

A GUIDE TO INTERNATIONAL OUTSOURCING

HOW TO ACHIEVE SUCCESS AND AVOID COMMON MISTAKES



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Common Mistakes

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This book is for sale at

<http://leanpub.com/aguidetointernationaloutsourcing>

This version was published on 2013-10-26

ISBN 1492835056



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*This book is dedicated to all our customers (past and present) – it
has been our privilege to work with them.*

Contents

INTRODUCTION	i
History of Outsourcing	iii

INTRODUCTION



According to Greek mythology, Zeus the king of the gods wanted to find a human capable of performing several complex assignments. However, it seems that no human was capable of rising to the task. It was out of the question, of course, for gods to intervene in affairs on earth. So, Zeus came down to earth pretending to be the husband of Alcmena, the beautiful daughter of Electryon and the wife of Amphytrion. Zeus mated with Alcmena who, in turn, conceived Hercules. Apparently it was all right for Zeus to get involved personally in this type of affair.

Hercules grew very strong and powerful. However, he was hated by Hera, the wife of Zeus, who drove Hercules to perform terrible acts. At last repentant of what he had done, Hercules

became subservient to King Eurystheus, who he despised. King Eurystheus sent Hercules out on 10 assignments or exploits to atone for his actions. Hercules passed all ten of these exploits but King Eurystheus added two more because he considered one of the original ten to be performed in a somewhat unsatisfactory manner. Hercules completed the last two with success. The gods were happy with his overall performance and when he died he was granted immortality for his great works. In a way, this is an excellent example of outsourcing and how it works.

We use the term “outsourcing” to indicate that a business activity like manufacturing, product development, technical support or other corporate functions has been contracted out to another organization in geographic areas with less expensive labor. Usually outsourcing implies the placement of projects or production that occurs in another country. We will refer to a customer or a client as a company that contracts out its projects. Organizations that are commissioned by the customer that performs projects will be called a vendor or outsourcer.

Another term is “nearsourcing.” This is used when projects are contracted out to be performed less expensively in certain areas of the same country or in neighboring countries with common borders. An example of this would be a USA company contracting out work to a company in Mexico so that the work could be done less expensively.

Sometimes a vendor contracts out a project or a part of a project that it received from a customer to a third party. If the third party is located in the same country where the project originated (the customer’s country) then such a case is called “backsourcing.” For example, a difficult part of a project may be “backsources” by a vendor because the latter lacks expertise in a certain field.

History of Outsourcing

Outsourcing is a wide-spread economic phenomenon. It emerged in its modern form relatively recently when in the 1960s General Motors built a car manufacturing plant in Mexico. Why so late? The reason is that in order for outsourcing to be successful several very important conditions must exist.

First, it is essential for the emergence of outsourcing that industrially advanced countries reach a certain development level, since a company must have some technological advantage to justify moving its business activity to other geographical regions. In other words, there must be something to be outsourced. For example, from a historical perspective it is clear that Europe did not always have as technologically advanced state as certain other countries like China. In the middle of the 13th century, the Venetian merchant Marco Polo was engaged in industrial espionage in China. But, now things are different.

Second, there must be a sufficient gap in labor costs between countries or geographical locations for the outsourcing to be worth utilizing.

Third, developing countries must also achieve a certain level of professionalism; skilled personnel should be available, decent infrastructure should be in place, and reasonable security – both physical and intellectual (in order to prevent theft of intellectual property) should be implemented.

Fourth, it is necessary for the emergence of outsourcing to have a developed communications system, because without an effective operational link, remote management becomes unrealistic. By the mid-20th century a better developed telephone system emerged, airlines started to use jets for regular scheduled flights, and container shipping became a very cost effective way to transport goods. All of these advances have made it possible to move production or research to other countries.

Fifth, the political situation in the world should be relatively stable. Travel for business clients or freight shipping to another

country must be safely accomplished. Look at the history of the early 20th century. Safety was out of the question for much of the period. World War I was followed by the Great Depression, much turmoil in Europe and in many other parts of the world and then World War II ensued. It was only sometime after World War II that all of the above mentioned conditions for outsourcing came to exist.

In 1960, for the first time in world history, General Motors established a precedent of outsourcing by assembling Chevrolet products in Mexico. Due to the differences in labor costs, the company profited. Following General Motors, other car manufactures erected assembly plants outside of the United States, but later returned because car assemblage became very much automated. Fewer workers were needed and the benefit of the wage difference diminished.

The next step in the development of outsourcing occurred in 1983, when an Indian company, Infosys, received a contract for the development of software from an American customer. Infosys had been created two years earlier, and this was its first experience in outsourcing. Infosys now thrives with approximately one hundred and thirty thousand employees.

In the 1980s some more outsourcing contracts were arranged, but these were still isolated cases. Explosive outsourcing growth occurred in the 1990s. This happened for two reasons: the invention of the Internet (and hence the possibility of rapid exchange of information by e-mail) and the decreased cost of telephone calls.

Outsourcing companies specializing in software development are for the most part located in India, where the prerequisites for such development are favorable. For example, among the developing countries, India is a political ally of the United States and Europe. Since India is a former British colony, there is a good system of education and a lot of English-speakers. Finally, India is a very large country, and it offers a lot of skilled personnel in the labor market.

China has established itself as a traditional place of industrial production, but it is less popular for software outsourcing. In many

instances, Chinese companies take orders for software development and pass them on to outsourcing providers in India or Russia.

A number of outsourcing companies exist in Russia (however, there are relatively few) and in Eastern Europe (Belarus, Ukraine, Poland, Czech Republic). Other outsourcing locations include Hungary and Armenia in Europe and the Philippines, Thailand, Taiwan and Bangladesh in Southeast Asia.