EASTERN PROMISE IS A WESTERN LURE

More than half of FTSE-100 companies contract some of their information technology and business processes to outside organisations.

A study by Cap Gemini Ernst & Young suggests that one in five of these companies has a single outsourcing contract worth at least 3% of its market capitalisation.

Offshoring

What is relatively new is the phenomenon known as offshoring. This entails the exporting a whole range of jobs – back-office positions in banks and other financial institutions, call-centre jobs and IT support positions – to low-wage economies, as in countries such as India or the Philippines.

At a recent seminar on offshoring, hosted by the London office of the international law firm Latham & Watkins, Christopher Gentle, director of Deloitte Research, told attendees that the cost base of the world's top 100 financial service institutions was $2.34 trillion. Of this, $356bn would move offshore within five years, leading to a migration of two million jobs.

The concept is gathering momentum and those companies that take up offshoring earlier are going to see the biggest benefits.

Risky business

But offshoring is not without risks. Many straightforward outsourcing projects fail. Add such factors as language and culture barriers, in addition to distance and different time zones, and the chances of achieving success seem slimmer.

What's This India Business? by Paul Davies is the first book of its kind that examines "the phenomenon that is the offshoring and outsourcing of services jobs". It not only describes the practice and how it fits into globalisation generally, but also uses the author's extensive experience of India to explain exactly how businesses should go about seizing this opportunity to gain an advantage over their rivals.

Davies says the practice is becoming so widespread that just taking part in offshoring is not enough; the advantage only comes from doing it well.

India is not the only country supplying service workers for western companies. But Davies is adamant that it is the pre-eminent location. "Because of India's significant advantages in language, education, culture and entrepreneurship, choosing a country [other than India] for offshore work has to be a deliberate, fully conscious decision," he writes.

Davies has, throughout his time in the country, gradually worked out seven criteria to be used in choosing an outsourcer.

1. Management capability
Davies says this is more than just identifying a good manager. What is required is a company with an effective management structure, culture and personnel. This is rarer than you might think as Indian business schools do not tend to address cultural and motivational issues.

Davies advises UK businesses to note how Indian directors treat the staff serving them tea and coffee. This, he says, gives a good indication of how the middle managers will treat the staff working on your account.

2. Alignment with western business practice
Many outsourcing companies will pepper their speech with words like 'key performance indicators', 'lean development' and 'unique selling points', but real alignment with business practice is more important than jargon, says Davies. Companies must try to understand how outsourcers conduct their internal budget rounds.

3. Competitive threats
A good relationship between client and outsourcer is one way to avoid outsourcers moving into the client's own market. If an outsourcer takes on more and more of a company's process, then at some point the outsourcer may be able to take away the company's business and customers as well. This is not common, but worth considering.

4. Size
Large outsourcers are popular because they provide a more stable financial track record. But he says these companies may become a competitive threat to their clients over time. Davies suggests that as soon as a UK business reaches a sticking point in early negotiation with an outsourcer, that is the best time to assess whether the outsourcer is big enough to do business with. The outsourcing market will eventually consolidate, so small outsourcers should be avoided.

5. Understanding each other
Davies says there needs to be a firm understanding of both the client and outsourcer's strategic aims. As outsourcing is developing, fast companies should only do business with those that can articulate clearly their medium- to long-term strategy.

6. Shared objectives
In special cases, Davies says companies may wish to take stock in the outsourcing companies. In India, a 26% shareholding is enough for an effective veto. Joint-venture arrangements with outsourcers have been established by some larger companies.

7. Intention
Indian business culture means that outsourcers are reluctant to say no to any request. But this causes many problems when outsourcers agree to tasks they cannot undertake. Davies advises western companies to challenge outsourcers to communicate constantly any problems and issues that arise. If they say there are no problems, you are doing business with the wrong company.

Benefits

Davies explains that moving services offshore is not solely about making cost reductions. "It is about making the most appropriate cost reductions and, at the same time, achieving enormous business gains in other ways. The scale of the revolution, the speed with which it is happening and its sustainability would be in doubt if immediate cost reductions were the only, or even the eventual, major benefits."

Among the benefits is changing what the company does, so that rather than just exporting inefficient practices, the processes are themselves adapted. Another benefit is gaining better educated and motivated staff, and obtaining better value from buildings and infrastructure as a result of using the time difference between India and the West to utilise them more effectively.

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A wide range of Briefings can be found at www.financialdirector.co.uk/briefing

Useful links

- ***What's This India Business?* is available from Nicholas Brearley International for £20. *www.nbrearley-books.com***