



















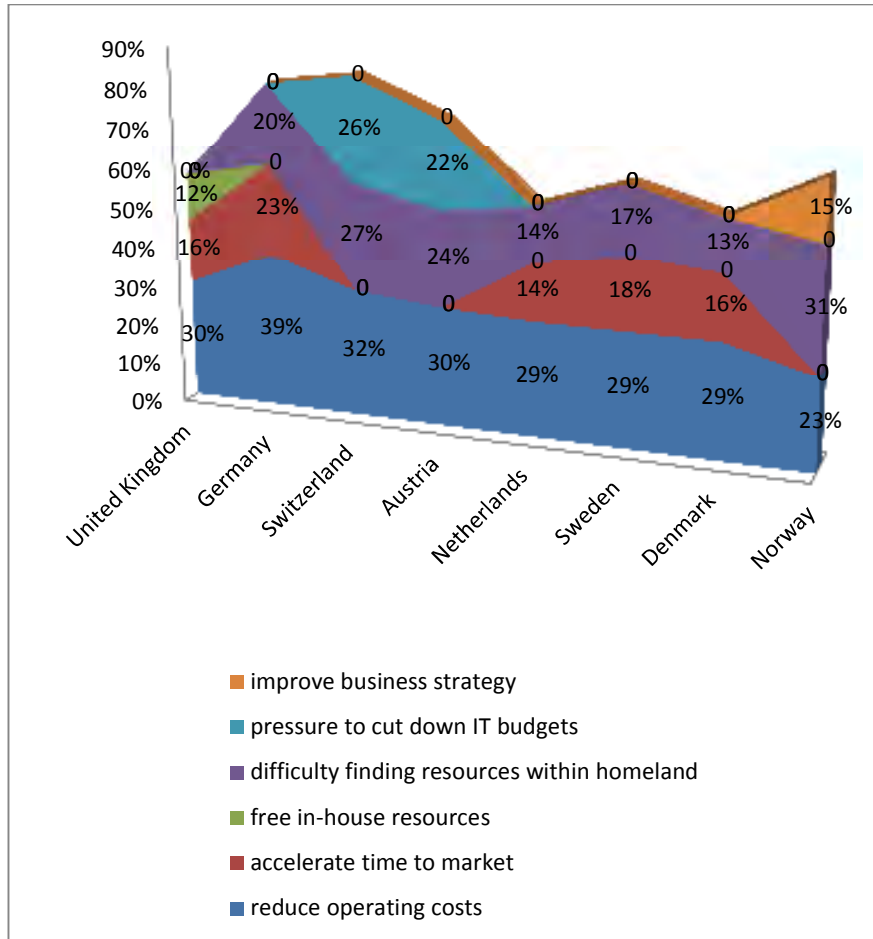








**Figure 8: Key pressures that impact corporate decisions to outsource software/web development**



**Figure 9: Most popular actions companies take prior to engaging in ITO partnerships**

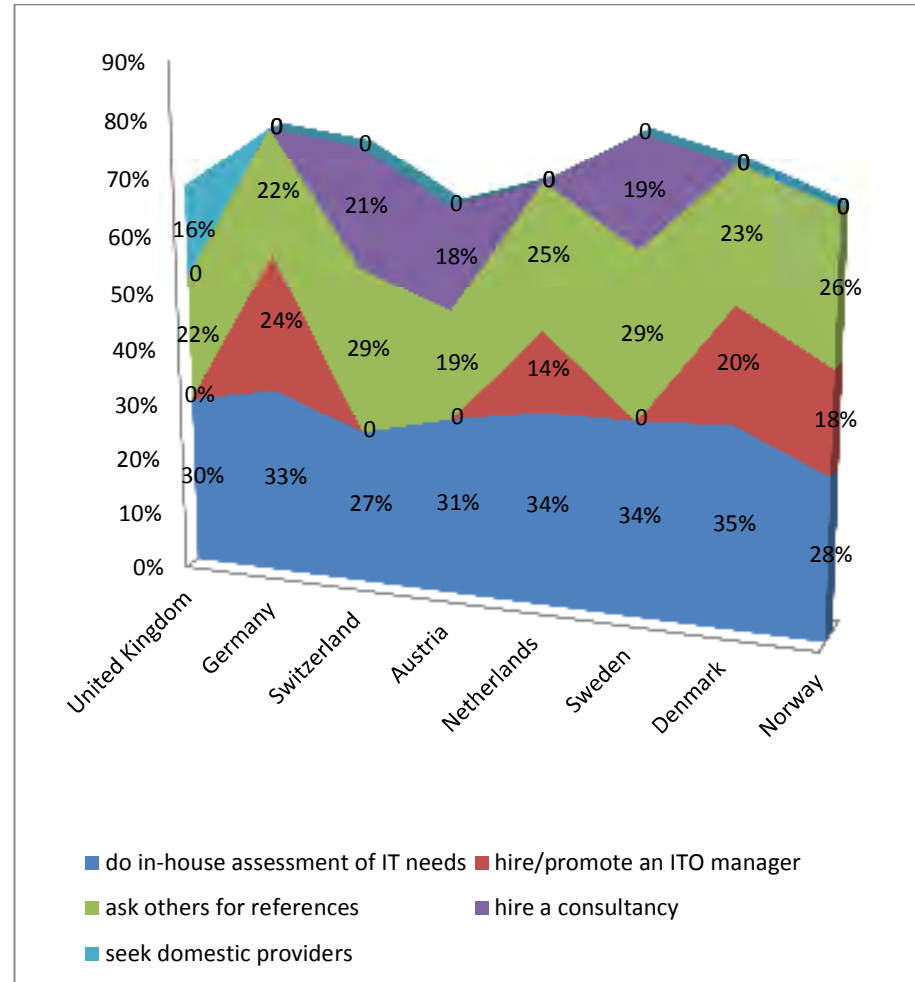


Figure 10: Volume of the outsourced software development

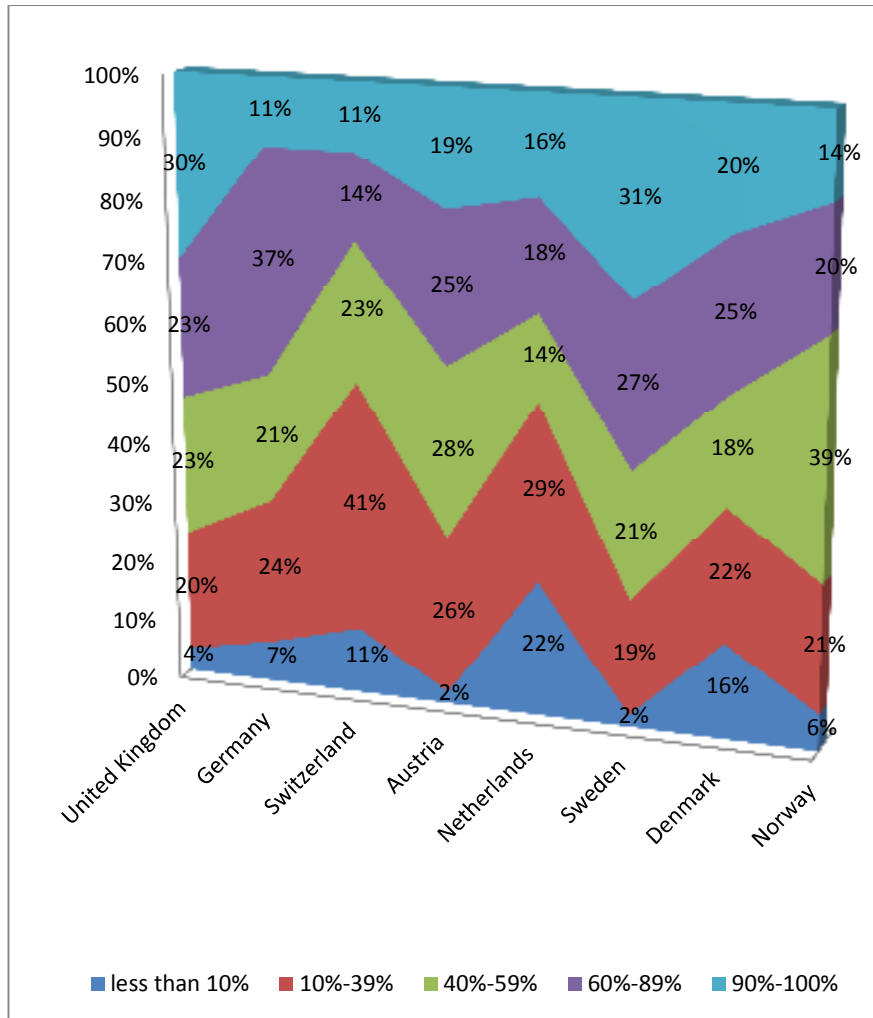


