

# Offshore Software Development: The Philippines

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## 1.1 Introduction

Offshore development is a buzzword in present IT industry. As Thomas L. Friedman says in his latest book **“The World is Flat”** : *A Brief History of the Twentieth Century*. The book talks about ten flatteners of the world. In one of the flattening point he talks about “outsourcing” and “offshoring”, which is a new form of collaboration. Today, in the world of globalization, outsourcing is not only helping countries go global but companies as well individuals go global. This convergence is helping people and companies work together irrespective of society, culture, geography and even language.

There is no doubt that the reasons companies go for offshore development is because of cost and time effectiveness. Moreover, one of the prime reason why there is so much outsourcing work in India and China today is not because they are just smarter and efficient than other countries, but because of the economy and availability. It's no more only China and India where the countries like US and Japan is looking for outsourcing work but there are countries like Philippines, Vietnam, Malaysia, Russia, etc who are also participating in this competition. Particularly, Philippines have been in focus of outsourcing since long period especially, in the field of manufacturing, accounting, finance, BPO, call center, etc. It's only now the country has been noticed in offshore software development and estimated to stand just after India in development work. As the cost of Indian programmers and developers are increasing day by day so the companies are no more showing interest in outsourcing, rather look for service providers and developers in countries like Philippines and Vietnam.

It has been proved that because of the close affinity with US there has been always a good relationship with Philippines. Every year there is a substantial amount of outsourced work from US to Philippines. Now, it has been recognized that the Filipino developers and programmers are no worse than Indian ones. So, lot of mid-size US companies are looking for their software development work in Philippines. Among, the development work specific sectors are application development, custom development, migration of application, application maintenance, mobile application development, etc.

## **1.2 Offshore Software Development: Meaning of it and why do it?**

Offshore development in the IT world is the term most often used to describe the business of outsourcing software programming and engineering services beyond national boundaries. The three most common justifications for offshore development are cost reduction, internationalization and inadequate supplies of domestic resources.

Cost reduction is the traditional reason for offshore development. Low-level tasks such as coding and software testing can be performed in less-developed countries for as low as ten percent of what it costs at the domestic front.

Software manufacturers seeking international markets and needing to localize their products to specific platforms, languages and cultural requirements often find it more efficient to use offshore development resources in or near their target markets. Ireland, Philippines, China, Malaysia, Russia, Ukraine and Scandinavia are some of the countries which are best suited for this type of outsourcing today. Cost savings from these more developed countries remain available, but are less dramatic now.

The growing shortage of IT professionals, especially in the most developed countries, is rapidly becoming the most important reason for offshore development. For instance, the U.S. Department of Commerce reports a shortage of 1.4 million computer programmers in the United States alone.

In the case of software development, "outsourcing" or "offshore" development often brings the best results by providing high quality software solutions at an inexpensive price. The following reasons influence companies, including some in the Fortune 500, to engage in offshore development:

- Constant shortage of world-class software professionals;
- Pressure to cut costs during recession;
- Need to update IT skills and tools constantly.

❖ **Benefits of offshore software outsourcing:**

- Substantial reduction in total project costs;
- Flexibility resulting from the ability to attract resources for large projects quickly
- Compression of project development and implementation time
- Access to a resource pool of highly skilled and experienced IT professionals
- World-class quality of developments

## 1.2 Offshore Development Delivery Models

There are several different delivery models existing today in the field of software development. These can be categorized as variations of outsourcing or 3rd party models, wholly owned subsidiary models and body shopping. Further categories are defined within this section.

