Five Strategies for Global Sourcing of Application Development

Why Captive ODC makes sense for Enterprise IT

A Lionbridge White Paper

February 3, 2005
Executive Summary

Companies considering global sourcing of application development will want to evaluate multiple approaches before making a decision. Five high-level business strategies exist for offshore execution:

- Tactical Outsourcing
- Captive ODC (Offshore Development Center)
- Build-Operate-Transfer
- Do-It-Yourself ODC
- M&A (Mergers & Acquisitions)

While this paper describes the benefits of each strategy, enterprise IT organizations working with a Captive ODC can expect these standout benefits:

1. Short and long-term cost efficiencies
2. Optimal accountability for productivity and quality
3. Short and long-term risk avoidance

With Captive ODC, a partnership is formed between an established service provider and a client company to use the service provider’s dedicated offshore delivery center to support the company’s development needs. The relationship is longer-term and more exclusive than traditional outsourcing, giving client companies an appropriate number of dedicated, expert resources to use over a set period of time.

For application managers, program offices, and CIOs operating in a three to five year planning window, we believe the Captive ODC offers compelling advantages for programmatic application development and maintenance.

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Captive ODC offers a safe and effective means of remaining competitive in the global marketplace. It is not necessary to own the infrastructure to take advantage of global sourcing.
The Move Offshore

Competitive pressures are compelling U.S. companies to consider offshore outsourcing. Many have already moved application development to places like India, Russia, and China. Eighty-six percent of participants in DiamondCluster International’s 2004 Global IT Outsourcing study expect their use of offshore IT outsourcing to increase over the next 12 months (up from 32 percent in 2002).

Microsoft, for example, has set up development centers in India, China, and Israel. Other leading independent software vendors, such as Oracle, Siebel, and SAP, have also moved development offshore.

Freeing up internal resources to focus on more critical initiatives has emerged as a key factor, further fueling the outsourcing trend.

Why the increased sense of urgency? IT organizations face harsh realities.

- Infrastructure and applications increase in complexity as enterprise management expects more from the IT organization.
- Technology and customer requirements continue to evolve, forcing companies to look at how effectively they have trained and re-skilled their development teams.
- There are greater risks associated with relying on a technical talent pool from a single geography.
- Resource requirements always fluctuate, making planning a challenge.

The cost of retraining developers to become proficient in modern technologies, such as Java and .NET, is significant. Recent data shows that 75 percent of enterprises that seek to become early adopters of new technology will fail. This is due to both a lack of skills and an inability to change their risk tolerance and IT budgeting patterns [Gartner, December 2003].

For IT organizations dealing with these challenges, the appeal of offshore outsourcing is growing, and not simply for the cost savings. According to 2004 DiamondCluster research, the outsourcing euphoria seen in 2002 has been replaced with a focus on outsourcing as a business-enabler. While reducing costs is still the number one reason that companies look to outsource, freeing up internal resources to focus on more critical initiatives has emerged as a key factor, further fueling the outsourcing trend.
Companies that are thinking about outsourcing will want to consider a variety of approaches before making a decision. In this paper, after a short review of five offshore models, we focus on the Captive Offshore Development Center (ODC). We believe Captive ODC is the most effective model for Enterprise IT development under the following conditions:

- Enterprise applications requiring multi-platform support and migration.
- Ongoing code support for “Sunset” platforms — applications no longer under active development, with a significant user base.
- Predictable development requirements over a 3-5 year timeframe.

For Enterprise IT organizations, innovation and core development may continue in the US, Europe, or Japan, while code maintenance and migration activities move offshore. However, Indian ODCs have increasingly become key providers of architecture services, e-business development, and application integration [Gartner, October 2003].

Offshore Options

There are five approaches to consider when moving application development and maintenance work offshore.

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**Scalability** — The ability to rapidly scale operations requires existing offshore infrastructure, HR personnel, and training facilities.

**Long-term cost avoidance** — Owned offshore operations increase fixed expenses, and if needs change, exiting can be costly.

**Short-term cost avoidance** — Captive ODC and Build-Operate-Transfer minimize outsourcing costs by committing to a base staffing level for a multi-year term.
Knowledge retention — In Tactical Outsourcing, knowledge inevitably degrades between one project and the next, as individual contributors come and go. M&A also poses risks, as acquired management and other employees may depart.

Productivity and Software Quality — Outsourcing vendors must meet specific criteria in order to win contract renewals, giving customers optimal leverage on these issues.

Long-term risk avoidance — As market cycles, corporate development goals, and geopolitical and macro-economic climates evolve, owned offshore infrastructure and employees could become a liability.

Short-term risk avoidance — The added impetus for knowledge transfer in Captive ODC and B-O-T eliminates a key risk of Tactical Outsourcing. With Captive ODC and B-O-T, you also avoid a series of hurdles found in Do-It-Yourself or M&A: regulatory issues, hiring and training, management inexperience with international operations, etc.

