CIO

Offshore drift

India remains the jewel in the outsourcing crown but CIOs are beginning to look to other destinations in a bid to ensure competitive pricing and service

BY DARREN HORRIGAN

It is no surprise to learn from the gurus at Gartner that India, as undisputed champ, and China, as greatest challenger, remain the leaders for offshore IT and business process outsourcing services.

Still no surprise that many other countries such as Malaysia, Poland, and Chile are investing heavily to become credible alternatives. But it says much about how global IT outsourcing has changed that Gartner claims the destinations now just outside the IT offshoring club are Pakistan and North Korea. In his latest book, Obama's Wars, legendary investigative journalist Bob Woodward describes Pakistan as the most dangerous country in the world. And North Korea?

In its report 10 Leading Locations for Offshore Services in Asia Pacific and Japan for 2010, Gartner analysed countries as offshore services locations using criteria such as language, infrastructure, education, cost, cultural compatibility, legal maturity, and security. All the countries on the Asia-Pacific list, including Australia and New Zealand, make Gartner's global top 30 offshore locations for 2010.

India continues to grow its IT services exports, but its share of the worldwide total has declined, and wage pressures, geopolitical troubles and financial scandals are creating opportunities for other countries.

Meanwhile, currency fluctuations against the US dollar have made some countries less compelling. As the Australian dollar hovers close to parity with the greenback, for example, Australian demand for offshore services should increase. But it will also make Australia less attractive as an outsourcing destination.

Management consultants AT Kearney rank the most attractive offshoring destinations for many business activities — IT services and support, contact centres, and back-office functions — in an ongoing research project called the Global Services Location Index, or GSLI (**see page 66**).

The firm's latest GSLI reveals a dramatic shift in the geography of outsourcing destinations, due to diminishing cost advantages in some countries, and improved skills in others.

The Middle East and North Africa is emerging as a major offshoring region because of its large, well-educated population and its proximity to Europe. Countries in Latin America and the Caribbean continue to capitalise on their closeness to the United States as nearshore destinations. There are also onshoring trends to lower cost cities within the US, UK, France and Germany — big western democracies facing political pressure to keep jobs at home.

Thanks to emerging technologies such as cloud computing, service providers are offering more outcome-based pricing. While clients believe pricing for infrastructure services is competitive in the early years of an agreement, adjustments over the life of a contract struggle to keep pace with the market. More CIOs are looking to ensure competitive pricing for the life of their agreements.

CIOs are also seeking more vertical expertise from outsourcers. Service providers, traditionally hired to improve efficiency and reduce costs, are being asked to also identify and solve inefficiencies in clients' internal environments. Clients are leaving the bulk of their original scope with incumbent outsourcers, but they are carving out some portions and awarding them to other providers in a multi-sourcing, best-of-breed approach.

Great expectations

In Australia, CIOs are also trying to get more from their existing outsourcing arrangements. Clients and incumbent vendors are renegotiating deals before they expire; both recognising they can save money by avoiding the competitive chore of going to market and rebuilding a better deal.

Success, however, is elusive.

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Clients may want to cut a new deal, but few vendors have the flexibility to move from their current service delivery models. Vendors are influenced by the day-to-day pragmatism of their business-as-usual team, rather than the creativity of their sales people.

John Liburti is the founding director of Cherub Consulting Group, whose recent clients include BHP Billiton, National Foods, Mitsubishi Motors, Westpac, Woodside, and the University of Melbourne. Liburti's specialty is strategic sourcing. He says the big challenge is client expectation; Often, clients want the new deal to deliver the future today. But a renegotiation is about changing an old deal, not building a new one.

"Either way, the move is a change in the dance step, rather than a change in the dance beat," says Liburti. "Where vendors fail is that they understand change is required, but they can't demonstrate the journey to the client. How do we get there? What are we going to do that is different? The result is that clients see the renegotiation is doomed so they go to market."

Organisations are also starting to re-invest in their own people rather than rely on vendors. They are rebuilding internal teams by hiring a new breed of IT expert; not people expert in doing the work — that's the reason they outsourced in the first place — but people who are experts in identifying internal business needs, extracting information from advisors, filtering feedback, and converting it into intelligence that helps the CIO build a strategic IT roadmap for the business.

"You don't want your people 'doing'; you want them 'managing'," says Liburti. "That means vendor management, which is one area most organisations neglect. They think a contract is all they need. Most outsourcing deals that go wrong reveal there is as much blame with clients as with vendors."