### I. Onsite Team

Onsite needs only project coordination

- Well-suited for cases where:
  - There is reduced customer interaction
  - There is reduced knowledge transfer from customer
  - The scope is well defined
  - The processes and policies are well defined

### Offshore Team

- Detailed design, Code and Unit Test
- Integration Test
- Well-suited for cases where:
  - There is ongoing interaction with customer
  - A changing business environment is prevalent
  - A new technology is used

### Onsite and Offshore with lead team onsite

- Lead Team at Onsite
- Project Management Lead
- Knowledge Transfer Lead
- Quality Assurance Lead

### Onsite and Offshore with lead team offshore

- Lead Team at Offshore
  - Project Management Lead
  - Knowledge Transfer Lead
  - Quality Assurance Lead

### II. Onsite and then Offshore

**Lead Team arrives from offshore**

- Knowledge transfer
- Procedure setup

**Lead Team returns offshore**

- Setup environment
- Performs knowledge transfer
- Functions as knowledge expert
- Well-suited for cases where :
  - The initial learning curve is high
  - The nature of work is repetitive

**Onsite, Offshore and then Onsite**

- Lead Team arrives from offshore
- Lead Team returns offshore
- Lead Team arrive onsite again
- Implementation
- Knowledge Transfer
- Well-suited where:
  - Knowledge transfer is needed from offshore
  - The customer needs support for implementation

**III. Fully Offshore - Full team is at offshore**

- Well-suited for :
  - Customers with very well-defined work units procedures and policies that are well defined
  - Communication-intensive cases

**IV. Full team is offshore under customer management**

- Well-suited for :
  - Creating virtual organizations
  - Delivery, that depends on multiple customer points of contact
  - Cases where work forecast horizons are limited

**V. Fully Onsite - Full team is onsite**

- Well-suited for :
  - Staff augmentation at customer locations
  - Consulting
  - Onsite studies

- Offshore engagement planning projects
- Short term engagements

### **1.3 Offshore Software Development Global Landscape**

In the current scenario India and China are not the only destinations gaining in strength for IT services. Developers and programmers are now spreading around the globe. More and more countries are taking initiatives for the Information Technology services and solutions. More and more destinations are showing interest in becoming another India or China for IT services. This is the main reason why Offshore Software Development is spreading globally.

India, the destination of IT services, has gained lots of popularity because of its talents and especially for lower labor cost for overseas development services. But now, the rising pay scale may dull India's IT outsourcing industry. Country's IT services is getting more and more expensive day by day.

The demands and expectations of the employees are also increasing with their increasing demand in the market. In spite, of the fact that with an anticipated rise of around 28% in the financial year 2005-06, scorching rise carry on to be the trend this year also. Till date, country has the monopoly in the IT industry as far as IT Outsourcing is concerned. Along with Offshore Software Development country is also demanded for BPO services. A number of overseas giants have already established their presence in India for such IT services.

But now the time has come to think about the rising salary of the Indian employees. The foreign countries chose India as they found the lower labor rate in the country. But the recent survey by NASSCOM suggests that the average pay scale of the employees has increased between 16 and 18%. The increasing pay scale is making these companies search for alternate overseas destinations in Asia especially China, Philippines, Vietnam and Malaysia.

### **1.4 Focus on Offshore Software Development**

Both the countries like Ireland and India enjoys the advantages of offshore development tremendously. The reason is firstly Irish universities produce IT professionals to allow Irish offshore development business to grow. The close links between the universities and hardware/software platform manufacturers ensure that graduates are well prepared to begin working when they complete their studies. As a result, today, there are some 550 Irish offshore development companies, 80% of which are Irish owned. Moreover, Irish Government policies strongly support these developments.

Secondly, India also shares most of the same advantages, but with significantly lower wage rates. The Indian government is aggressively helping to develop the offshore development sector, which now accounts










for more than 10% of the value of all Indian exports. The Indian National Association of Software and Service Companies (NASSCOM) is one of the strongest industry groups in the World. India has an excellent university support system that works closely with leading hardware and software manufactures. During the year, the number of quality certified software companies from India increased to over 170; Fifteen (15) Indian companies now have the unique distinction of a SEI-CMM Level 5 certification. (Only 23 companies worldwide have achieved level 5 Certification).

Within the last few years other countries have also emerged as locations for offshore software development. The countries of the former Soviet Union and Eastern Europe, China and Philippines fall in this category. The current wage rates and sound educational set ups in these countries put them at similar levels to India.