Figure 11: Most outsourced areas of expertise

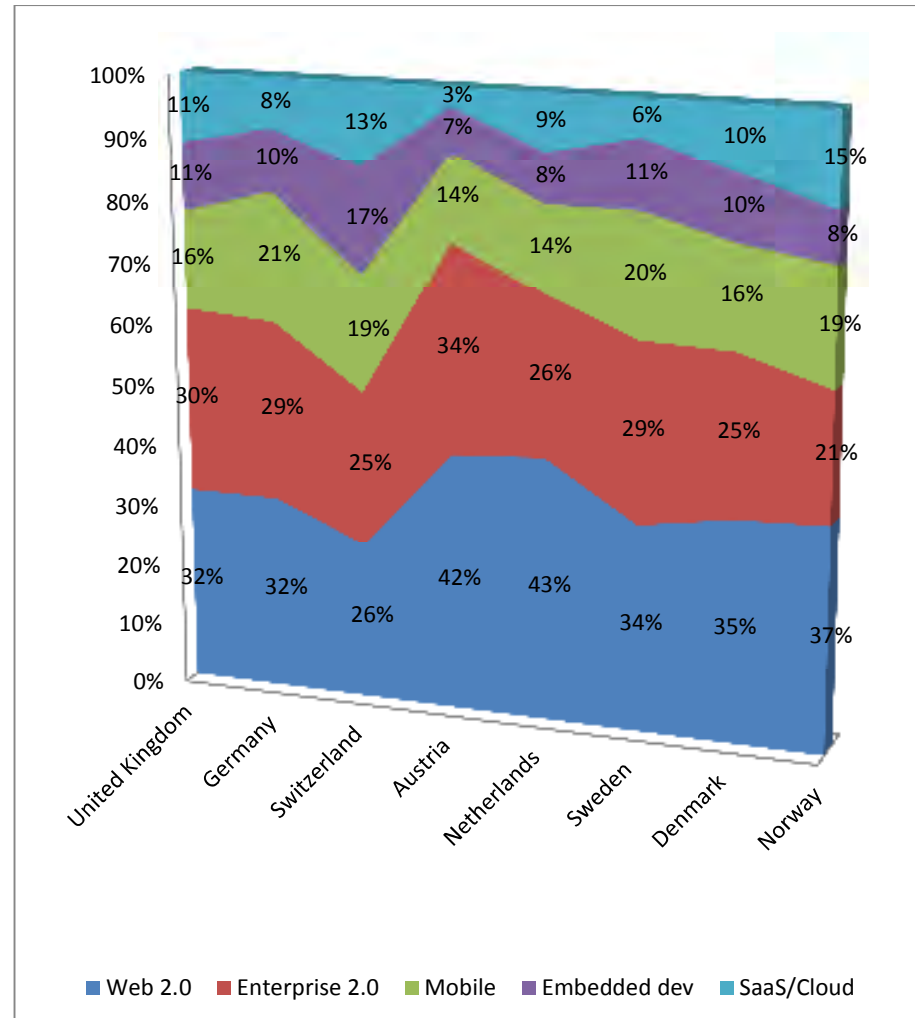


Figure 12: Key drivers of the choice of the outsourcing destination

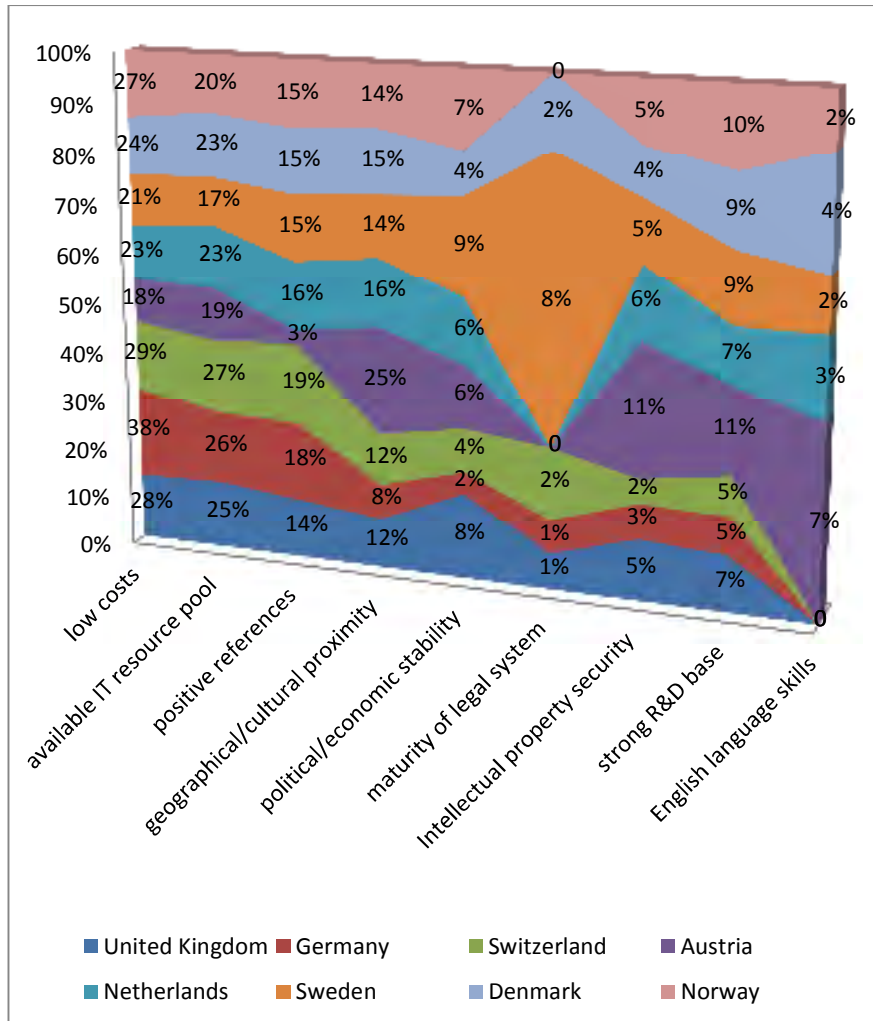
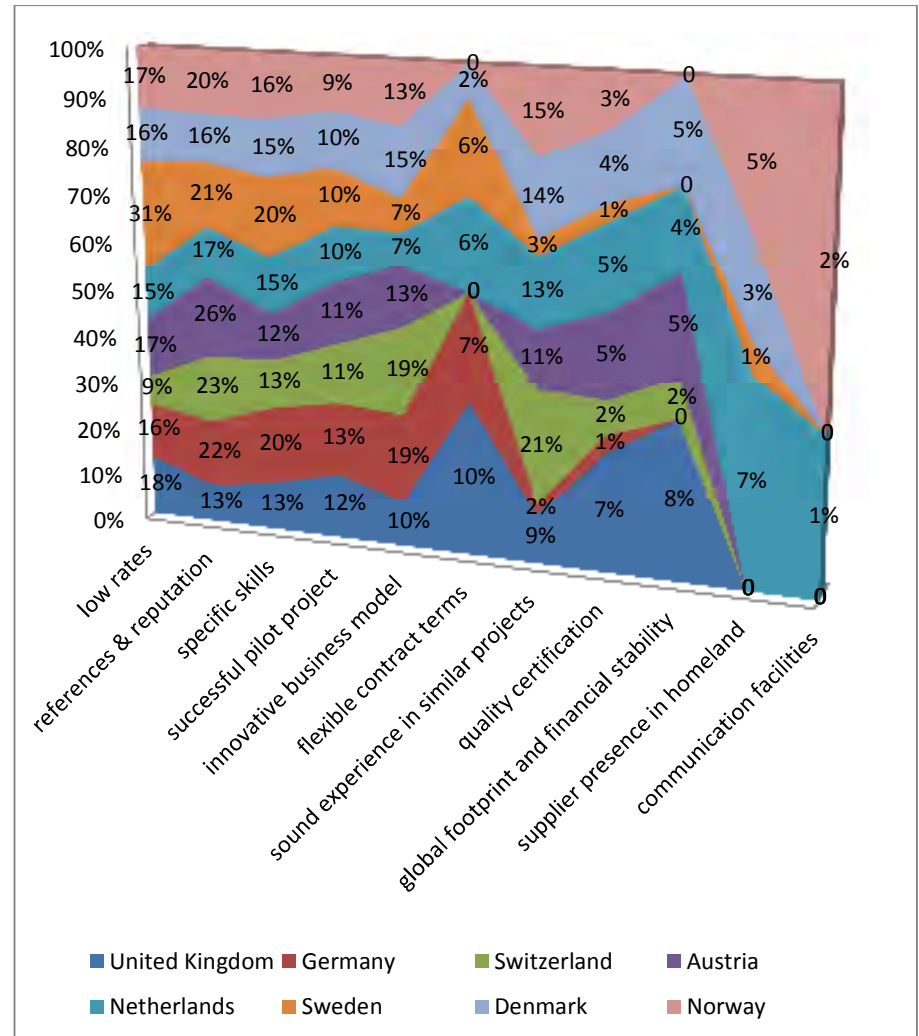
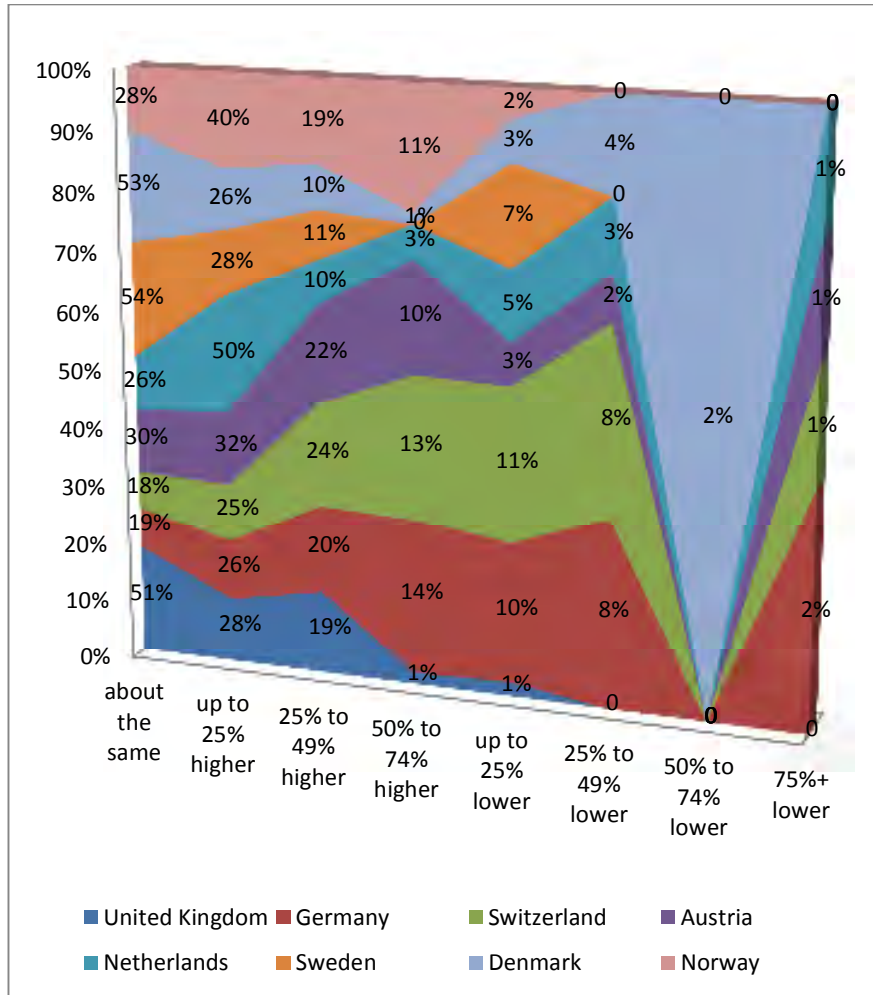


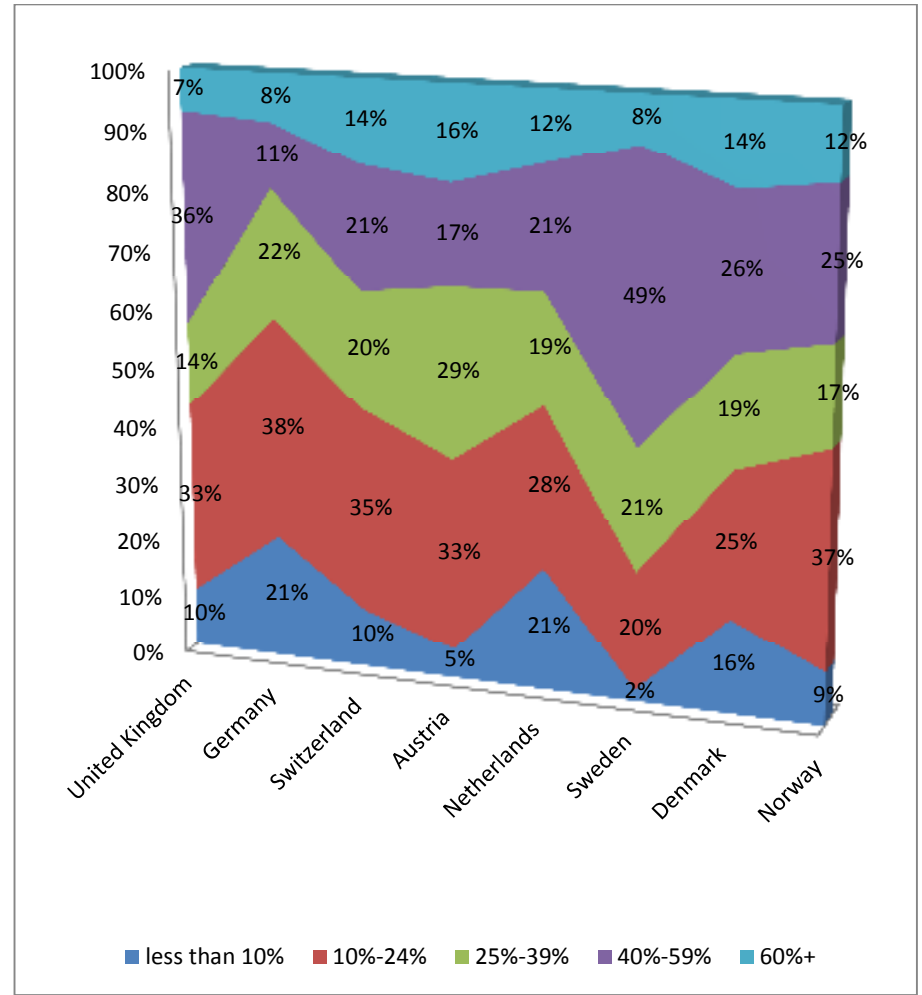
Figure 13: Key drivers of the choice of the outsourcing partner



