

# Offshore Consulting: Benchmarking Future Success

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# Executive summary

Outsourcing services and knowledge work to low-cost economies – what we term offshoring – isn't new, but is it here to stay? And is offshoring a wave about to break, or a bubble about to burst?

If the last five years have taught the consulting and IT services industries anything, it's the sheer unpredictability of market trends. Yet despite uncertainty, despite the accepted difficulties of integrating consulting and IT services firms, there's much talk of acquisition. Onshore firms are looking to meet clients' price expectations by building up their own offshore delivery arms; offshore firms are looking to build direct relationships with their clients by fielding onshore account managers and consultants.

In fact, the questions raised by offshoring go far beyond simple onshore/offshore distinctions. What's at stake here is how a consulting or IT services firm can create the optimal and sustainable balance of high-cost selling and relationship management (onshore) to low-cost delivery and resources (offshore). Future success will be determined by a firm's resilience – the extent to which its resources can be adapted to radically different scenarios.

The purpose of this report is to:

- explore the factors that will affect the balance of onshore/offshore resources in IT services and consulting firms
- analyse the critical uncertainties driving those factors
- construct contrasting scenarios of the way in which offshoring may change both the supply and demand side of the IT services/consulting industry in the future
- assess what kinds of firms will be the winners and losers in each of these scenarios.

Five factors will determine a supplier's balance high-cost, onshore to low-cost offshore resources:

1. supplier's desired level of direct access to clients;
2. clients' fluid definition of what services fall within the scope of "offshore-able";
3. clients' perception of risk;
4. public/private sector split of a supplier's client base;
5. pressure on a supplier's margins.

There are two key uncertainties here:

1. How likely is it that clients will be prepared to sacrifice face-to-face contact with their suppliers in order to save costs?
2. How risky will offshoring be perceived to be?

These two variables are used as the basis for four scenarios of the future impact of offshoring.

1. *Scenario #1: Constant confrontation* – While the market for offshoring has grown significantly and now extends to medium as well as large scale organizations, trust has not. Reinforced by constant haggling over price, client-supplier relationships are at an all time low. Clients have established their own procurement departments, staffed by outsourcing and offshoring experts who cultivate a confrontational style. Larger offshore suppliers have responded in kind, recruiting (or acquiring) their own class of aggressive, onshore account managers.
2. *Scenario #2: Profitable distrust* – Continuing concerns over the political and social stability of low-cost economies means that offshoring is seen as a high-risk strategy. Larger companies, still attracted by the cost differentials, manage the risk by relying heavily on the advice of independent intermediaries. The importance of independence also means that those onshore suppliers which combined offering advice and brokering deals with their own offshore facilities have had to choose between the two.
3. *Scenario #3: Onshore returns* – A gradual upturn in the world economy post-2003 puts a break on the seemingly inexorable expansion of offshoring. Clients turn increasingly to their more familiar, onshore suppliers to explore revenue-generating ideas: demand for outsourcing and offshoring has plateaued, while demand for traditional management consulting is growing.
4. *Scenario #4: Offshore rules* – A succession of stories in the press, highlighting the proven advantages of offshoring, together with continuing budgetary pressure on clients, result in an explosion of the offshoring market. Offshore suppliers have grown rapidly. Increased access to clients has meant that many of the larger firms have succeeded in their aspirations to move up the value chain. Mounting revenues have allowed them to expand their onshore resource base without compromising their economic advantage. Some have acquired onshore suppliers to boost their immediate presence in local markets. Most have abandoned any pretence of working through third-party, onshore partners.

Firms which perform well under one scenario may not necessarily do so under others. Thus, the main beneficiaries of Scenario #1 are either large-scale onshore firms (Deloitte, Covansys, CSC and CGEY) with a sizeable offshore presence which they're in the process of growing rapidly, or large-scale offshore firms (Infosys, Wipro and Satyam) already building onshore account managers and consulting teams.

Onshore management consulting firms are also likely to perform well in Scenario #3. As clients' attention swings back to consider revenue generating ideas, instead of the cost-cutting strategies they have

pursued since 2001, they're more likely to turn to the onshore players they've historically used in this capacity (Booz Allen Hamilton, Deloitte, CGEY).

Intermediary firms (DiamondCluster, NeoIT, TPI) are likely to perform best in Scenario #2. Among this segment of the industry, those prepared to take a hands-on role fare better than those staking out the purely advisory role.

Access to offshore resources will be a critical determinant of success in Scenario #4. Not surprisingly, therefore, it's the likes of Infosys and Wipro which stand to do best out of it. Outside this segment, performance is likely to be patchy.

Of the 26 firms profiled in this report, Infosy, TPI and Wipro appear most likely to be able to withstand the potential threats of offshoring and/or exploit its possible opportunities across all four scenarios.

Of the firms that still score well, though not as well as the top three, some (like Fujitsu Consulting) perform reasonably consistently irrespective of the scenario. Others (Covansys, DiamondCluster, NeoIT) perform more variably, doing very well under some circumstances and very badly under others.

Looking at firms' relative positions overall, it appears that the consulting, outsourcing and IT services industries stand to gain, rather than lose, from offshoring. For many firms, however, success lies on a knife edge.

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