Organisations are recognising vendor management as a way to evolve the contract, as opposed to just keeping it humming. They are building their ability to manage vendors and improve their understanding of their own business.

Smaller and shorter deals are back in vogue, Liburti says, since they are easier to manage and more flexible. Most clients are looking to reduce the value and duration of their contracts to achieve faster implementations, and more responsive exit and change strategies.

"There is no point having long deals that you are locked into if you are trying to change the way you do things," says Liburti.

Clients are also seeing the value of building an in-house project management capability, not only to manage internal resources, but to manage vendor projects to their organisation, in order to maximise the visibility of costs, the quality and the vendor activity.

Standardised processes, training, consistent reporting, portfolio management, and project prioritisation are all becoming the norm in organisations that historically relied on vendors to provide these tools, skills and disciplines.

Top 30 countries for offshore IT services: Gartner

Europe, the Middle East and Africa

Czech Republic, Egypt, Hungary, Ireland, Israel, Morocco, Poland, Romania, Russia, Slovakia, South Africa, Spain and Ukraine

The Americas

Argentina, Brazil, Canada, Chile, Costa Rica, Mexico and Uruguay

Asia Pacific

Australia, China, India, Indonesia, Malaysia, New Zealand, the Philippines, Singapore, Thailand and Vietnam

Global versus local

Australian CIOs are interested in what is happening overseas, but unless they operate within an organisation that plays on the global stage — such as banking or resources — the options available from vendors for services, skills and innovation are fewer than in Europe or the US.

"Asia is our backyard, but you hear of so many offshore deals hitting the wall," says Liburti. "While CIOs in Australia are not gun shy, they are very selective about which trend they follow. They pick the eyes out of the better ideas; the ones that have a proven bottom-line benefit to the business.

"Take cloud computing. Most researchers tell you it's the next big thing. While I agree it has promise, those same organisations place caveats on their predictions by saying there is still a lot of work needed to prove the concept. Some CIOs are testing the water, but they are doing a lot of homework, surrounding themselves with colleagues and advisors, and creating excellent change management processes."

Infosys managing partner, **Robert Liong**.

Joanne Stubbs, the CIO at Bakers Delight, does not believe there is such a thing as a global outsourcing trend.

"I've been in IS for more than 25 years and it just depends on where you are in the world at any given time, global financial crises, stock market plunges, Aussie dollar rates, or how mature your business is as to whether you outsource or not," she says. "Like anything in IT, it goes in circles every seven years."

One of the first moves Stubbs made at Bakers Delight, after stints as CIO at The Good Guys and General Motors Acceptance Corporation, was to outsource all the bakery franchise's printing to Australian-based provider, Upstream. But while many of her CIO colleagues around the world seem happy to use low-cost centres outside their shores, Stubbs would never outsource overseas.

"I inherited an outsourcing contract at Bakers Delight, for a call desk, that did not stipulate that the provider needed to seek our agreement if they wanted to outsource their call centre elsewhere," Stubbs says.

"It meant that if we had an issue and we rang their call centre in Australia we could be put through to India or Malaysia. I won't even enter into discussions with outsourcers that have their call centres offshore. I don't want my customers having to deal with that experience."

Maintaining relationships

Tony Joyner has seen it all when it comes to negotiating outsourcing contracts. Joyner is a partner at law firm Freehills, where, as a senior member of its national projects team, he advises some of Australia's biggest companies. His mantra: Negotiate fairly, be vigilant and keep everybody happy. If only it was that easy.

"I did a huge outsourcing deal once, and on this rare occasion we were acting for the outsourcing company," says Joyner.

"The customer was a very, very big Australian company. And they were exceptionally unpleasant. They were rude. They were arrogant. Our client needed this deal to survive. The customer knew it, and just crunched them. At one stage I asked: 'Why are you being so rude to these people, when next week, they are going to be in your office in control of a critical service you need?'"

The people who were acting so awfully were a mix of the customer's lawyers and finance people. From their perspective, they won the negotiation. They got the best contract possible for the least amount of money. But the net result of different people with different goals taking care only of their patch, mean such wins are always hollow.

Joyner says negotiation does not have to be a fight. The biggest issue in any outsourcing contract is to aim for that old chestnut — a win-win.