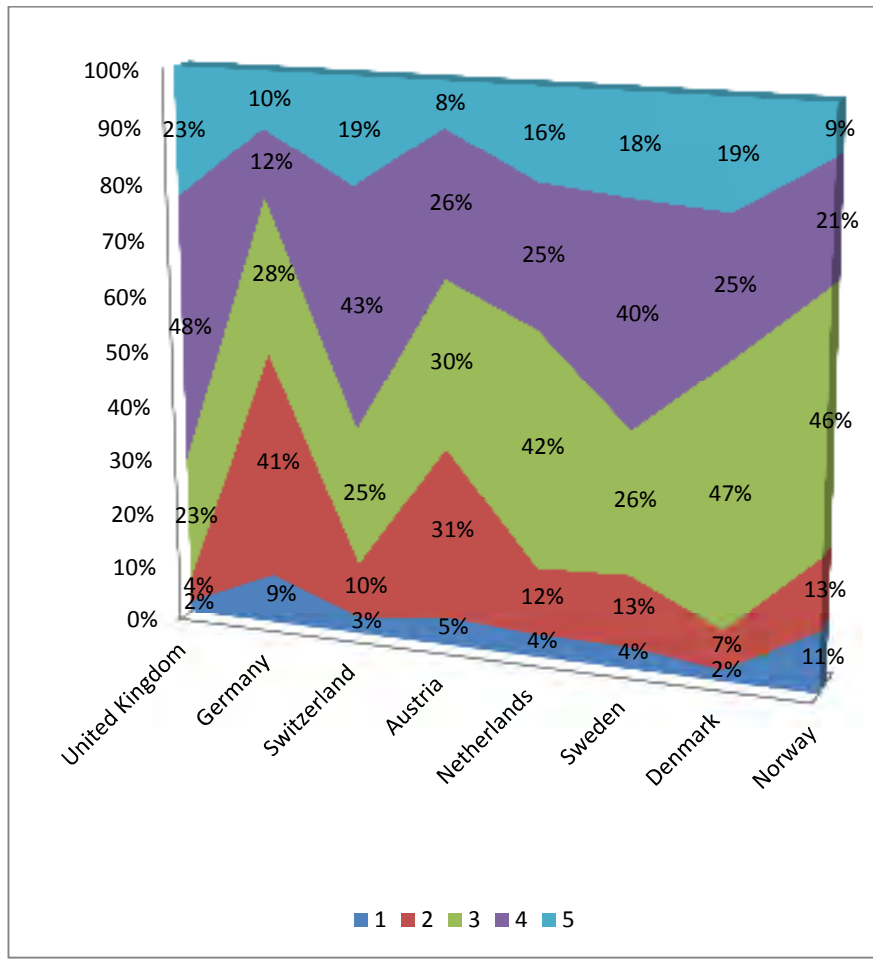
**Figure 14: How actual incurred annual costs of the outsourced development compare to the expected (contracted) ones**



**Figure 15: Actual savings from the outsourced software development**



**Figure 16: Companies' assessment of their ITO providers on a 5-point scale, where 1 is least satisfied and 5 is most satisfied with the received services, project execution quality, attitude, prices etc**



**Figure 17: Do Western European & Nordic clients know exact salary of each of the team members on the outsourced development team?**

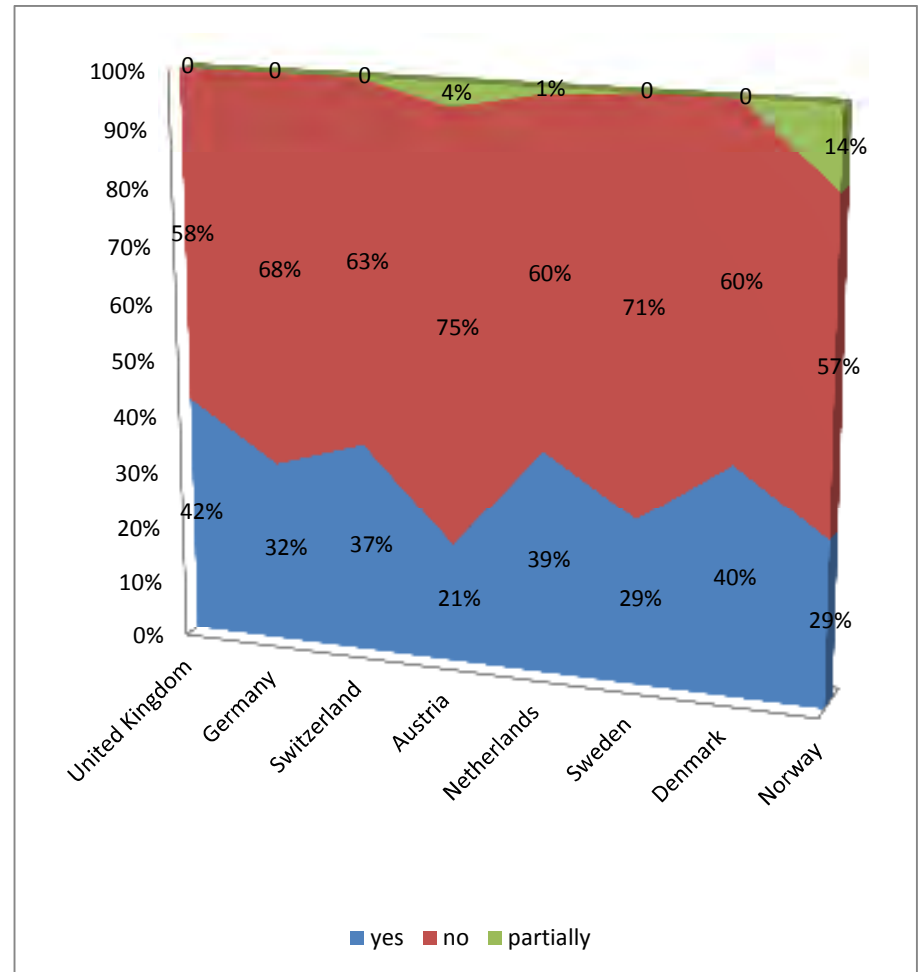
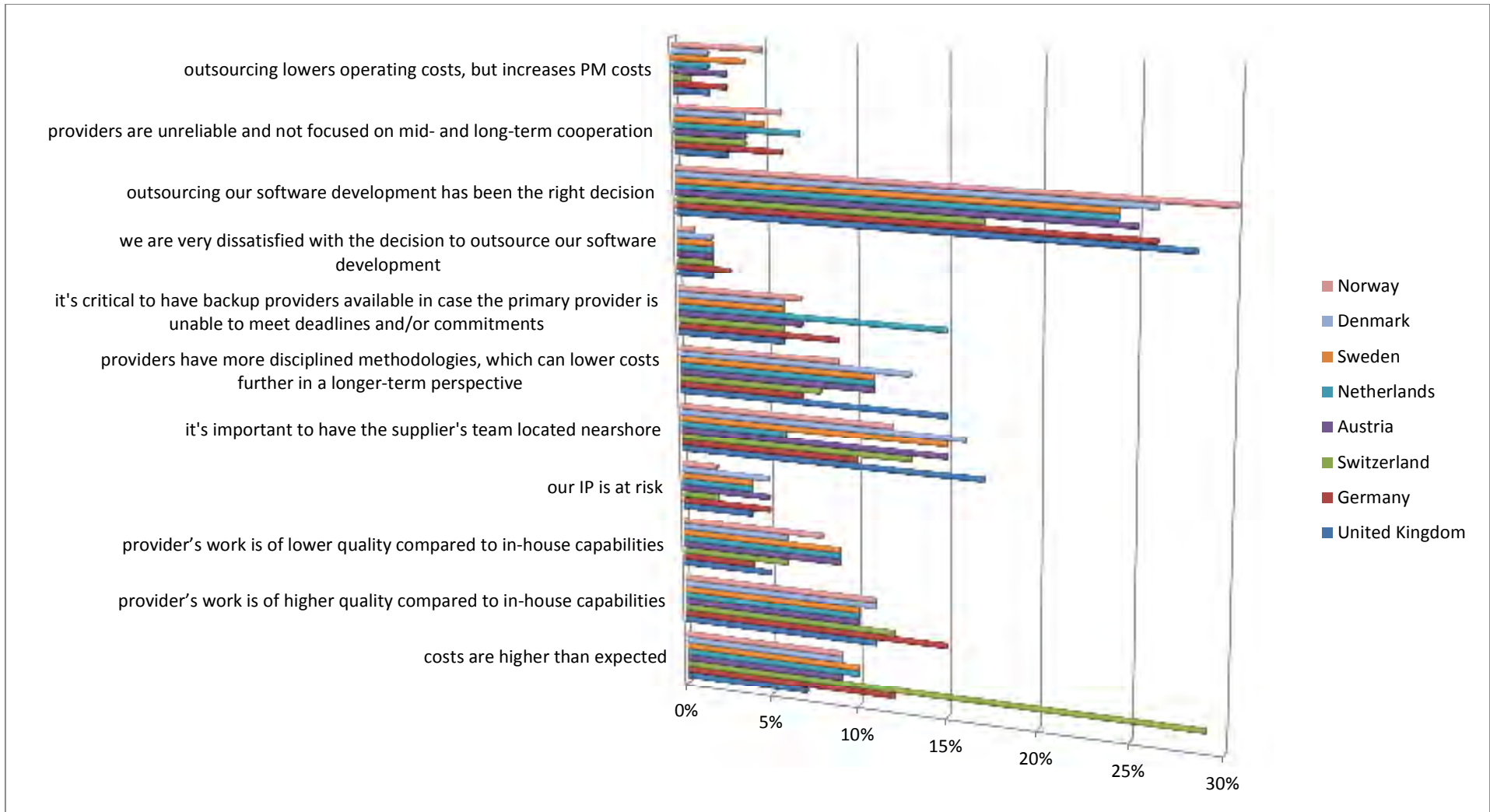


