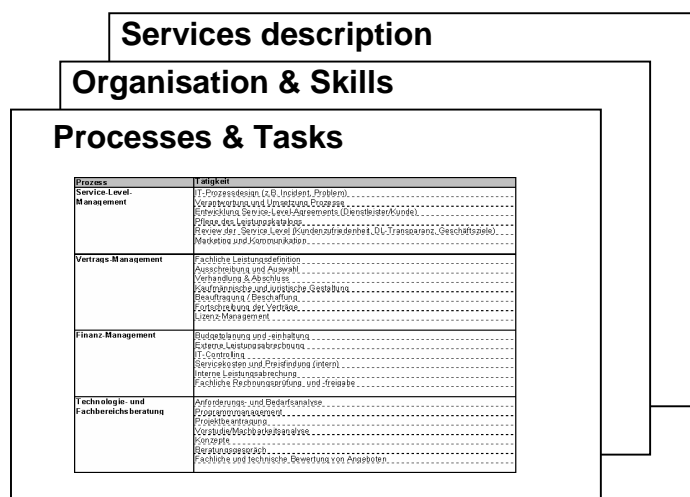
- § Standard skills and processes
- § Service volume (more than 1500 project days per year)
- § Stability and descriptiveness of services requirements

## Level of maturity

- § The sourcing capability maturity model is a descriptive model for analyzing the organizations fitness for outsourcing
- § For successful offshoring level 3 and above is required on both sides

# Navisco Sourcing Capability Evaluation Methodology

## Assessment



### Analysis:

- scope of services
- process maturity level
- governance capabilities

### Findings:

- strength and weakness of organisation
- sourcing risks analysis

### Profile:

- achievement of objectives
- lacks in key process areas and key practices

# Best Practice in Offshoring shows how to establish successful Partnerships and how to reduce Risks



## Risk Management

- 1. Partner and Country Selection
- 2. Involvement of own Organization
- 3. Independent Expertise
- 4. Think Big, Start Small
- 5. Contract Negotiation



## Partnership Management

- 1. Cost Management
- 2. Calibration of Organizations
- 3. Relationship Management
- 4. Management Culture



[www.process-alliance.org](http://www.process-alliance.org)

## **CONTACT:**

**Dr. Michael Heym**

[michael.heyman@navisco.com](mailto:michael.heyman@navisco.com)

**Prof. Dr. Armin Heinzl**

[heinzl@uni-mannheim.de](mailto:heinzl@uni-mannheim.de)

**Navisco AG**  
**Hamburg, D-20249**

**Heilwigstrasse 33**

**Tel. +49.40.2531.3280**

**Fax. +49.40.2531.3288**