"There is no point screwing the people who will be your outsourcing partner," he says. "Two reasons: If they're not going to make enough money out of the deal, they'll put their

B-team on it and provide you with a sub-standard service. And on a personal level, they'll hate you."

Joyner takes the view that in any complicated outsourcing deal you will not get all the detail right 100 per cent first time. There is always the chance to calibrate aspects of an agreement later.

"If you've done a deal that means the outsourcing company is losing money, or life is horrible for them, there is no point insisting on it because over the long term you will lose," he says.

Joyner also advises clients to keep a close eye on the relationship. Whatever area of the business the outsourcing agreement covers, pay attention. The closer the outsourced service is to your core business, the more alert you need to be in checking user satisfaction and service delivery. The best way is to keep sufficient expertise in your organisation to monitor agreements intelligently. Don't leave your organisation exposed.

The final task is to keep everybody happy.

[Don't get too interested in who is selling, because you won't see them again]

"You need to make it easy for the outsourcer to want to do the right thing by you," Joyner says. "Remember, you have handed them control over some parts of your business. If they want to do the right thing by your company on a personal level, then a whole lot of little irritations will disappear. And a whole lot of good things just happen. You don't want your outsourcer taking advantage of you, but you need them to be happy. Happy outsourcer, happy service. That's on an organisational level and on a personal level."

For Stubbs at Bakers Delight, as in any good relationship, it's the little things that count.

"You have to go in with exactly the same objectives," she says. "Rarely does this happen. The main rules are: Don't have contracts that last too long, or if they do last for more than five years, make sure the contract is flexible enough to allow both parties, as they learn, to change the terms and conditions to reflect the new business environment or the mistakes made in the first contract. Because rest assured, you will both make mistakes."

Notes from the trenches

CIO spoke to many sharp people for this article; people who have been there, done that. Their collective and unmistakable message is that business is essentially about people. The irony is that this is the first thing people forget.

"All organisations say people are their most important asset, but when it comes to the crunch they get too involved in

Outsourcing dos and don'ts

Defining relationships

- Treat outsourcing vendor contractors as you would your own employees in terms of respect and mistake management
- Develop local leaders who understand the corporate culture
- Obtain approval rights for vendor leadership personnel
- Locate contractors at your captive overseas locations
- Establish dedicated relationship managers on your team

Negotiating new terms

- Clearly define service expectations
- Expect contracts to need adjustment over time
- Keep it simple; avoid complex formulae for severity levels and escalation rules
- Frame renegotiation in terms that emphasise the benefit to the vendor

Key performance indicators

- Explain to business leaders that outsourcing requires more management oversight and planning than in-sourced service
- ✗ Don't set key performance indicators (KPIs) for performance that can't be measured
- Establish KPIs before creating service level agreements
- Include regional managers as early as possible in establishing performance requirements
- Develop a performance measurement process that does not force users to distinguish between outsourced and internally-provided service