Tactical Outsourcing

Contracting out your development work to an offshore vendor means outsourcing on a project-by-project basis.

- You avoid the cost and challenge of updating your organization’s technical skills every time a project requires a special capability.
- As your development cycles ebb and flow, you are able to staff your projects with appropriate numbers of low-cost resources.
- If performance becomes an issue, you are able to terminate the outsourcing relationship.
- Pricing is based on project scope — either time & materials or a fixed bid.

Captive ODC

Like tactical outsourcing, a Captive ODC provides your company with an extended development arm that already has dedicated physical space and an established system infrastructure. The important difference is that the ODC provides you with resources that are 100 percent dedicated to your development work for the length of your contract — typically three to five years. This creates a more stable and reliable production environment and gives you the workforce you need to support your ongoing development programs. It also gives you cost benefits.

- Dedicated resources are made available to you for a flat rate, based on the number of developers you need.
- You commit to a fixed number of years, adding or subtracting from that timeframe after a minimum engagement period.
• You mitigate your risk in hiring and building a team.
• Very little of your management bandwidth is required to get your teams up and running.
• You have access to a wide range of skills and technology expertise.
• You retain continuity of business and process knowledge around your applications and users.

When built within or in tandem with an established infrastructure, such as the Lionbridge facility in Mumbai, India, a Captive ODC can save you 40% on infrastructure costs and 30% on facility costs compared to Do-It-Yourself ODC.

**Build-Operate-Transfer (B-O-T)**

While the Build-Operate-Transfer model is a long-term solution with many of the same benefits of Captive ODC, an important difference is the anticipated transfer of ownership.

• You are able to establish a subsidiary with minimal upfront investment.
• The transferred team hits the ground running from day one.
• There is minimum disruption to your development cycles.
• Typically, M&A is triggered only by pre-set productivity, quality, and scale parameters.

**Do-It-Yourself ODC**

Building your own ODC requires a large investment in time and money, with scaled results typically not realized for many years. With an organic approach, you need to:

• Build and manage an offshore infrastructure, including property, facilities, and telecommunications. Issues as fundamental as electricity, water, and physical security must be addressed.
• Hire highly skilled developers to work in the offshore country, as well as experts who have successfully established and managed international IT operations.
• Buy and maintain all the necessary development equipment, software, and services.
• Provide language and cultural training for newly hired offshore workers, as well as for current personnel who manage or interface with offshore staff.
• Ensure cohesion of corporate culture in transnational work environment.
M&A

Buying an established offshore development company gets you up and running more quickly, but finding the right company can prove difficult, and your investments are significant and permanent.

- Many of the best IT companies have already been bought.
- Technical proficiency and work quality are issues. If the company you buy is sub-standard, your risks increase.
- Seasoned, multi-lingual project managers are needed to work through language and cultural barriers.
- Not all companies have the money or expertise to make Offshore M&A succeed.

Like Do-It-Yourself ODC, M&A should be considered only when a strategic imperative exists.

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<th>Preferred approach</th>
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<td>zero to 36 months</td>
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<td>Captive ODC</td>
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<td>five to 15 years</td>
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Why Captive ODC Makes Sense for Enterprise IT

Enterprise IT departments have specific goals for offshore development. For application managers, program offices, and CIOs operating in a three to five year planning window, we believe the Captive ODC offers compelling advantages for programmatic application development and maintenance.

Enterprise IT outsourcing goals

In addition to reducing the total cost of building internal business systems, enterprise IT departments seek to build and maintain a greater number of applications for the same budget dollars. They want to improve their service levels and timelines, and can benefit from exposure to new skills and industry best practices. As IT organizations acquire flexibility and scale through programmatic use of offshore execution, managers are able to refocus their existing internal teams on core business activities.

Enterprise IT concerns

Enterprise IT organizations are looking for guarantees and service level agreements (SLAs) from their offshore relationship. The offshore method they select must offer a mature software development process as well as proven success in knowledge transition and process migration. State-of-the-art tools and technologies, along with strong communication skills, complete the requirements list.

Characteristics of Captive ODC

Captive ODC is a growing trend in offshore programming services, particularly in India. With Captive ODC, a partnership is formed between an established service provider and a client company to use the service provider’s dedicated offshore delivery center to support the client’s development needs.

Typically, the service provider commits state-of-the-art workspace, a highly skilled technical talent pool, servers, workstations, and software to the arrangement. A seamless extension of the client’s development environment is formed, with built-in flexibility to adhere to the client’s project governance models, key processes, and best practices.
Captive ODC is best used for programmatic development where a fixed number of resources are required on an ongoing basis.

The service provider assumes responsibility for the cost and management of organization-wide services like infrastructure, communication, process compliance monitoring and improvement, certified quality audits, human resources, and training. This enables the client to reap the benefits of the ODC more quickly since the service provider has already established these functions.