In terms of offshore software development, Russia is truly a “diamond in the rough,” offering exceptional un-mined promise. Unlike most countries, Russia’s resources are ample. The education level of available talent is extraordinary on a global scale, and its software development capabilities are arguably unmatched. Today, Russia Offshore Software Development represents an attractive device with which to mitigate the risk posed by global instability. The business climate in Russia has never been more favorable for establishing strong, mutually beneficial relationships. For enterprises, in search of uncommon levers to comparative advantage, Russia warrants critical consideration as an Offshore Software Development resource.

Russia is frequently mentioned as a rapidly emerging offshore destination for software development. The size of the Russian offshore software development industry market is currently estimated to have grown to between \$130 million and \$200 million. Estimates for growth through 2010 vary widely from \$1 billion to \$6 billion and that in the same period the IT sector will account for 2 percent of Russia’s total economic output (compared with the current level of 0.61%).

A survey shows the current outsourcing IT works to the following countries:

<b>India</b>	<b>38%</b>	
<b>China</b>	<b>6%</b>	
<b>Mexico</b>	<b>5%</b>	
<b>Ireland</b>	<b>5%</b>	
<b>Canada</b>	<b>5%</b>	
<b>Malaysia</b>	<b>4%</b>	
<b>Philippines</b>	<b>4%</b>	
<b>Russia</b>	<b>4%</b>	
<b>Singapore</b>	<b>4%</b>	

## 1.5 Offshore Software Development in Philippines

### ❖ Status

The Philippines is one of the South East Asia Pacific countries and has a culture very close to United States. It has a population of 85,236,913 million (2005 projection) with a literacy rate of 94.6% and a growing IT literacy rate of approximately 7% every year. Since a decade, there has been an increase of more than 20,000 Mathematics and information Technology (MIT) graduates in Philippines every year.

The Philippines, one of the largest offshore destinations for business process outsourcing (BPO), is home to a \$350 million offshore outsource software services sector. The primary focus of the Philippines software development firms is on systems and application development and maintenance of legacy applications. Its strength lies in cultural affinity with the US. The Philippines, with its highly westernized culture (a US protectorate for nearly 50 years), and third largest English speaking population makes it an excellent destination for cheap transition, low-level maintenance work to an offshore location. Another aspect that favors the Philippines as an offshore outsource services location is that it is seen as a safety valve against possible service disruptions due to political tensions in larger locations such as India or Russia.

The downside for the Philippines software services sector is that it lacks the size and scale of its primary competitor, the Indian software industry. The main problem for the industry is that the Philippines need more software development companies. Currently, there are only about 30 software companies focusing on software development for the offshore market. This compares unfavorably to the almost 800 software companies currently focusing on the software services sector in India. Also, none of the Philippine software companies possesses major certification such as Carnegie Mellon Universities Capability Maturity Model (CMM) certification, while most of the major Indian firms are CMM-I certified at level 5.

Another major issue that faces the software services sector in Philippines is the political instability. The nation has been hit with a guerilla insurgency which gives a pause to foreign corporations when choosing a partner in their offshore software development site. Although, India, Russia and China also have their share of political turmoil, their size and stature make them a much easier choice.

Owing to the above reason, currently the only solution for the Philippines is to continue offering low-cost, dependable solutions for multi-national corporations (MNC's) BPO needs. This will allow the nation to pick up more business to scale up the industry and allow foreign corporations to overlook any political or security issues.

#### ❖ **Government Support**

After witnessing the success of the Indian software services sector the Philippine government has started promoting itself as a viable offshore outsourcing hub. To increase visibility of the software services sector, the government formed the Information Technology and E-Commerce Council (ITECC), an interagency government and private body which advises the Philippine government on IT and e-commerce policies and projects. The focus of the government's information and communications technology (ICT) policy is on five areas:

- Enhancing the Philippines information infrastructure
- Providing a regulatory environment conducive to growth
- Promoting services such as call centers, BPO, software development, data transcription; and
- Developing IT parks and zones.

Further, the Philippine government encourages growth in the ICT sector through favorable tax and regulatory policies designed to encourage investment in the country.