Figure 18: Companies' overall impressions of SD outsourcing





## Analysis of Challenges & Solutions

Figure 20: Challenges of the outsourced software development

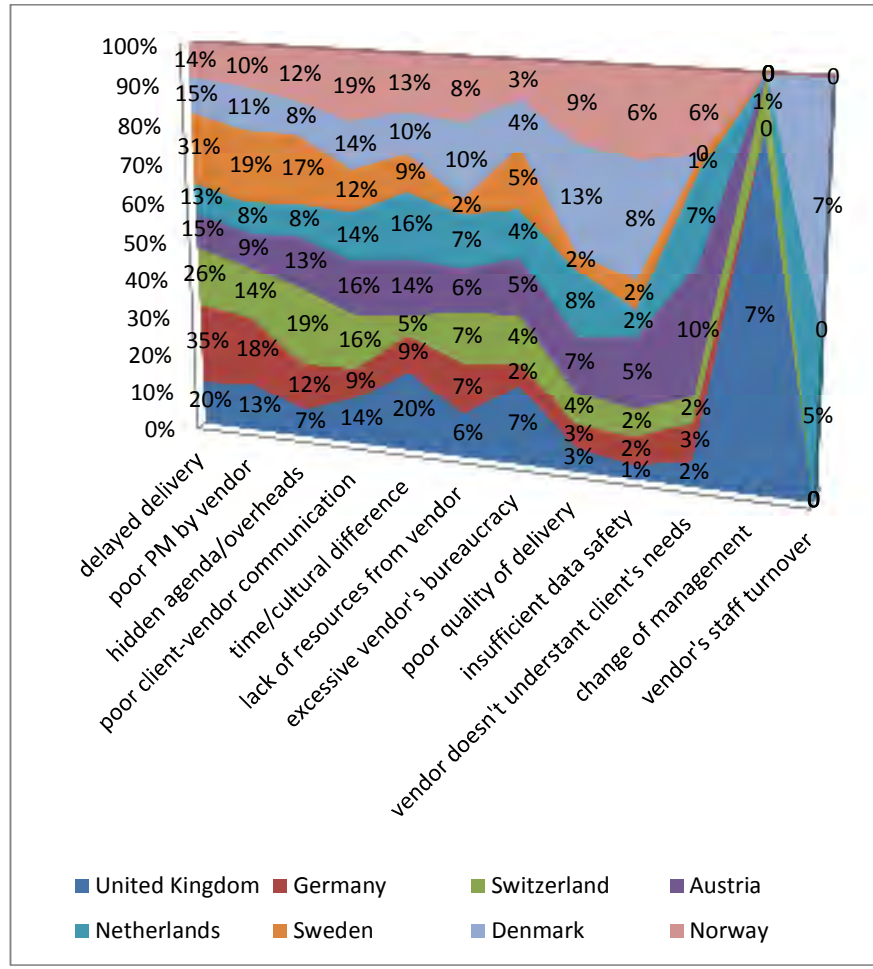
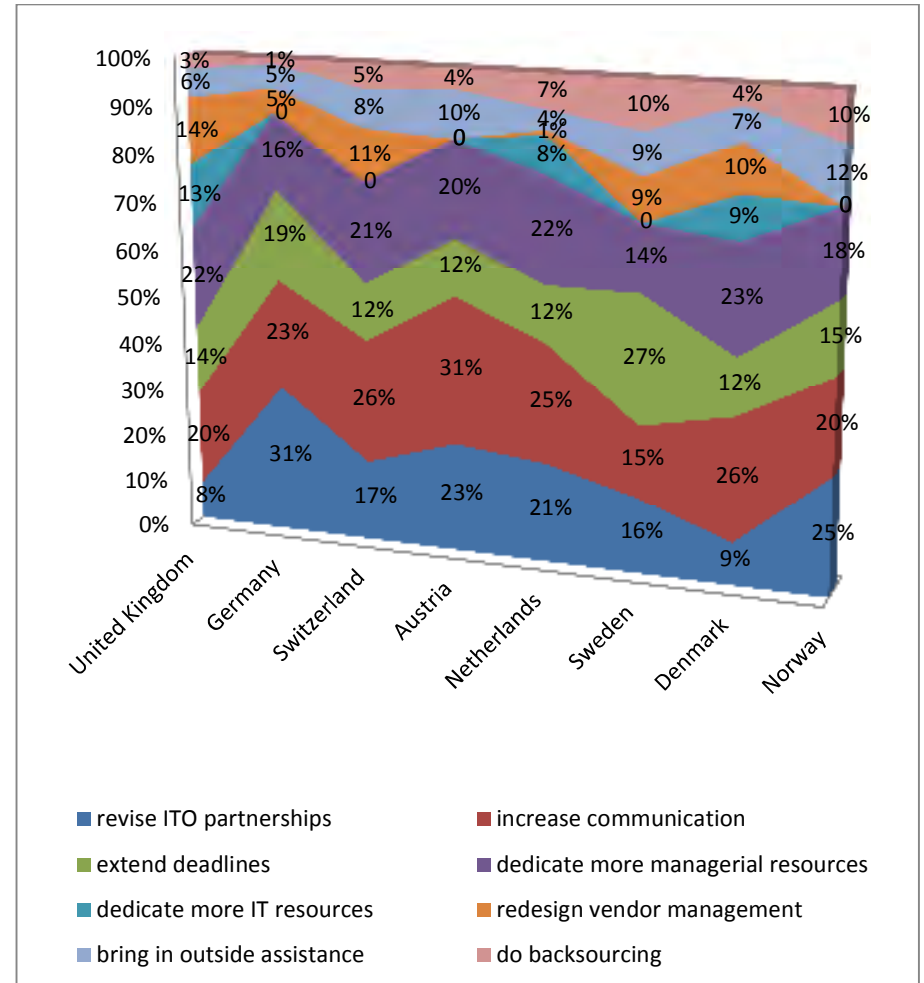


Figure 21: Actions companies take to respond to challenges of the outsourced development



## Part II: Findings' Discussion

The European IT Outsourcing Survey 2010 allows us to observe certain trends and challenges among the Western European and Nordic companies that outsource their software/web development function to a 3d party offshore, nearshore and/or within own countries.

The study results show obvious similarities and differences in the ways how outsourcing companies from different countries behave in terms of software development outsourcing management, maintenance and improvement, how they respond to their most critical challenges and what best practices they use to squeeze as much value from the outsourcing transactions as possible. These results help better understand the level of ITO maturity and grasp of innovation of every European country surveyed and predict to the future trends and challenges that will most likely influence the further evolution of the ITO practices in Western Europe and Scandinavia.

IT Sourcing Europe believes that the study sample generally shapes the actual state of affairs at both country-specific and All-European ITO markets in 2010, which makes the given research findings demonstrative of the actual trends and challenges facing software development outsourcing companies in every country surveyed.

To begin with, it is important to know the ratio of small, mid-sized and large companies that act at each surveyed country's ITO market. As seen from [Fig. 1](#), in 2010 small companies appear to be the most active users of the outsourced software development in the following countries: Germany, Switzerland, Austria, Netherlands, Sweden, Denmark and Norway. United Kingdom is the only country surveyed in which mid-sized companies remain the most active adopters of SD outsourcing. This finding allows assuming that the overall outsourcers' profile in Europe began to change in the post-crisis years, bringing more small companies (start-ups, early-stage, venture capital backed etc) to the foreground. It suggests

that in the upcoming years the stereotype that outsourcing is for large and mature companies only will be absolutely busted and more small companies will be sourcing IT resources and talents outside their own countries in order to grow at a faster pace and with long-term benefits.

Regarding the annual revenue expectations among the outsourcing companies in 2010, most of Swiss and Norwegian companies anticipate to earn less than € 1 million, most of German, Dutch and Swedish outsourcers expect to earn € 1 to 49 million in annual revenue, while most of Austrian companies plan to gain € 50 to 99 million in annual revenue. Additionally, a rather high percentage of Norwegian software development outsourcers (10%) claims they expect to earn more than € 500 million in annual revenue in 2010 ([Fig. 2](#)). As seen from [Fig. 3](#), outsourcing helps most of German, Swiss, Austrian, Dutch, Swedish, Danish and Norwegian companies increase their annual revenue by 1% to 9% and most of the UK companies – by 10% to 19% in 2010.

These findings generally demonstrate that United Kingdom has the most mature SD outsourcing market compared to other Western European and Nordic countries surveyed in the course of this research. The UK companies, especially the mid-sized ones, traditionally adopt the outsourced SD in order to leverage operating costs and increase annual revenue via faster time to market and sustainability while cutting down corporate IT budgets. In terms of maturity and readiness to adopt SD outsourcing, the UK companies are followed by the German outsourcers.

Regarding the overall SD outsourcing experience, the leading countries, most of which companies have been outsourcing their SD function for more than 3 years now, are again United Kingdom and Germany, followed by Netherlands, Sweden and Denmark. Austria has the smallest number of companies outsourcing for more than 3 years and the greatest number of companies who first outsourced their development only less than 12 months ago. It suggests that Austria has the "youngest" SD outsourcing market among the all countries surveyed (See [Fig. 4](#)).

Quite interesting findings were made with regards to the most popular destinations for the outsourced SD in 2010. As seen from **Fig. 5**, most of the German, Swiss, Austrian, Dutch, Swedish, Danish and Norwegian companies place their SD nearshore, while only the United Kingdom has the greatest percentage of companies that outsource their SD offshore. It proves the thesis that the UK companies still prefer offshore outsourcing because of their historic close links with India and Pakistan. From this viewpoint, the UK appears to be the most conservative country whose business development is driven by tradition rather than common sense and strive for more effective client-vendor communication and grasp of innovation which are easier to achieve in geographically closer environments (this statement will be proven further in the Report).

The following findings relate to the major factors driving corporate decisions to outsource entire or part of SD function to execution by the 3d party in 2010. As seen from **Fig. 8**, reduction of operating costs remains the most powerful driver of outsourcing decisions in all 8 countries surveyed. Among the other most frequently cited factors are: acceleration of time to market (UK, Germany, Netherlands, Sweden and Denmark), difficulty finding required IT resources and specific skills within own country (all surveyed countries except the UK), pressure from investor(s) and/or executive management to cut down IT/SD budgets (Switzerland and Austria) and business development strategy improvement by focusing on company's core competences (product/service marketing, customer relationships management etc) (Norway) and freeing in-house resources for other critical tasks (the UK). Thus, cost efficiency and optimization and time to market acceleration are the top 2 pressures that pump up corporate decisions to outsource SD in the UK, Germany and all Nordic countries surveyed; while cost efficiency and optimization and willingness to get access to more expanded and qualified IT resource and talent pools are the top 2 outsourcing drivers in Switzerland and Austria.

Prior to engaging in ITO partnerships, most of companies in all countries surveyed conduct an in-house assessment of the SD elements/areas to be outsourced to the 3d party (**Fig. 9**). Swiss, Austrian and Swedish companies rely on external assistance such as ITO consultancies in their decisions to outsource more often than their fellow companies in the UK, Germany, Netherlands, Denmark and Norway. On the other hand, UK is the country whose companies seek domestic low-cost IT services providers to outsource their SD to more often than companies in other countries surveyed. Another most popular action (after in-house SD needs assessment) is asking other companies for positive vendor references and sending corporate RFPs/RFQs straight to the suggested vendors.

As seen from **Fig. 16**, besides the UK that demonstrates the highest level of satisfaction with the quality of services and project deliverables received (71% of respondents issued 4 and 5 points to their current ITO providers), Switzerland and Sweden are two other countries whose companies are quite satisfied with their current providers (62% of Swiss respondents issued 4 and 5 points to their providers versus 58% of Swedish outsourcers). This tendency may be explained by the fact that Swiss and Swedish companies proactively use professional consultancy services to help define the highest priority areas/elements to be outsourced as well as the entire short- and long-term corporate outsourcing strategy. Companies that try to avoid using professional help are more likely to overestimate own outsourcing needs assessment and, thus, establish the wrong partnerships, use the wrong SD methodology or the wrong destination. All of these factors inevitably lead to the outsourced projects' failures and high levels of dissatisfaction with the outsourcing outcomes (See **Fig. 16**).

Regarding the volume of the outsourced SD in each country surveyed, the research comes up with the following findings: UK and Sweden are the two countries whose companies outsource most of their SD function (90% to 100%). On the contrary, Netherlands is the only country with the greatest number of companies outsourcing less than 10% of their SD volume (**Fig. 10**). Additionally, most of German and Danish companies outsource 60%-89%, most of Swiss and

Dutch companies outsource 10%-39%, while most of Austrian and Norwegian companies – 40%-59% of their SD volume.

Regarding the most outsourced areas of SD expertise, all of the surveyed countries have the same or nearly the same indicators: Web 2.0 is the most demanded area, followed by Enterprise 2.0. Germany and Sweden demonstrate the highest rates of mobile development outsourcing (21% and 20% of respondents correspondently), while Switzerland shows the highest rate of the outsourced embedded development (17% of respondents) and Norway shows the highest rate of SaaS/Cloud computing outsourcing (15% of survey participants) (See [Fig. 11](#)).

