

Outsourcing IT in the Global World: Choosing an Offshore Destination

*Babita Gupta, School of Business, California State University Monterey Bay, 100 Campus Center, Seaside, CA 93955, 831.582.4186, bgupta@csumb.edu
Sasi Bhushan Sivadasan, IT Support Manager, Capital Insurance Group, 2300 Garden Road, Monterey, CA 93940, ssivadasan@ciginsurance.com*

ABSTRACT

Outsourcing information technology functions has many challenges. These key challenges includes political, geographic, legal, security and privacy and organizational issues. This study develops a model for choosing a destination for offshore outsourcing of IT functions and tests it by surveying participants who are middle or senior level managers in organizations. Statistical analysis indicates that in choosing an offshore IT destination country, top management support and involvement is one of the key factors for successful offshore outsourcing outcome.

Introduction

Outsourcing information technology (IT) functions have become an increasingly accepted cost-reducing strategy and a method of increasing company's productivity. IT outsourcing refers to the practice of handing off software development, call center operations, data center management and other IT support function to an external agency. Size of global outsourcing market is estimated to be about US\$479 billion by 2016, increasing from US\$370 billion in 2012¹ with worldwide business process outsourcing (BPO) services market expected to grow from US\$147.2 billion in 2010 to US\$191.02 billion in 2015². However, there are many challenges and risks associated with IT outsourcing. Companies need to understand these challenges and barriers before choosing a country for outsourcing destination to avoid risks. These key challenges include political, geographical and legal issues such as security and privacy safeguards in destination country. This research develops a model to study the challenges and barriers that companies face during offshore IT outsourcing and empirically tests it.

Literature review

The most common definition of IT outsourcing includes turning over a firm's computer operations, network operations, software development and maintenance, or other IT functions to a provider for a specified time, generally at least for few years (Ezigbo, 2012; Lacity, Willcocks and Khan, 2011; Haried & Ramamurthy, 2010; Pfannenstein & Tsai, 2004). Offshoring is a term often used in the United States to specifically refer to outsourcing to another country, most often today to India, Ireland, the Philippines, China, and other countries (Pfannenstein & Tsai, 2004). Business globalization and the advances in IT and communications technology have led to a growing trend for businesses within the financial services sector to outsource abroad (Ball, 2005). Main motivation behind IT outsourcing decisions is the opportunity to save significant amount of time and money and to refocus on their core competencies. In spite of concerns about decreased control and security and privacy, more and more companies today are moving toward

¹ <http://www.doz.ae/press/7-news/111-value-of-global-outsourcing-market-expected-to-touch-us479-billion-by-2016>

² http://www1.cimaglobal.com/Documents/events/BB_MDeC_June2012_idcreport.pdf

outsourcing to save time and money (Ezigbo, 2012; Dev, Kholekile & Wang, 2011; Dirk-Jan & Vincent, 2010; Hormozi, Hosteller & Middleton, 2003).

Most of the literature gives cost reduction and focusing on strategic goals as the main reasons affecting the outsourcing decisions (Fakhraddinmaroofi and Jalali, 2012; Gantman, 2011; Gonzalez, Gasco & Llopis, 2010; Lacity, Khan and Willcocks, 2009; McKeen, Smith, Joglkar, & Balasubramanian, 2002). Companies need to comprehend some of the major issues such as compliance risks, potential legal and financial problems that can arise due to lack of data security, privacy, intellectual property rights and executive accountability (Peslak, 2012; Lacity, Khan and Willcocks, 2009; Ramanujan & Jane, 2006). Particular societies tend to have distinct ways of working, and this can be problematic when attempting cross-border collaboration (Krishna, Sahay & Walsham, 2004).

Research hypothesis and model

This research focuses on the challenges of IT outsourcing from an organizational and national perspective. Based on literature, five key constructs were identified that would affect an offshore IT outsourcing decision and a research model was developed (see figure 1).