#### ❖ **Industry Association Support**

Outsource Philippines is an organization which acts as a information gateway to the Philippines major ICT activities of BPO, call centers, transcription services, software development and maintenance. This organization purports to fulfill the same capacity as India's NASSCOM, which is to provide potential outsourcing clients with industry sector and company information. This organization also promotes certification within the Philippines ICT industry to improve the overall level of service that the associations' members provide to clients. Finally, the organization acts to promote the Philippines IT services sector by lobbying the Philippines companies on the domestic as well as foreign fronts.

Almost all of the Philippines offshore software services firms are located in one area, the National Capital Region (Metro Manila). There is very little economic development, and almost no software services firms outside of the Metro Manila region, especially in the Southern Philippine islands. The reasons for the concentration of software services firms in the metro manila region is much due to the availability of human capital (especially educated IT professionals), the infrastructure especially telecommunications infrastructure), and other collaterals in this area.

### ❖ Cultural Integration

The Philippines is a country closest to United States in terms of culture, legal and political systems. Out of every extended Filipino family some one is living and working in US. The fact is very much reflected in their society, fashion, food and lifestyle. Even the malls and the cinemas are full of US brands and movies.

It has been also proven in the call center industry that Filipinos are the easiest to train and adopt to US accent and lifestyle compared to several other locations in Asia and Europe. The education system and course outline is closely aligned with the US system. Having such a closer cultural link helps reduce some of the problems that result from teams with differing cultural backgrounds.

Moreover, the Filipino people are always warm, friendly and hospitable to visitors. This personality has helped them to be highly successful in the call center industry. Filipinos have developed a reputation in the call-center industry as being highly caring, quick to master an American accent, and speaking empathetically when answering a customer complaint.

### ❖ Availability of resources

The Philippines have a substantial reserve of software development resources waiting to be tapped. Its institutes of higher learning and universities continue to produce thousands of graduates in IT, IT-related or engineering fields. Notwithstanding, a continuous brain drain, these specialists are still growing in number. One of the main benefits of tapping into Philippines offshore development capabilities is the relatively low labor cost when compared to similar specialists in other markets specially India.

Worldwide, as the demand for programmers has continued to grow faster than the available supply of qualified specialist, companies have been looking for new sources of labor to fill the gap. It is estimated that approximately 52,110 (in the year 2002-2003) professional were employed in IT software industry in Philippines and with the growing demand this number will show up more in the coming years.

The Philippines takes pride in its high-performing IT professionals with an excellent industry track record. Philippine IT professionals are recognized worldwide for their credibility and expertise, in the fields of advertising, banking, communication, defense, education, finance, government, health, insurance, manufacturing, mining, public utility, realty, science and research, shipping stocks, and trading. Manila is recognized as a major outsourcing center for companies in the US, Japan, and Europe.

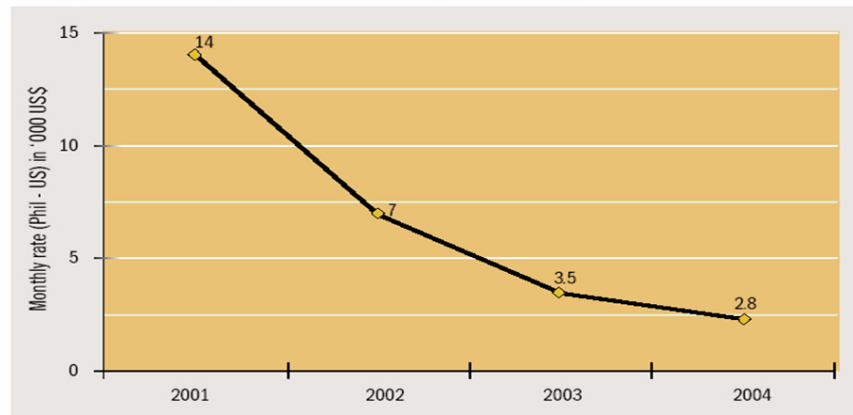
## ❖ Infrastructure Availability in Philippines