[Fig. 12](#) demonstrates the key drivers of the choice of the outsourcing destinations in Europe in 2010. Low costs of software development and maintenance is the major factor helping determine where to locate the outsourced development in all countries surveyed except Austria, where the major factor is geographical and cultural proximity. According to [Fig. 5](#), Austria shows very high rates of outsourcing nearshore and nearshore and within own country. Surprisingly, but, on the other hand, Austria (along with Norway) shows the smallest percentage of companies outsourcing their SD within own country (only 5% of respondents). Other most frequently cited factors (in all countries surveyed) are: available IT resource and talent pool and positive references. Factors such as political/economic stability, legal system maturity, IP security, strong R&D base and proficient English language skills are considered by companies in the lowest priority.

In order to select an ITO partner, most of the companies surveyed in the UK and Sweden consider low services rates, while most of German, Swiss, Austrian, Dutch and Norwegian outsourcers consider vendor references and positive track record. Availability of specific skills that are hard to find within own country appears to be important for the majority of the UK, German, Dutch, Swedish, Danish and Norwegian companies, while innovative business model is a very decisive factor for German, Swiss, Danish and Norwegian outsourcers.

Further, IT Sourcing Europe explored the way how actual annual incurred costs of the outsourced SD compare to the expected (contracted) ones in each country surveyed ([Fig. 14](#)). The study shows that the actual and the expected costs are about the same for most of the UK, Swedish and Danish companies. For most of German, Swiss, Austrian, Dutch and Norwegian companies the actual incurred costs are up to 25% higher than expected. Denmark is the only country among the surveyed ones whose outsourcers (2% of respondents) have actual costs to be 50% to 75% lower than expected. Additionally, 2% of the German, 1% of the Swiss, 1% of the Austrian and 1% of the Dutch respondents claim that their actual incurred costs of outsourcing are more than 75% lower than expected.

Overall, as shown on [Fig. 15](#), the majority of the UK, Swedish and Danish companies save 40%-59% of operating costs from the outsourced SD, while the majority of German, Swiss, Austrian, Dutch and Norwegian outsourcers save 10%-24%. Less than 10% of costs are saved by relatively big numbers of companies in Germany and Netherlands, while more than 60% of costs are saved by a lot of Austrian companies.

As seen from [Fig. 17](#), most of Western European and Nordic ITO services buyers (cumulative 40.96%) still engage with their partners via “traditional” outsourcing models such as dedicated development center (DDC) or captive centers etc, which do not allow them to have as much control of the outsourced projects and development team members as possible and have transparent pricing structures. Only cumulative 21.52% of the European companies know exactly and cumulative 1.52% know partially what they pay for and are fully/partially involved in the process of HR hiring for their outsourced projects. This finding is demonstrative of the growing number of Western European and Nordic companies who enter the ITO relationships via some innovative business models, able to provide them with better control of the outsourced projects and, thus, better ROI.

Further, IT Sourcing Europe explored the key challenges and issues in the outsourced SD and their most popular solutions. As shown on [Fig. 20](#), delayed

product deliveries and missed milestones are reported to be the most critical SD outsourcing challenge by most of the UK, German, Swiss, Swedish and Danish companies. Alternatively, a lot of the UK and Dutch companies point to time and cultural difference as the most critical challenges of their SD outsourcing. IT Sourcing Europe determined the top three challenges for each country surveyed (in a descending way from most to least faced): UK – delayed delivery, time/cultural difference and poor client-vendor relationships; Germany – delayed delivery, poor PM from vendor’s side and hidden agenda (actual costs far exceed the expected ones); Switzerland – delayed delivery, hidden agenda and poor client-vendor communication; Austria - poor client-vendor communication, hidden agenda and delayed delivery; Netherlands – time/cultural difference, poor client-vendor communication and delayed delivery; Sweden - delayed delivery, poor PM from vendor’s side and hidden agenda; Denmark - delayed delivery, poor client-vendor communication and poor quality of delivery; and Norway - poor client-vendor communication, delayed delivery and time/cultural difference. The less critical challenges identified are: excessive vendor’s bureaucracy, insufficient data safety, change of management and inability to control and reduce vendor’s staff turnover. The lack of appropriate resources from vendor’s side can be considered to be a somewhat critical issue in the process of successful outsourced development.

To respond to the most critical challenges, most of companies from all of the surveyed countries increase face to face communication, revise their ITO engagements and dedicate more managerial resources. They do it by hiring additional ITO and/or project managers, relocating them to work permanently on vendor’s site, improving the training function for the outsourced teams, changing SD methodology, process, interaction with team members and PMs, canceling current ITO contracts and looking for new partners etc (see [Fig. 21](#)). Another big ratio of companies extends project deadlines and brings in outside assistance such as ITO consultancies etc.

The least popular actions include: dedication of more IT resources for the improvement of client-vendor relationships, vendor management redesign and SD outsourcing termination and back-sourcing (bringing development back to house). It is interesting to note that Swedish and Norwegian outsourcers are most active in cancelling ITO engagement and back-sourcing, while German ITO buyers are most reluctant to cancel their outsourced development.

Overall, the above findings make an impression that in most of cases today’s SD outsourcers are ready to sacrifice fast time to market for the benefit of retaining their current ITO engagements. On the other hand, Western European and Nordic outsourcers become more insistent in challenging their ITO partners to improve value-added services, PM and product quality and to provide transparent cost structures as well as a combination of speed, cost management and growth supported by business agility and unprecedented technological innovation.

Further, IT Sourcing Europe asked survey participants to share their general impressions of the outsourced software development. As reflected on [Fig. 18](#), more outsourcers have rather positive than negative outsourcing experiences. Thus, the majority of companies in all countries surveyed admitted the fact that outsourcing their software development has been the right decision after all. The statement that it is critical to have backup providers in case the primary provider is unable to meet deadlines and/or commitments was supported by most of the surveyed companies with dominance from Netherlands and Germany. The statement that it is important to have the supplier’s team located within or close to the same time zone (i.e. nearshore) was supported by most of the surveyed companies with dominance from the UK and Denmark. The statement that provider’s work is of higher quality compared to the in-house capabilities was supported by most of the surveyed companies with dominance from Germany and Switzerland, while the statement that provider’s work is of lower quality compared to the in-house capabilities was mostly supported by Austrian, Dutch and Swedish outsourcers. The statement that providers have more discipline,

which can lower down costs further in a longer-term perspective, was mostly supported by the UK and Danish companies.

Further, the majority of the Swiss respondents, followed by the German ones, claimed that costs were higher than expected. The majority of German, Austrian and Danish outsourcers expressed concerns that their IP is at risk. Most of German, Dutch and Norwegian outsourcers complained that ITO providers were unreliable and not focused on mid- to long-term cooperation. The most dissatisfied with the decision to outsource their SD are the German companies, while the Norwegian outsourcers appear to be the least dissatisfied ones. Additionally, most of Norwegian and Austrian outsourcers believe that although the outsourced development lowers down the operating costs, it inevitably increases the PM costs.

Further, IT Sourcing Europe explored reasons why companies in the countries surveyed refuse to adopt SD outsourcing. As shown on [Fig. 19](#), the most frequently cited reason is that companies want to have 100% control of their SD projects. Additionally, the majority of the UK, German, Swiss and Danish companies do not outsource, because they are afraid of hidden agenda/overheads; most of the UK, German, Austrian, Danish and Norwegian companies do not get any pressure from investors and/or executive management to reduce costs and/or cut down SD budgets. Most of the UK, Dutch and Norwegian companies do not outsource, as they do not actually believe in the high-tech potential of the low-cost countries, the qualification of their IT resource and talent pools and quality of delivered products and services. Most of the Austrian companies followed by the Norwegian ones do not outsource, because they think they are yet too small, immature and/or have underdeveloped infrastructures to be able to successfully adopt the outsourced development. Most of the UK, Austrian, Dutch, Danish and Norwegian companies also think that the outsourced SD will eventually cost them more money, resources and other 'headaches', compared to the in-house capabilities and think

that the outsourced SD will eventually result in poorer quality and, as a result, higher customer dissatisfaction rates.

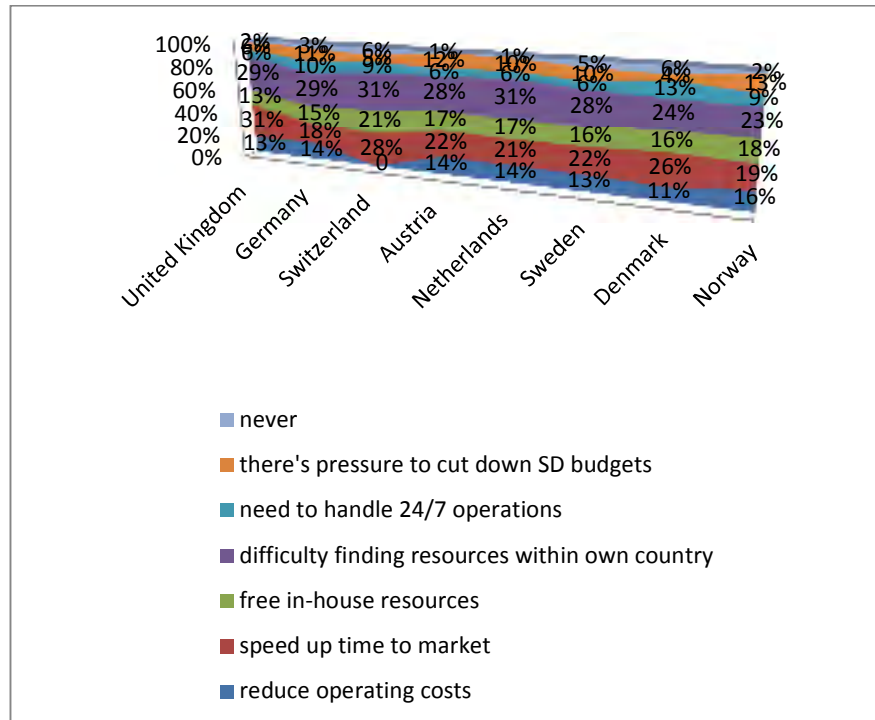
It is interesting to note that very few companies in the countries surveyed do not outsource, because they think that outsourcing is an unethical practice and work should be kept within own house and own country and because they had negative outsourcing experience in the past.

All of the above findings prove the overall efficiency of the outsourced SD, its actual potential to leverage operating costs, optimize IT and human resources, improve business development strategy, accelerate time to market and bring both short- and long-term value to corporate growth and sustainability.