The relationship is longer-term and more exclusive than outsourcing, giving client companies an appropriate number of dedicated, expert resources to use over a set period of time. Unlike outsourcing, which provides offshore developers on a project-by-project basis, this model is best used for predictable programmatic development where a fixed number of resources are required on an ongoing basis.

Key features of Captive ODC

**Project governance and SLAs**

Established service providers typically bring their own process optimization, QA methodologies, and project governance models to the management of an ODC. The following elements must be harmonized with the client's existing work practices:

- Institutionalized quality initiatives (ISO 9001, etc.)
- Project tracking methodologies
- Process management frameworks
- Risk management and business continuity
- Configuration management
- Metrics-based performance reviews
- Communication

Well-defined SLAs ensure that the ODC will meet client requirements for a range of performance targets, including:

- Productivity
- Schedule adherence
- Knowledge transfer efficiency
- Product defect thresholds

Industry enforced certifications such as CMM ratings and ISO 9001 registration are critical elements to ensure process maturity and the institution of quality programs at vendor sites.
Global program management

Dedicated and experienced ODC program managers ensure that customers receive metrics-based performance tracking, proactive internal communication, and thorough knowledge transfer. Careful planning, monitoring, and reporting ensure that measurable cost savings are achieved, not just low hourly rates. But make sure your partner is credible in their claims for multiregional program management capability.

Skills and technology expertise

Captive ODCs are appropriate for a wide range of development projects, including:
- Custom application development and maintenance
- Enterprise application development and maintenance
- Legacy systems maintenance
- Application and systems testing
- Quality Assurance
- User support and documentation
- Content development for training and eLearning

Skills that are not required regularly, such as database design, UI design, and prerelease testing, can be made available on an as-needed basis. The offshore provider managing your Captive ODC may have specialists available in order to address changing or unusual development requirements.

Flexibility

While designed to accommodate steady and predictable development, a Captive ODC can also bring flexibility to resource staffing. After an initial waiting period, companies can upsize and downsize their ODC development teams to support changing needs, giving them the best value for their investment. Some offshore vendors, such as Lionbridge, also provide a dynamic model allowing “flex” resourcing from day one.
Lionbridge dynamic resource management minimizes cost for clients. In this graphic, we demonstrate how a Lionbridge Captive ODC offers dedicated resources with flexible capacity for optimal blended rates.

Benefits of Captive ODC for Enterprise IT

**Cost savings**

As greater numbers of internal business systems are developed and maintained offshore — at significantly lower cost — enterprise IT departments are able to turn their focus to new, more strategic initiatives. Captive ODC also makes IT budgets more predictable.

**Greater efficiency**

Unlike traditional outsourcing, where changes in project scope mean budget renegotiations and temporary work stoppages, Captive ODC is a more efficient process. The Captive ODC budget is streamlined and easily monitored, accommodating project changes without administrative haggling.

**Exposure to new skills and industry best practices**

Many midsize businesses have had difficulty reaching industry best practices. Working with a Captive ODC can give IT organizations access to technology and development methodologies that otherwise would be too complex or too expensive to put in place.

**Effective knowledge transition and process migration**

Captive ODCs with CMM Level 5 ratings (like Lionbridge India) offer mature processes for knowledge transfer and process migration. Seasoned program managers — with strong experience managing complex programs across languages, cultures, and time zones — ensure the lines of communication are well established and that reporting methods are tailored to customer requirements.
Project governance and SLAs

Captive ODCs built within or in tandem with established infrastructure are born from day one with mature processes, trained personnel, and a refined project governance model. Likewise, well-defined SLAs ensure that performance targets are met and that application managers (and CIOs) are kept abreast of progress in all areas.

Conclusions

Companies with programmatic application development and maintenance requirements should consider the Captive ODC model. Unlike Tactical Outsourcing, a Captive ODC is a long-term, exclusive relationship that provides a ready team of offshore developers for ongoing program execution — a relationship managed by experts who understand the local culture and can deliver the most value to your organization.

Captive ODCs built within an established infrastructure further optimizes the model:

- Fully operable physical and network infrastructures from day one.
- Easy access to “flex” resources for special skills and variable workload requirements.
- Process maturity already in place, granting immediate process maturity for software development, knowledge transfer, project governance, Quality Assurance, and other industry best practices.

In contrast to Build-Operate-Transfer, Do-It-Yourself ODC, or M&A strategies, Captive ODC retains long-term flexibility as market cycles, corporate development goals, and macro-economic conditions continue to evolve. Captive ODC offers a safe and effective means of remaining competitive in the global marketplace.

Additional resources

To learn more about application outsourcing and offshore transition, visit the Lionbridge Knowledge Center: www.lionbridge.com/kc

To speak with a Lionbridge specialist, call +1 781-434-6111 or email info@lionbridge.com.