### ➤ Bandwidth :

Dial-up connection (maximum 56 Kbps) is still the most common mode of accessing the Internet, although the Philippines has both fixed and wireless broadband capabilities (via cable, DSL and satellite)

The graph shows the Bandwidth usage in Philippines from year 2001-2004:

**Philippine E-1-2 Mbps Bandwidth Rates (2001-2004)**



Source: Knowledge Institute analysis

### Cost of Dial-up

- Internet access is between \$0.30 and \$0.40 per hour. A 2001 survey of Philippine Internet users showed that 63 percent of respondents still accessed the Internet via a dial-up connection.
- They spent an average \$15.50 per month for Internet access. This is around 2-3 percent of the monthly wage of the average Internet user.
- Cable and DSL connections for home use cost \$50 per month on the average. Service, however, is limited to mostly urban areas.
- The ICT industry is one of the fastest-growing industries in the Philippines, with foreign currency earnings exceeding those of any other industry.
- It is also ranked second to India as the largest producer of computer services in Asia. A number of global companies are outsourcing their ICT and ICT-enabled business processes to the Philippines.
- In the Global New e-Economy Index released in 2001 by the Meta Group, the Filipino workforce is ranked fourth worldwide in terms of ICT competencies

➤ **Philippines Internet Demographics :**

Currently, it has been estimated to have approximately 7 million Filipino Internet Users (FIU) and around 191 Internet Service Providers (ISPs), 1500 Internet cafes in Philippines. We define an Internet user as someone who has access to the Internet through its own PC, corporate facility, schools, and Internet cafes, among others. The FIU is different from its Western and Asian counterparts. The FIU is not necessarily a PC owner and it will be more and more to be that way as its Internet user population increases.

Around 60% of home Internet users access the Internet from their homes. 40% use prepaid Internet cards to access the Internet. The prepaid Internet market is bigger and we currently estimate this to be worth 818 million pesos. The Internet cafe has provided the means for the FIU to be connected to the New Economy. It has served as a powerful tool in bridging the digital divide. Surprisingly, the FIU in the countryside are more tech-savvy and comes from across all classes of the Philippine society. This is brought about by cheap Internet cafe access in the provinces ranging from 10 pesos to 35 pesos an hour unlike in Manila where Internet cafe prices are from 30 to 150 per hour.

With the greater availability of online facilities from Internet cafes, cheaper dial up subscriptions, DSL, broadband, broadcast, satellite, cable, it is forecasted that the number of Internet users will increase with at least 1 million every year.

➤ **PC Penetration and Internet access :**

- PC penetration is estimated at 1.9 for every 100 persons.
- Internet penetration is at 6 for every 100 persons (or 4.5 million of the total 76.5 million Filipinos).
- Of these Internet users, 3.1 million (about 70 percent) are said to access the Internet using prepaid cards at Internet cafés.
- Two recent ACNielsen reports give a deeper insight on Philippine Internet users (3) Its "Activate" survey show that the majority of Filipinos between 13 and 30 years old access the Internet daily for at least an hour after work or school (and usually before bedtime).
- The other survey, NETScan, reveals that as of the second quarter of 2002 an estimated 6 percent of the total urban population is using the Internet, almost half of whom are based in Metro Manila (or 11 percent or 900,000 of the population in Metro Manila). Over half of those with Internet access belong to the upper and middle economic classes, although there is substantial representation from "Class D". This means that the upper and middle economic classes account for almost two out of three users.
- There are an estimated 191 ISPs nationwide, mostly operating in urban areas, with 20 percent in areas with export processing zone. There are only about five Tier 1 ISPs. There are also three Internet exchanges, which are all located in Metro Manila.
- The subscriber base to date of these ISPs is approximately 1,850,000.

- It has been noted, "Internet-wise, the Philippines is part of the US Internet at the end of a very long string across the ocean". This observation is based on the fact that "foreign (mostly US) traffic makes up 90 percent of the consumers' consumption" and that "connectivity to other Asia-Pacific countries is a small fraction compared to the US connection."