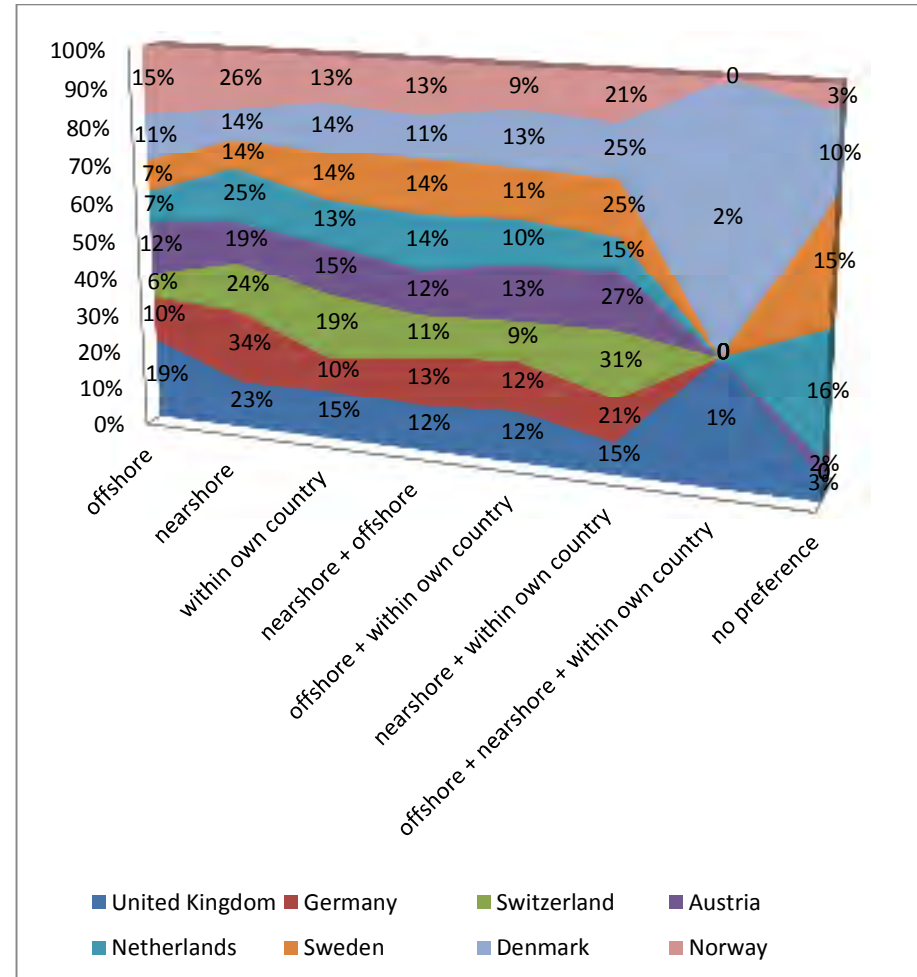
### Part III: Forecast on the Future Adoption of the Outsourced Software Development by Western European & Nordic Companies

The following country-specific data are presented in the form of industry aggregates.

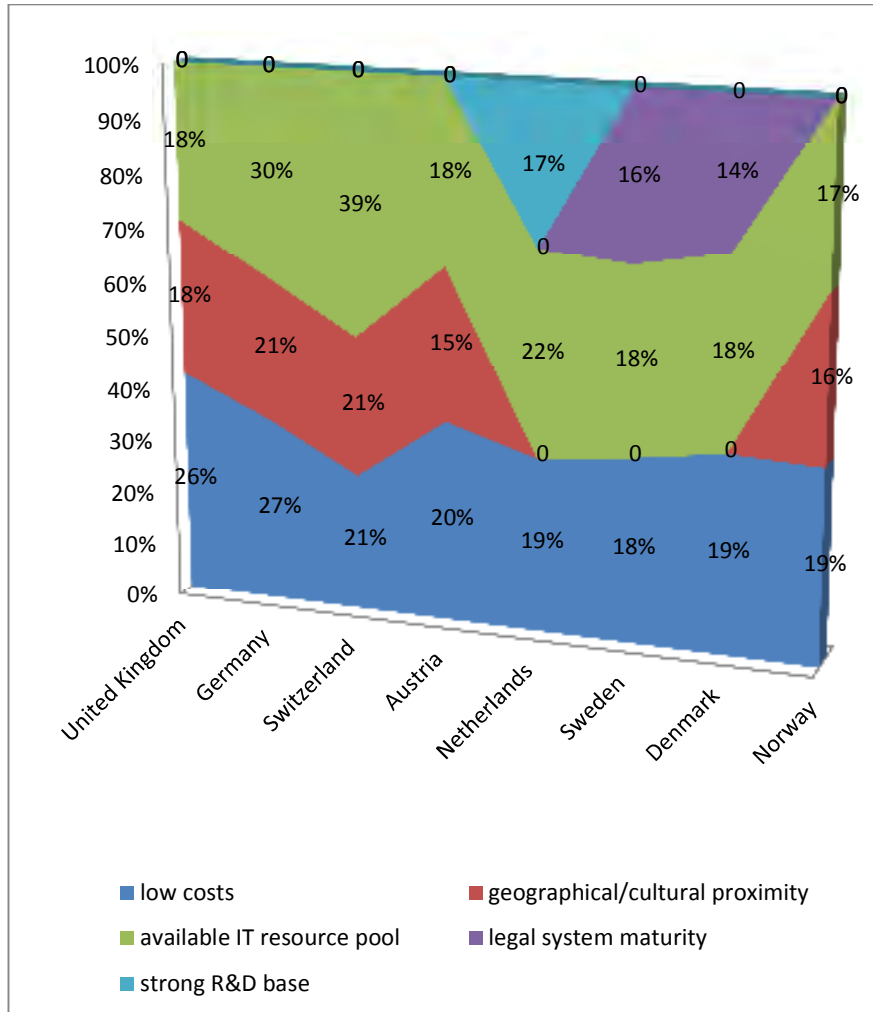
**Figure 22: Factors that will drive more companies to adopt the outsourced software development in the years to come**



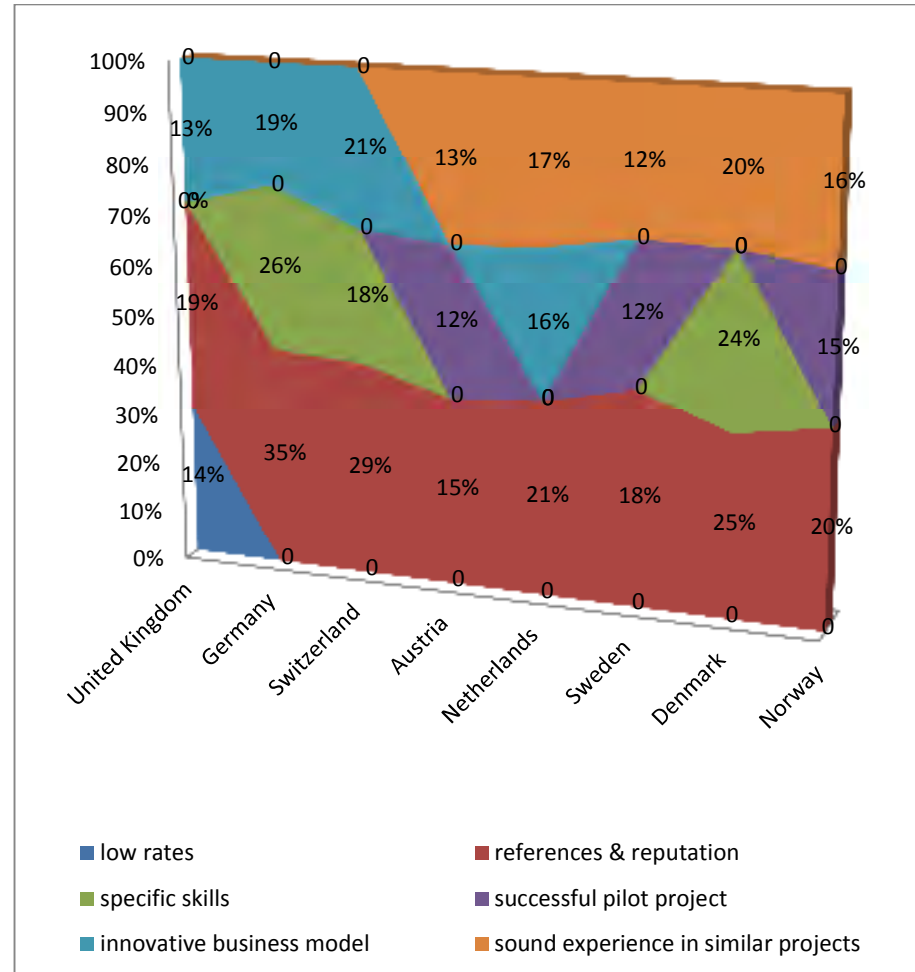
**Figure 23: Where will today's non-outsourcers place their outsourced development in the future?**



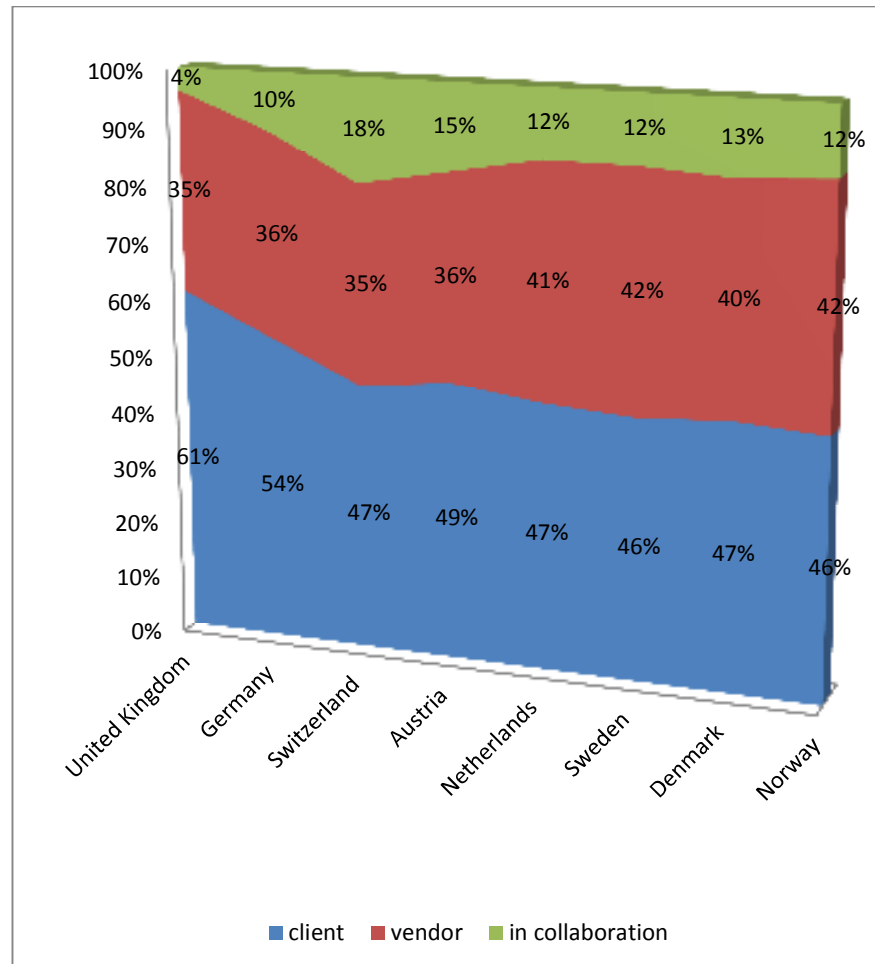
**Figure 24: Top Three destination selection criteria to be considered in the future outsourcing decision making**



**Figure 25: Top Three vendor selection criteria to be considered in the future outsourcing decision making**



**Figure 26: Who will decide on the size and cost of the outsourced development team(s) in future SD outsourcing?**



## Findings' Discussion

IT Sourcing Europe has surveyed non-outsourcing companies in the selected countries in order to be able to predict to possible scenarios of future adoption of SD outsourcing in Western and Northern Europe. Based on the findings of IT Sourcing Europe's country-specific surveys of the in-house software development, the following forecasts were made:

- 1) **Surprisingly, but reduction of operating costs will not be the key driver of future decisions to outsource part of/entire SD, unlike in 2010 (Fig. 22).**

In the years to come, Western European and Nordic companies will source IT resources outside of their home countries due to the significant shortages of domestic IT resources and specific skills. It will be the number one reason for most of German, Swiss, Austrian, Dutch, Swedish and Norwegian companies. In the United Kingdom and Denmark, though, most of companies will most likely choose to outsource in order to accelerate time to market. Overall, it is the second most popular driver of future decisions to outsource SD. The third most popular driver is the need to free in-house resources for more critical business goals and core competencies. The less important factors cited are: need to handle 24/7 operations (support functions outsourcing) and pressure from investors/executive management to cut down the SD budgets.