Service level agreements

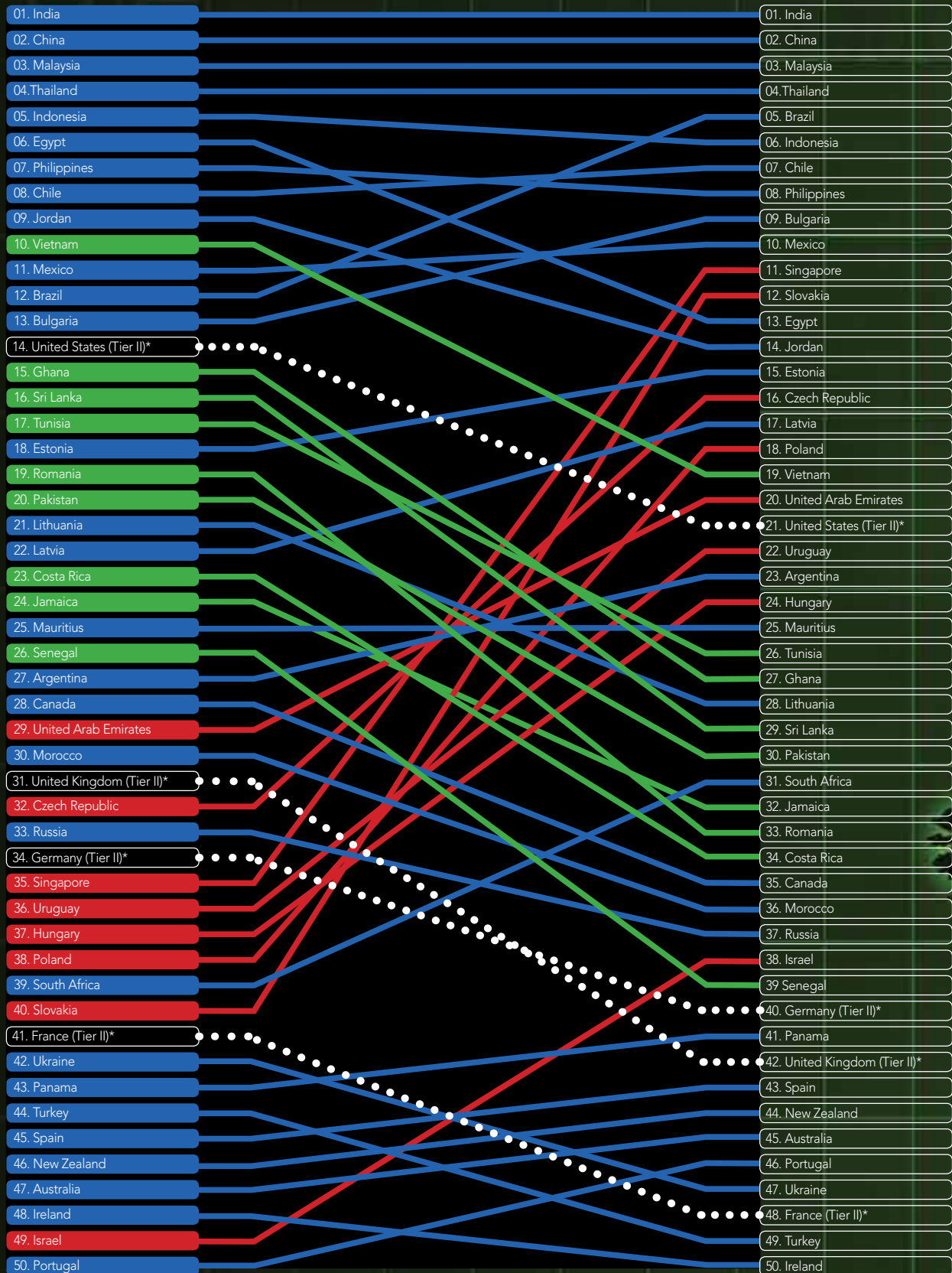- Keep service level agreements (SLAs) to a minimum — if you didn't track it before, you may not need to track it now
- ✗ Don't create SLAs for every little thing
- Establish SLAs as a minimum expectation, not the optimal goal
- ✗ Don't make SLAs technical and disconnected from the end result
- Expect to adjust SLAs as contracts change
- Try adjusting SLAs rather than renegotiating whole contracts

Source: CIO Executive Council

New outsourcing hubs

Ranking in 2009

01. India
02. China
03. Malaysia
04. Thailand
05. Indonesia
06. Egypt
07. Philippines
08. Chile
09. Jordan
10. Vietnam
11. Mexico
12. Brazil
13. Bulgaria
14. United States (Tier II)*
15. Ghana
16. Sri Lanka
17. Tunisia
18. Estonia
19. Romania
20. Pakistan
21. Lithuania
22. Latvia
23. Costa Rica
24. Jamaica
25. Mauritius
26. Senegal
27. Argentina
28. Canada
29. United Arab Emirates
30. Morocco
31. United Kingdom (Tier II)*
32. Czech Republic
33. Russia
34. Germany (Tier II)*
35. Singapore
36. Uruguay
37. Hungary
38. Poland
39. South Africa
40. Slovakia
41. France (Tier II)*
42. Ukraine
43. Panama
44. Turkey
45. Spain
46. New Zealand
47. Australia
48. Ireland
49. Israel
50. Portugal