❖ **Contact Center Industry Booming in Philippines**

Business Process Outsourcing (BPO) continues to be a bright spot in the Philippine economy. Built on the strength of the Philippines' skilled and trainable human resources and the presence of good telecommunications infrastructure, the country has established itself as a competitively priced provider of quality services. BPO includes several sub sectors such as contact centers, software development, transcription services, business services (such as finance, HR, and IT services), and animation. In 2005, the sector is projected to generate close to \$2 billion in revenues, the bulk of which comes from contact centers.

In 2004, contact centers alone generated an estimated \$750 million out of 40,000 seats (or \$18,750 per seat). While the growth from the sector has been fantastic, overall, the Philippines still accounts for only 2.4% of the total global market.

In 2004, the big players in the industry had established a presence in the country. Also noticeable was the presence of more and more India-based players making inroads into the Philippine market (necessary in establishing a multi-country presence and making economical sense). Both countries have their advantages.

The Philippines has certain advantages when it comes to cost of human resources and the cost of telecommunications infrastructure. The Philippine centers do not have the added cost of shuttling their employees to and from their homes, have lower attrition rates (for now), and much lower bandwidth cost. In addition, the Philippine Peso's depreciation (by 4.8%) and the Indian Rupee's appreciation (by 6.45%) against the US Dollar have also affected cost structures.

Today, opportunity exists in the industry and there are still relatively untapped markets for contact centers in the Philippines such as European countries. Mergers, acquisitions, and consolidation are expected to continue (though there will be less and less local targets) as size is an important factor in the industry. Percentage growth will not be the same as in previous years and more contact centers are seen to expand into other non-voice BPO services such as finance, accounting, and human resource services.

## 1.6 Requirements in Offshore Software Development

As an offshore software developer, you should be able to fully explain your workflow. You should have a common process that applies to every project in offshore software development. The process should define how you gather your customers' requirements and specifications, how you develop schedules and prices, how you communicate with your customers, how you develop, test, and document the product, and how you deliver the product to your customers.

To work out this methodology under offshore software development, you must follow the first step of Software Development Life Cycle which is a "Problem Identification and Requirement Specification". Once you identify the actual problem i.e. the aim of the project, you can turn to gather the information. There are different sources through which you can collect and analyze software requirements.

- **Interview:** If the client is available, then conduct an interview through MSN Messenger or Yahoo Messenger or through any Instant Messenger; discuss your problems related to software. Note down the important things for offshore software development. Ask limited questions and try to collect all the relevant information in least time. This is the best technique for analyzing Software requirement in offshore software Development.
- **Questionnaire:** An offshore software developer uses this technique for collecting information. If an interview is not possible. In this process you send a Questionnaire to your client via email, and then collect relevant information. As an offshore software developer your questionnaire must be formatted with again limited questions. All the questions must be meaningful with explanatory format. As an analyst under offshore software development, you can further send the Questionnaire for detailed information as per the requirement.
- By the nature of your specialization, you must bring extensive world- class resources to meet the needs of your customers. Partnering with an organization with world-class capabilities can offer access to new technology, tools and techniques that you may not currently possess therefore you, as an offshore software developer, should always use more structured methodologies, procedures and documentation and should try to create competitive advantage through expanded skills.

### ❖ **What are you looking for?**

You must look forward in achieving the best software solution for your offshore client and you must have a preferred method of doing business with companies for numerous positive reasons. As an offshore software developer, you must think about the following with respect of your client company and you should make sure that your software solution provides for.

- Effective utilization of resources
- Enhancement of corporate financial goals by IT Department
- The compatibility of current resources and new technology
- Quicker and more effective method to handle these issues.
- Find out the consequences for a wrong decision.

❖ **Why do you need to collect the information?**

A project under Offshore Software Development is not deemed complete until you have proper documentation with you. "System Design" is the main phase of Software Development Life Cycle. This phase is the skeleton of your Software and that is why you must request for a layout of the working process. In offshore software development you can request your client to furnish the flow of information in their working area.