This forecast is enhanced by the findings of the In-House SD survey 2010 with regards to the most critical challenges facing today's non-outsourcers in the selected countries. According to the findings, slow time to market, high cost of in-house development and maintenance and lack of domestic IT resources and skills are the top three barriers in the way of successful SD within own house. These challenges basically set the ground for the future profile of companies that outsource their SD function to the 3d party offshore, nearshore and/or within own countries. It suggests that in the near future Western European and Nordic companies will be looking out to outsource their SD to accelerate time to develop, implement and market the product/service and to have an opportunity to win their own niche at the market before the competitors do so.

As most of today's non-outsourcers refuse to outsource, because they want to have 100% managerial control of the SD projects and teams involved (see [Fig. 19](#)), the future ITO engagement will inevitably shape this factor. A greater focus will be placed on the long-term benefits from outsourcing as well as use of outsourcing for strategic goals of business development improvement rather than sole cost reduction achievement. The findings of the given study demonstrate well that future outsourcers will have to establish specific partnerships with their ITO services suppliers, in which the management role will be assigned to the client, while the supplier will act as a resource and skills supplier rather than a project executor. Companies will be looking for innovation via agility and flexibility combined with payment transparency. The latter will shape the overall state of affairs in the post-recession business world, where companies tend to grow smart towards money spending and proper investments allocation.

**2) More Western European and Nordic companies will be sourcing nearshore ([Fig. 23](#)).**

Cumulative, only 6.96% of companies surveyed (from all countries selected) admitted the likelihood of outsourcing offshore in the future, versus 14.4% of those who plan to outsource nearshore. This finding proves the assumption that nearshore SD outsourcing will be the key outsourcing destination in the years to come. 2010 as well as the previous post-recession year have shown an unprecedented trend towards SD quality, speed and sustainability. Managing an SD project outsourced as closely to the home country as possible eliminates extra hassle associated with development teams management, long and expensive trips to vendor's site, time and cultural difference etc. On the other hand, nearshore outsourcing is able to increase project traceability, face-to-face communication between the client and vendor and, in case of disappointment with the outsourced development, shortens time to back-source.

Another future tendency observed is that companies will tend to try and challenge several potential ITO vendors to decide whom to stay with for long-term cooperation and benefits. Thus, outsourcing SD projects nearshore is able to facilitate the task of disseminating the outsourced projects among two and

more vendors in different locations, including the homeland, and then to move several pieces of project to the main provider.

**3) Low costs will continue to map the future SD outsourcing destinations ([Fig. 24](#)).**

Although, as seen from [Fig. 22](#), cost reduction will not be the main driver of the corporate decisions to outsource SD in the near future, low costs will still be considered among the primary criteria in the process of selecting the outsourcing destination. Low costs are one of the top three future SD outsourcing location selection criteria in all countries surveyed, with dominance in the UK, Netherlands, Denmark and Norway. Another important criterion identified in the course of the research is geographical and cultural proximity, cited among the top three selection criteria in the UK, Germany, Switzerland, Austria and Norway. Available IT resource pool is the third most frequently cited criterion in all countries surveyed. As a shortage in domestic IT resource and talent pool is one of the most critical challenges of the in-house SD in 2010, it is logical enough for future outsourcers to focus on locations with high annual numbers of IT graduates and IT workforce employed, strong R&D base/legacy and legal system maturity.

**4) Most of today's non-outsourcers in Western and Northern Europe will partner with ITO suppliers with positive references and strong track record in the future ([Fig. 25](#)).**

Positive references and reputation will be the main driver of the future choice of the ITO provider, according to the given research findings. This factor was marked by the majority of participating companies from all countries surveyed (cumulative 14.5%). This tendency will eventually challenge ITO providers to improve their client management and retention practices, expand the range of add-on and value-added services such as consultancy, staff training etc and offer innovative business models able to provide the clients with 100% control of the outsourced projects, no hidden agenda and minimal errors fixing at the production and post-release stages. ITO providers will also be challenged to find the golden ratio between new client winning and existing client retention and to

make customer relations practices work side by side with the sales and marketing efforts.

Access to specific skills which are hard to find within home country is named among the top three vendor selection determinants by most of German, Swiss and Danish companies. Innovative business models are named among the top three vendor selection criteria by most of the UK, German, Swiss and Dutch companies. A lot of Austrian, Swedish and Norwegian non-outsourcers named successful pilot project completion by the potential vendor as one of the most decisive drivers of their future choice of the ITO partner. Additionally, most of Austrian, Dutch, Swedish, Danish and Norwegian companies pointed to vendor's sound experience in similar projects as one of the three factors influencing their future outsourcing decisions. Surprisingly enough, but low service rates were named among the top three future vendor selection criteria by most of the UK companies only. In other countries surveyed, companies did not put low rates among their top three vendor selection indicators.

**5) In the future, more outsourcers will strive to control their outsourced projects (Fig. 26).**

Unlike current SD outsourcers, most of whom do not know the exact salaries of each of the member on the outsourced team and are not involved in the process of hiring the HR to be involved in the outsourced project(s) (see [Fig. 17](#)), the future Western and Northern European outsourcers will tend to be more active in the outsourced project management and monitoring of vendor's staff turnover (which is a very critical issue influencing success or failure of the outsourced projects).

To conclude with, in the upcoming years more companies from Western and Northern Europe will outsource their SD mainly for the purpose of getting access to qualified IT resources and to speed up time to market. Future outsourcers will be sourcing mostly nearshore and will demand from their ITO vendors the following: strong track record as a credible and reliable IT services provider, differentiation, outstanding technology expertise and projects portfolio, transparent pricing structures, 24/7 support, involvement in HR hiring process

and team members' compensation negotiation, strong ability to retain and grow staff, the state-of-the-art quality and grasp of innovation and cultural proximity. Low costs of SD as well as low IT salaries (compared to the domestic market) will be the number one reason of the choice of the future outsourcing destination, while references and reputation will be the major driver of the future choice of the outsourcing partner. Western European and Scandinavian ITO services buyers will be focused on establishing long-term relationships with their ITO partners. It will no longer be enough for companies just to offload their SD to the vendor and focus on core competencies; companies will tend to get as much managerial control of their outsourced SD projects as possible and will need more open and face-to-face communication with their vendor's PM and development teams.

## Part IV: Conclusions and Recommendations

The All-European IT Outsourcing research 2010 shapes the highly unsettled conditions in which most of today's Western European and Scandinavian outsourcers work. Companies basically use outsourcing to leverage operating costs and increase in-house capacity by embracing on-demand strategies aimed to achieve their global reach and fix market presence. Therefore, companies prefer easily scalable, pay for use models to process-packaged, capital-intensive and fixed-cost engagements. Outsourcing plays a vital role in margin protection by providing an opportunity to quickly scale up and downsize SD budgets without harming the end-product quality. In the past years, ITO services providers in Central and Eastern Europe were hungry for new clients from Western and Northern Europe and, thus, made aggressive actions towards winning the clients and helping them optimize their IT costs, while upgrading and enhancing own infrastructures in part at the client's cost. Providers strived to make a fortune off the immediate income and cared more about filling up their pipeline than retaining the existing clients. As a result, most of providers became hardwired in the traditional way of thinking and focused on short-term benefits, thus failing to establish strong partnerships based on the concept of mutual trust, credibility and permanent "bar raising". This led to the failure of most of the outsourced projects and rather high rates of customer dissatisfaction with services and deliveries received. Modern companies no longer need process-packaged relationships and excessive vendor's bureaucracy. Instead, they need agility, flexibility and speed, combined with access to vast IT resources and specific skills, to solve their current challenges of the in-house development such as the lack of domestic IT resources and man force, high costs of development and maintenance, staff turnover etc. Today's SD outsourcers need to create a core capability of reinforced operating flexibility that will eventually contribute in development of highly valued business partnerships rather than unavoidable "overhead" that outsourcing is often associated with nowadays.

On the other hand, the research demonstrated well that SD outsourcing in 2010 is different from outsourcing of, say, ten years ago. It is no longer a risky undertaking for the majority of companies, regardless of their size, annual revenue and business goals; instead, it is a mainstream strategy that is being proactively and widely adopted across the corporate universe all over Europe. Today, a typical mid-sized organization in Western or Northern Europe transfers 10% to 59% of the corporate SD function to execution by the 3d party, while a typical large company outsources 90% to 100% of their SD, meaning the entire development lifecycle. It proves the assumption that companies do trust outsourcing and gains one can get from it. When we asked our survey participants to share their general impressions of the outsourced development, the cumulative majority of companies (around 85%) ticked the option "outsourcing our SD has been the right decision". On the other hand, when we asked participating companies to assess their current level of satisfaction with the services, project delivery quality, prices and attitudes provided on a 5-point scale (where 1 is least satisfied and 5 is most satisfied), the cumulative majority issued their ITO partner(s) 3 points, meaning they are somewhat satisfied, but not very much satisfied. These contrasting findings show the actual discrepancy between clients' business needs and the wrong engagement model through which they partner with their providers. It is rather obvious that under the current economic conditions many IT decision makers overestimate their own role and/or believe that it is their duty to the organization to find an external vendor and increase corporate savings. Relying on their own experience, which may not be enough to make the right ITO decisions, they solely select the vendor and location and then have to deal with increased PM costs, vendor's infrastructure improvement and hidden agenda, which prevent companies from enjoying the maximum benefits from the outsourced development in a longer-term perspective. If at least one tiny thing is missed in the process of planning outsourcing strategies (e.g., cultural fit or time difference are not considered from the beginning etc), then the whole project and ITO relationship are at a great risk of going wrong. As a result, the ITO services buyers blame their providers of inability to understand their business goals, using hard-to-manage

business models and/or not delivering on time, often ignoring the fact that they are guilty too, as they couldn't make the right outsourcing decisions and failed developing a smart sourcing strategy. Client's dissatisfaction with their ITO providers can be partly explained by IT executives' wrong understanding of why they need outsourcing at all. This finding demonstrates a strong need of the new thinking in outsourcing, from the partner selection to the project results' measurement. It is high time to begin thinking about outsourcing as an opportunity to add value to the corporate climate by implementing cultural change, adding quickly mature capabilities, introducing new disciplines and methodologies, developing differentiators and best practices and learning from the errors of the past. When more companies begin to think of outsourcing in this way, they will be able to partner based on personal relationship rather than a structured process and, thus, enhance their SD processes and evolve further out of the multicultural environments they create.

Below is a set of actions that IT Sourcing Europe would recommend to every company thinking about the adoption and/or revision of its ITO engagements. We believe that these few preparatory practices will help clients select vendors able to bring innovation, optimize both costs and processes and fit culturally into the organizational alignment.

#### **1) Companies willing to outsource their SD should set clear vision!**

Clarity of corporate vision, mission and goals is critical to success of any ITO partnership. Prior to make any outsourcing decisions, companies should understand their own priorities and drivers, rank their partner selection criteria and, what is more importantly, open a dialogue with multiple stakeholders to determine which areas/elements/processes should be outsourced and which – retained within own house, how to integrate the outsourced and in-house project outcomes at the production stage with as few mistakes and bugs as possible, what SD methodology would best fit in this certain project and what business model to use in the future ITO collaboration. When setting the vision, IT managers on client's side should not forget that outsourcing will inevitably bring

about organizational change that all-level stakeholders will have to cope with. Actions should be planned proactively on how to facilitate different stakeholders' adaptation to the change and how to manage it with minimum damage for internal and external clients. When setting the vision, IT executives should not forget that outsourcing is all about people rather than processes and technology. Outsourcing obviously affects the daily operational activities of many employees involved, so HR management strategy should also be planned in a strategic way prior to entering any ITO relationship.

