



TenStep Supplemental Paper

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Is your Organization Looking at Offshore IT Development?

Offshore development has been an option for some time. You have all heard of the trend toward globalization. Technology is making the world smaller and smaller. With the Internet and basic technology infrastructure, it is hard to tell if you are dealing with companies down the street or on the other side of the world.

More and more people work outside of the physical office. If you decide that your workers no longer need to physically be in the office, does it really matter any more if they are 20 miles away or 2,000 miles away?

Outsourcing is another industry trend. Companies are deciding to outsource much of their IT capability because they don't think that it is one of their core competencies. Again, once you make the decision to outsource, does it really matter if the outsourced staff works in another state or another continent?

Well, in some ways it does matter. There is no question that there are complexities involved with sending work offshore that do not exist if the work remains in-house, or even in the country. However, there are definitely some business benefits as well. The question each company needs to answer is whether the business benefits outweigh the costs and the risks. The risks posed by offshore development are not as great now as they were even a few years ago. Therefore, it is an option, at least, that more and more companies are considering.

Let's look at the benefits of offshore work

When people think of offshore development, they typically think of India. India is the most dominant player in the market today, since they had a head start, and at least from the perspective of the United States, they have the added advantage of speaking English. However, there are many players in this market, from Canada to Eastern Europe and Russia. In fact, the Indians are worried about their market as well, with a growing competitiveness and even lower costs in China.

There are many benefits of offshore work. Some are obvious and some are more subtle, but still important.

Cost is usually the place to start

Let's start with costs savings since that is the one advantage that everyone hears about. The comparison is more complicated than just looking at the relative salaries of the offshore worker. First, no offshore company is going to charge you only the raw labor costs. Offshore development companies are in business too. They still have to pay for managers, benefits, taxes, facilities, equipment, sales people, etc. So, just as with a US outsourcer, your costs of using an offshore firm are going to take into account the full costs of doing business, as well as a profit margin.

Of course, your company has many of these costs as well. If you don't have the developers working for your company, you do not have to buy computers for them, pay



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benefits for them, have desks for them, etc. So, the fully burdened cost of your labor is also more than just the base salary.

However, there are at least some incremental costs. Your company needs people who are responsible for managing the offshore relationship. This is an incremental cost that you do not have today. You may outsource the work, but you still need people to manage the relationship, perform quality assurance, and make sure the work is progressing as expected. This is true with all outsourced relationships.

However, after taking all of that into account, the cost of offshore labor is cheap enough that the overall proposition for most companies is that they can save money by sending work offshore. It is not a 90% reduction, or a 75% reduction, but a 25% or more cost reduction might be reasonable. Of course, cost savings are not the entire answer.

Faster cycle-time may be a benefit

Some say the biggest advantage of hiring IT people from overseas the biggest advantage is faster turnaround time. Some organizations divide the work so that one developer works on one piece during the day, while another developer works on the same piece or a different piece at night. Their main value point is that you can get your critical projects delivered in half the time.

There is no question that faster turnaround time is a business benefit. It can be a huge benefit to companies that need to get products to market quickly. From a practical standpoint, many offshore companies also need this capability, since they must have people available during our working hours – even if it is nighttime in their country.

Is the work quality acceptable?

If the cost is lower and the cycle-time is faster, then the quality must be poorer, right? Not necessarily. This is an area that offshore companies have really been focusing on. Since they are building this outsourcing business model, the offshore companies have really been focusing on using quality processes and techniques. Many of them, or even most, have been rated highly on the Capability Maturity Model scale.

ROI

If offshore development has advantages from a cost, quality and cycle time perspective, then you can put together business arguments in terms of Return on Investment (ROI). In essence, all of your projects have a higher ROI if you can receive the same benefits (or similar) for less cost and perhaps even more quickly than the home grown option.

Loss of control is one limiting factor

With the benefits described previously, why doesn't everyone make the move to offshore development? Companies still need to rationalize the value proposition for their own circumstances. The first area to consider is what it means to your company to give up control. There is no question you give up some level of control when you outsource work. You have to manage an offshore relationship, not the actual work itself. Some companies decide that they do not like the risks associated with losing control of their



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development processes or their critical application support, and so they do not pursue the offshore options. Other companies come to different decisions.

Do you want IT development to be one of your core competencies?

A company also needs to determine what they want their core competencies to be. The reason many companies outsource is that they decide that they really don't want to do that kind of work. For instance, many large companies are outsourcing their telecommunication work. These large companies have decided that they don't want to be good at managing networks and replacing phone lines. Instead, they outsource that type of work to companies that are supposedly experts.

Development work is the same way. Many companies send development work to offshore companies because they decide they no longer want to have that core competency. Instead, they will hand it to an IT development company that does that kind of work for a living. The company will then manage the relationship to ensure that they receive the deliverables and the value they need. They no longer manage the actual work.

Most companies aren't there

On the other hand, many companies, perhaps most, are not yet to a point where they feel comfortable giving up the control, and most companies still want to have a strong development organization. These companies feel that having an in-house development capability will give them a competitive advantage in the long run and will help them better execute their strategy in the short run. This is more important to them than "saving a few bucks."

Outsourcing your work can also require more rigor, discipline and organizational skills. If you outsource new development, your business clients must be much better at communicating requirements, and they have a heavier burden to make sure that they get their scheduled work done on time. This can be a good thing, but it is one that requires more focus. The business clients can get away with a lot of things given the flexibility of an in-house development staff. Much of that flexibility can go away when you are working in a contractual partnership.

Summary

So there you have it in a nutshell. There are definite advantages to having an offshore partnership. For some companies, it is even a no-brainer. However, the value proposition does not work for all companies. There are risks involved with losing direct control. Some companies feel they can manage the risks. Others prefer not to. So, although the globalization trend will continue, and the offshore development trend will continue, there may never be a point where the majority of domestic IT is being handled offshore. However, it is at least an option that more and more companies will at least consider over time.