This information is needed for proper structuring of your collected data under offshore software development process. If your client has an existing computerized system then you must focus on the drawback or limitation of the previous system. As an offshore software developer, you must study the Software and Hardware specification to improve the performance of the proposed system. You should also study their management strategies for a System Design.

❖ **How do you communicate back what you create?**

As an offshore software developer, you must implement the Software Quality Assurance (QA) process that addresses the quality assurance needs at every phase of the development cycle. Your QA team must focus on quality control checklist. In addition, you must also have a comprehensive Quality Testing Checklist to ensure that every solution delivered measures up to the highest possible international standards.

Testing and implementation is one of the phases of System Development Life Cycle. As an offshore software developer, you must ensure through proper planning, that the project does not move away from its targeted goals. While the customer has a clear definition of the project, knows the project status, and has ready access to project deliverables at any point of time should take every possible action to avoid any calling from the client's side. As an offshore software developer, you must ensure the timely and quality delivery of the following, for 100% client satisfaction:

- Prototypes & Staged Deliveries
- Weekly Status Reports
- Final deliverable

#### ❖ **How do you make sure?**

Under offshore software development process, you must check whether your client has received the reports, prototypes, final deliverable and obtain a receipt of the same. You should receive positive response from your client before progressing further at each level. As an offshore software developer, you must take care about their requirements. If your client is satisfied or impressed by your regular work then you can further improve the quality of deliverables.

The processes are based on the following principles, which are specifically designed to manage offshore outsourcing partnerships.

- Clear definition of roles and responsibilities
- Focus on well defined regular communications
- Minimize Complexity
- Result Oriented
- Give importance to training
- Document everything
- Review everything
- Continuously improve processes through learning
- Finally, define procedure to handle crisis and emergency situations, even if it is a remote possibility

#### ❖ **Communication Methods**

Working with offshore teams does not mean working with unknown entities anymore, thanks to the technologies that enable cheaper e-communication through chat, voice calls, web cam, etc. Clients are encouraged to get in touch with any of our developers through chat or voice over Internet Telephony calls, video conferencing or through other low cost means. This helps the members of teams across the shore to understand each other better. This understanding helps both teams to work towards a single goal in a coordinated way.

In spite of free communication, emphasis is also laid on regular scheduled meetings for reviews, status discussions, change discussions, feedback sessions, etc.

## 1.7 Offshore Development Center

### ❖ What is an ODC?

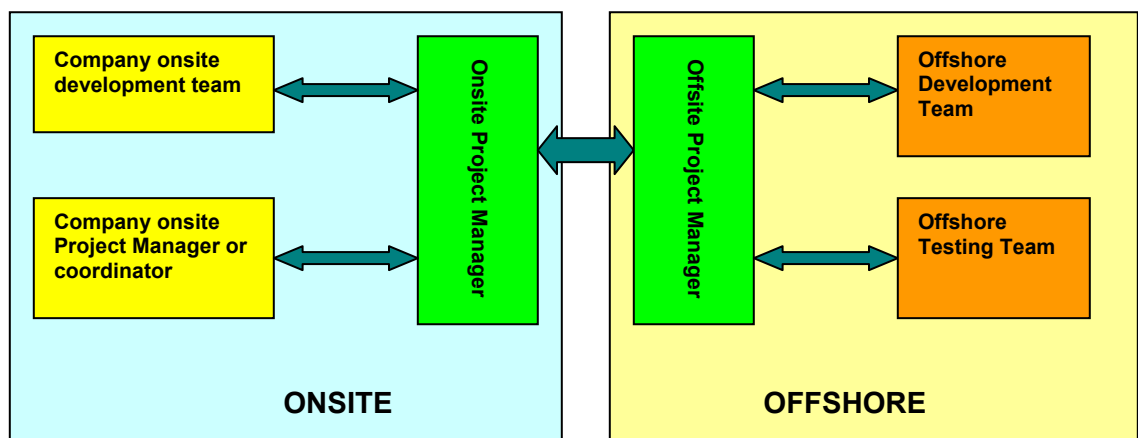
An Offshore Development Center or ODC is a dedicated development center, located outside the client's premises (most often outside the client's country) and is solely engaged in developing, testing and deploying software solutions and applications. The purpose behind an ODC is to take advantages of the technological know-how of the offshore partner, reduce the time to market and save on costs.