Figure 1: Model for choosing an offshore outsourcing destination

These key constructs or factors are: political, geographical, legal, organizational, and security & privacy. For each construct, main indicators were developed. A survey was then designed to determine the significance of each factor on choosing offshore IT outsourcing country. Survey questions for each indicator in each construct were created and measured using Likert scale.

Research methodology

Secondary research of current IT outsourcing literature was used for understanding basic concepts of outsourcing, challenges of offshoring and current outsourcing trends.

Empirical data was collected by surveying managers from different companies engaged in or considering offshore IT outsourcing. Unit of analysis for this research is the individual manager or project leader from IT or related business units in organizations that are currently outsourcing or planning to outsource IT development functions to offshore vendors. Study was carried out in several phases. In the first phase, a preliminary questionnaire was developed based on the items developed from the expert discussions and literature (Gupta & Iyer 2003; Dhar & Balakrishnan, 2006; Gupta 2007). Survey was approved by Human Subjects Committee.

In the second phase, a pilot test of the survey was conducted with four managers from different organizations. Pilot survey was refined based on the feedback from the pilot test managers. In the third phase, primary data was collected by administering the survey to managers, using both paper and online methods to increase the reach and to maximize response rate within the available resources of time and cost. Survey includes multiple-choice questions using Likert scale. Out of 62 managers from different organizations and industries who were contacted to participate in the survey, 39 responded back with a response rate of 63%. Statistical analysis of the survey data was done using SPSS.

Summary of data analysis

A summary of data analysis is presented here. Approximately 5% of the participants are executive level managers (CEO/CFO/CIO), 48% of the participants are project managers or project leaders, 5% of them have the job title of VP, and 41% of the participants fall under other category such as director, manager-sales, engineering manager, recruitment manager, area manager, senior manager and IT manager. Respondents were asked to indicate the IT offshore outsourcing activities they were planning or were already involved in - 80% indicated IT development, 46% chose call centers, 43% indicated business functions such as HR and 30% chose database/data warehouse activities. Analysis of countries (rank ordered) as IT outsourcing destination indicates that the three top choices are India, China and Brazil. Analysis of rating a company's success with their current IT outsourcing indicates that 10% rate it as excellent, 49% rate good while 41% rate as satisfactory.

Analysis of results

Survey results show that 63% of the respondents believe quality of government support to their IT industry is an important factor in choosing an offshore IT outsourcing country. Data analysis shows an interesting observation on the cross tabulation of revenue and the importance of government support to IT industry. Only 25% the companies with revenues greater than \$100 million rated the importance of government support to IT industry as very important while 50% of the companies with revenue less than \$500,000 rated it as very important. This suggests that smaller companies are more circumspect of destination country's political structure.

Approximately 63% of the respondents believe intellectual property protection laws are important. A significant observation from the analysis is that top management level respondents placed more importance on intellectual property laws of the destination country than the respondents from lower management levels. A high number of respondents, 71%, believe a country's record of accomplishment in ensuring data security and privacy is an important factor in choosing an offshore IT outsourcing country.

Conclusions and future research implications

Offshore outsourcing is becoming a business mantra to reduce the IT cost and increase productivity. Results from the empirical analysis in this study provide an understanding of the key factors involved in choosing an offshore IT outsourcing country. Statistical analysis indicates that in choosing an offshore IT destination country, top management support and involvement is one of the key factors for successful offshore outsourcing outcome. Quality of government support to IT industry, a stable government structure and trust in government are important factors in attracting the outsourcing projects from US companies. Ability of a destination country to ensure data security and privacy also play a significant role in choosing an offshore IT outsourcing country. Finally, geographic proximity of destination country to USA is not a significant factor. Results from this study could help businesses considering offshore IT outsourcing understand key issues and critical factors for outsourcing success.

This study provides a robust understanding of the challenges organizations face during offshore IT outsourcing decision-making. Main limitation of this study is the relatively small sample size. This study could be replicated in future with bigger sample size to ensure that findings can be generalized. This study could be extended in future to identify and analyze the critical success factors of the top three offshore IT outsourcing countries that are identified in this study.

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