Ranking in 2007

01. India
02. China
03. Malaysia
04. Thailand
05. Brazil
06. Indonesia
07. Chile
08. Philippines
09. Bulgaria
10. Mexico
11. Singapore
12. Slovakia
13. Egypt
14. Jordan
15. Estonia
16. Czech Republic
17. Latvia
18. Poland
19. Vietnam
20. United Arab Emirates
21. United States (Tier II)*
22. Uruguay
23. Argentina
24. Hungary
25. Mauritius
26. Tunisia
27. Ghana
28. Lithuania
29. Sri Lanka
30. Pakistan
31. South Africa
32. Jamaica
33. Romania
34. Costa Rica
35. Canada
36. Morocco
37. Russia
38. Israel
39. Senegal
40. Germany (Tier II)*
41. Panama
42. United Kingdom (Tier II)*
43. Spain
44. New Zealand
45. Australia
46. Portugal
47. Ukraine
48. France (Tier II)*
49. Turkey
50. Ireland

the technology and the numbers," says Joyner. "Outsourcers provide a service, just like any other business. But no matter what the agreement involves, you must have people you can trust. There is an inclination to think about outsourcing as just software and servers. It's not. It is about people, no matter how much technology is involved."

CIOs know that many outsourcing firms have a team that sells the service, and a different team that delivers the service.

"We often find frustrations when these charming, go-getting, intelligent, perceptive people do the deal with our client, never to be seen again," says Joyner. "You must find out who exactly will be doing your work. Don't get too interested in who is selling, because you won't see them again."

Joyner says it is now common for outsourcing contracts to include provisions that give clients some control over the senior people assigned to them. Some contracts even retain the right for clients to be involved in bonus discussions with people in the outsourcing team.

Planning is another issue. Everybody says planning is important, but in the rush and tumble of doing the deal and making a start, organisations often go into an outsourcing arrangement underdone.

"You really need to know exactly what you want," says Joyner. "If you don't know what you want, you will end up buying what the outsourcer wants to sell. A critical issue is that many organisations don't know what they don't know."

AT Kearney Global Services Location Index 2009 (ranking in 2007 GSLI)

The GSLI analyses and ranks the top 50 countries worldwide to determine the best destinations for providing outsourcing activities, including IT services and support, contact centres, and back-office functions.

Each country's rank is composed of a weighted combination of relative scores on 43 measurements, which are grouped into three categories: Financial attractiveness, people skills and availability, and business environment.

No significant movement

Significant movement up the index

Significant movement down the index

•••••• *** Based on lower-cost locations in each country: San Antonio (US), Belfast (UK), Leipzig (Germany) and Marseilles (France)**

The reality is that outsourcing companies do outsourcing all the time. So CIOs need somebody on their team who knows outsourcing. Joyner suggests a genuine, smart, outsourcing consultant.

"Clients often tell us that they have an IT team, so they don't need a consultant," says Joyner. "You may have a great in-house IT team, but this is not what they do for a living. The people you will come up against do this every day. You need somebody with the same experience, expertise, intellect, ability, and cynicism as the outsourcer. If you don't, they'll kill you."

Joyner hastens to add that most outsourcing organisations are "perfectly nice people who try to do the right thing". But he warns that the natural inclination for any service provider is to do as much as they can and to sell you as much as they've got. They're in business too.

"You must take control," Joyner says. "Make sure you trust the individuals you are dealing with; work out what you want internally before you get too involved with vendors; and have hard-core expertise on your side."

Robert Liong, managing partner for consulting and systems integration at Infosys, says win-win thinking wasn't part of the first generation of outsourcing — both sides were too focused on getting as much as possible for themselves.

"I was working on an early outsourcing engagement," says Liong. "The vendor had no problem coming up with a solution that met our technical specs. But meeting our expectations to deliver a great customer experience was much harder. The vendor was not keen to admit they didn't really know what we were talking about, and we probably weren't as good at articulating our requirements as we should have been.

"In that first generation of outsourcing — say, 2000-2005 — we saw a lot of missed opportunities. Clients were naive about the capabilities of the outsourcing partners and keen to outsource ill-defined challenges they themselves were struggling to deliver internally. And in a bid to build their businesses, some outsourcing companies were overly aggressive in their promises. There were some bad marriages.

"In the second generation, we began seeing some serious pre-nuptial agreements — which at least offered better escape clauses if the marriagwe wasn't working.

"In the third generation, I am starting to see a greater maturity and transparency between clients and outsourcing companies. Outsourcers will expect that technology and business stakeholders on the client side are on the same page — and step up to help broker that shared vision even with competing vendors. Clients will expect outsourcers to be more transparent about their capabilities and business models — so that the final solution works financially and plays to the strengths of both parties.

"Both sides are now asking more questions up front. This takes longer, but it is much less messy and less expensive than divorce." **CIO**

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