This research demonstrates that companies who bring in external assistance such as consultancies at the outsourcing planning stage feel more comfortable with their ITO relationships and more satisfied with the overall outcomes of their outsourced development, compared to those that rely on their own experience and expertise when planning an ITO strategy. So, we believe it is important for any organization to hire a group of professional IT auditors to determine which areas of the SD function should be outsourced and how. This investment, although tried to be avoided by many today's outsourcers, will provide the client organization with a significant return in a longer run, because many extra tasks such as bugs/errors fixing at the post-production stage, coverage of resources spent on the project team member's replacement etc will be eliminated or minimized later as the project goes.

The use of professional external help can allow organizations to build internal consensus on their business reasons for outsourcing, ensure that expectations are set properly for both the vendor and the client and the stage is set for the selection and negotiation process to follow.

#### **2) Companies willing to outsource their SD must know own strengths and weaknesses!**

Firms must come to the negotiating table with an accurate assessment of IT needs, current assets, talents and deficiencies. While external auditors can help determine needs for outsourcing, only internal assessment can show actual weak

and strong points of every organization. For instance, many Western European and Nordic companies wait for their vendors to perform due diligence, which is one of the most crucial mistakes leading to high level of dissatisfaction with the outsourced SD and failed projects. Due diligence performance may lead to situations when the clients discover in the middle of the project that their vendor has a much more disorganized infrastructure or unmanageable processes than expected. Such discoveries usually create and enhance the tension within the ITO relationship and set it on the wrong foot. Additionally, due diligence performance may force vendors to use undocumented software and/or processes, which will eventually make it hard to find all ends when the project has been completed. In other words, due diligence performance withdraws client's locus of control and leads the project to become unmanageable and unstructured.

It is a must for the client company to have realistic knowledge of the as-is state of project and to enter a pragmatic outsourcing relationship, able to eliminate or reduce delays in delivery and unforeseen expenses related to the wrong project management on vendor's side.

So, an internal audit of strengths and weaknesses is important to insure that the most critical problem will not be thrown over the wall, while the less critical one is paid too much attention to.

Later on, once determined, all of these weaknesses and strengths should be reflected in the RFP/RFQ to be submitted to the potential vendor. Based on them, the vendor should reflect in his response to the RFP/RFQ his ability to meet the client's expectations, not to dilute the ongoing vendor relationship with ad hoc performance and contract expectations, to understand and plan risk management and to be ready to support the entirety of the function that the client chose to outsource. In other words, in their filled-in RFPs the potential vendors should prove their ability to enhance client's current strengths and turn the weaknesses into new strengths. If the potential vendor fails to do so at the

pre-contract stage, the risk is high that he will fail to do so while the project is on the go.

### **3) Intangible benefits should be a stronger driver of decisions to outsource than mere cost reduction!**

As the given research shows, although in 2010 most of Western European and Nordic companies still choose to outsource to leverage operating costs and/or cut down the SD budgets, a strong tendency is observed that in the years to come more companies will focus on intangible benefits of outsourcing.

Outsourcing SD functions enables corporate IT decision makers to focus on competitive differentiation and innovation rather than keeping the lights on for routine SD functions. Contracting with an external IT services provider allows companies to get access to better expertise and tools, more qualified methodologies and disciplines and other features they would not get access to otherwise.

In Western and Northern Europe it is a way too expensive for some type of companies (startups, small, even mid-sized) to develop and implement own robust applications or hire full-time IT specialists with specific skills (e.g., virtualization experts). Since outsourcing uses clear metrics and performance incentives, it allows many companies, unable to develop own differentiated and highly competitive products within own house, to surface the real cost of SD and escape paying overheads associated with the in-house SD.

### **4) Companies willing to outsource their core development should search for innovative business models!**

By **innovative business models** IT Sourcing Europe means ITO engagements, able to provide agility, scalability and 100% managerial control of the outsourced project and development teams on the client's side. By **traditional business models** we mean engagements in which the vendor takes the client's project and executes it using in-house capabilities and available resources (e.g., DDC or staff

augmentation or project sourcing). The end results are then transferred back to the client and the support/upgrade is retained within the vendor organization. However, as the above findings suggest, today's outsourcers should change their way of thinking towards outsourcing and should tend to transform from mere customers to sole project executors using external resources. That is where innovative models are needed. Their major goal is to allow the client company to retain as much control of the project to be outsourced as possible. This control spreads from payment transactions to PM to staff retention and development.

One of such innovative models that IT Sourcing Europe recommends for consideration during SD outsourcing decision making is the Own Development Team model, in which IT employees fully belong to and are 100% managed by the client. The key differentiator of this model from traditional remote team model is that the client, not the vendor, makes the final decision on recruiting development team members and has 100% managerial control of both the outsourced project and each team member's compensation. Such control is very important, as it allows clients to retain their best employees and, thus, to keep the project at a higher quality level from initiation to completion. This model is perfect for the outsourced end-to-end software product development, as it is transparent, agile, fully scalable and independent from the vendor's technology skill sets. It is equivalent to managing own in-house team, but for lower costs and with no HR or administrative hassle, which is often associated with setting up own SD operations in a lower-cost country.

Within this model, clients partner with vendors under the following conditions: vendor agrees to act as a resource and office space provider rather than project executor and client organization agrees to make a respective change in order to allocate special roles to be in charge of the outsourced project management. Thus, the vendor supplies candidates who best meet client's requirements and the client selects people that he wants to see in his outsourced development team (depending on specification requirements) and negotiates a compensation with each member on the outsourced team, without any interference from the vendor. Every month the client receives a single bill comprised of the fixed vendor's service fee and each team member's monthly salary plus benefits. The client normally invests in the growth and development of his own outsourced

team as much as he wants and, what is more importantly, the client does not pay any overheads and has a chance to retain his best IT people without relying on vendor's HR retention practices. In traditional models, clients have no control over the vendor's staff turnover and cannot influence hiring decisions. Vendors try to literally squeeze as much from their staff as possible, that is why it is quite a common practice in DDC when the same person is involved in two or more different projects executed for different clients, faces a lot of occupation stress and burnout and, as a result, either quits job and looks for a better employer, or becomes demotivated, devastated and does not contribute all of his/her abilities, skills and stamina to the project. In addition, it is usually the client company who pays for new hires, role replacement etc. In Own Development Team model the client selects people and can be sure that these people will work exclusively on his project and it is up to him to motivate staff to work harder and more productively (via material and non-material incentives, business trips, better coaching etc). And if some team member still decides to leave the project, the client will have to find a replacement and to make sure that this replacement is the right fit and not just the "imposed necessity".

IT Sourcing Europe's continuous assessment of this model allows to conclude that it is perfect for both large and small and mid-sized companies and for the core end-to-end development. However, this model can only be successful as long as it is employed within the nearshoring context. Since the model suggests frequent face-to-face communication between the vendor and the client, it can hardly be manageable within the offshoring context, when outsourced teams are located 7 to 9 hours away from the home country. To ensure success within Own Development Team model, it is a must to locate the development team within or close to the same time zone.

The findings of the given study support the assumption that the Own Development Team model is likely to become the most demanded one in the years to come because of its agility, scalability and transparency. Today's outsourcers articulate their desire to have 100% managerial control of the outsourced projects, more open communication with the vendor's PM and development teams and payment transparency. Cumulative 10% of all companies surveyed (from all countries) (see [Fig. 18](#)) admitted the importance of having the vendor's development team located nearshore, which also supports

the statement that in the years to come Own Development Team model will be the major engagement means in global outsourcing.

**5) Companies must be able to manage their ITO relationship on a 24/7 basis!**

Now when the company has signed the ITO contract with the most fitting ITO vendor and has gained 100% managerial control of the outsourced project and development team, it must adjust/revise its corporate management policies to be able to properly manage the ongoing relationship. The ITO partner management requires specialized skills, strategic understanding of business and IT goals, strong negotiation and mediation capabilities.

Choosing to partner via an innovative business model means going beyond the typical Service Level Agreement (SLA) scope and requires an entirely new set of managerial skills. So, the client company should invest in hiring and developing own outsourcing manager(s) with an extensive experience of successful integration of the outsourced teams into the in-house IT team/department, strong facilitation and conflict management skills etc. In general, a good ITO manager is the one who is able to function equally well in four dimensions: quality, finance, relationship and strategy. In terms of quality, the ITO manager should monitor outsourced team's compliance with contract and accuracy of delivery. The specifically designed metrics should enable ITO clients to put their expectations to the plate rather than just hope for such qualitative benefits as process improvement or innovation and then turn those expectations into the critical project success factors. In terms of finance, the ITO manager should make sure that the actual incurred costs of outsourcing match the contracted ones and the overall payment structures are transparent and not process-packaged. In terms of relationship, the ITO manager should be able to plan the time and effort needed to establish relationship of mutual trust and reliability and make appropriate effort in reaching this goal. And in terms of strategy, the ITO manager should be able to track how current ITO strategy matches the corporate business goals and IT needs and make forecasts as to which direction the outsourcing strategy will move in the next 6 to 12 months, 1 to 3 years etc. These four dimensions both as a synergy and as separate units should aim to achieve

long-term benefits and help grow the company and differentiate the product/service.

To conclude with, IT Sourcing Europe reminds that outsourcing is a people-centric, rather than a process-centric business and cannot be treated as a simple business transaction. The client company should clearly realize why it is going to adopt the outsourced development and what benefits to expect from it. Without clear vision and goals companies are nearly doomed to fail their ITO engagements.

Although successful transition of the contracted responsibilities to the outsourcing provider is essential, it is not sufficient, as the primary focus should be placed on team morale improvement, combatting resistance to change and achievement of multicultural evolution with strict adherence to the key performance indicators and SLAs.

We believe that in the future the success of the ITO partnerships will be measured not by the significance of savings achieved, but by the client's ability to outsource SD and insource knowledge, skills, innovation and the state-of-the-art quality of development.

## About IT Sourcing Europe

IT Sourcing Europe Ltd is a UK-based research and consultancy company specializing in nearshore IT/software development Outsourcing. Our services include:

- Independent IT Outsourcing market research and analysis
- Independent surveys of Western European outsourcers and their ITO demand
- Independent surveys of Central and Eastern Europe's ITO services providers and their factual capability to deliver top quality products and services on time and on budget
- Consultancy and recommendations to companies planning to change their current outsourcing strategies
- Consultancy and recommendations to companies planning to outsource their IT function nearshore
- Custom market and competition research and surveys

Contact Details:

### ***IT Sourcing Europe Ltd***

The Meridian, 4 Copthall House,  
Station Square, Coventry, West Midlands,  
CV1 2FL United Kingdom  
Email: [info@itsourcing-europe.com](mailto:info@itsourcing-europe.com)  
Tel.: +44(0)2476992505  
Web: [www.itsourcing-europe.com](http://www.itsourcing-europe.com)

## © 2010 IT Sourcing Europe Limited, All Rights Reserved

Unauthorized reproduction or distribution in whole or in part in any form, including photocopying, faxing, image scanning, e-mailing, or making available for electronic downloading is prohibited without written permission from IT Sourcing Europe Limited. Prior to photocopying items for internal or personal use, please contact IT Sourcing Europe Limited. All trade names, trademarks, or registered trademarks are trade names, trademarks, or registered trademarks of their respective owners.

Information contained in this publication has been compiled from sources believed to be reliable, but the accuracy of this information is not guaranteed. IT Sourcing Europe disclaims all warranties and conditions with regard to the content, express or implied, including warranties of merchantability and fitness for a particular purpose, nor assumes any legal liability for the accuracy, completeness, or usefulness of any information contained herein. Any reference to a commercial product, process, or service does not imply or constitute an endorsement of the same by IT Sourcing Europe.

This publication is designed to provide accurate and authoritative information in regard to the subject matter covered. It is sold or distributed with the understanding that IT Sourcing Europe is not engaged in rendering legal, accounting, or other professional service. If legal advice or other expert assistance is required, the services of a competent professional person should be sought.