### ❖ Establishment of an ODC

The process of setting up of an Offshore Development Center (ODC) is in phases. The initial phase is required to accomplish the infrastructure set up for the ODC – which would include setting up of the Physical Infrastructure such as Office equipment & Development Environment and the assignment of professionals with relevant skill sets to the ODC. This phase takes around 4-6 weeks time. The next phase is very critical to the long term functioning of the ODC. This phase deals with setting up of a functional process, which will be implemented and improved upon through out the life of the ODC. A detailed discussion is held to decide on the process to set up the communication protocol, operational efficiency/reporting structure, specific roles and responsibilities assigned to specific personnel.

### ❖ A typical Offshore Development Center Setup

A typical ODC setup can be diagrammatically represented as below. The diagram below is based on the assumption that the client has a fully functional, though limited development team onsite (located at the client facilities) and the offshore development center works in coordination with this team through the client project Manager.



Listed below are some of the key issues that need to be addressed to ensure that goals of the ODC, which are covered in subsequent sections of the document, are met.

❖ **Key Issues**

- Protection of IP
- Exit Policy
- Security and backup policies
- Ramp up and ramp down
- Risk Management Plan
  - Attrition issues
  - Cultural Integration
  - Transition / Skill Orientation

❖ **Models of Offshore Development Center :**

In this model the offshore partner assists client to setup Offshore Development Center. The partner also helps in the operations of the ODC by providing the resources for development work, managing the ODC, etc. that frees the client from worry of the day-to-day operations of the Offshore Development Center. In case, the client wants to take over the operations and buy out the Offshore Development Center at a later stage, the following options can be adapted:

- Dedicated Offshore Development Center
- Offshore Development Center- Build, Operate, Transfer (BOT Model)

**1. Dedicated Offshore Development Center**

The partner company will set up a dedicated Offshore Development Center for the client. The dedicated offshore development center size is based on the requirements of the client

- The complete office space, infrastructure and resources will be dedicated
- May be housed within the development center

Client can start with a small team initially

- Scale up the team at a later stage
- Development center can be setup in a phased manner
- The client can start operating at development Center

- Can move from development center to dedicated location as they grow.
- Development center will handle the overall Operations and Administration.
- The Client can have their own Project Managers / Technical Managers managing the projects from onsite.

## 2. Offshore Development Center Buy Option (Build – Operate - Transfer)

In the Build Operate and Transfer Model of ODC,

- The Offshore Development Center will be setup according to the requirements of the Client
- Will run on a pre-defined terms and conditions.
- The offshore partner will set up and manage the center for the client for a particular period.
- Based on terms and conditions the control of ODC will be transferred to the client after a period.
- In case, the Client would like to buy the ODC, the purchase value of the ODC would be calculated as being equal to three months billing for the engineers being transferred from the ODC to the client.
- All facilities / infrastructure used by the ODC could also be acquired by the client on payment of the written down value of the facility / infrastructure.
- This model helps clients build up its own facility in offshore countries without having to be exposed to entry-level hassles.

## 1.8 Advantages of Offshore Software Development

Outsourcing has always been there in one form or the other but today, it is the buzzword in the IT industry. Offshore IT development is one of the key strategies that most IT ventures are capitalizing on. Outsourcing is considered one of the most full-proof measures in IT industry to stretch your budget and still get the highest quality. You can get your project done on time and that too conforming to the best technical standards.

Does it really offer a better alternative to in-house development? Let's look at both the sides of the picture:

### ❖ Reasons in favor of Offshore Software Development:

- **Competitive edge:** Outsourcing gives you competitive edge and helps to concentrate on your business and to initiate the project much faster. It provides you enough time and resources to concentrate on your core activities.

- **Hassle free services:** Outsourcing reduces your worry about infrastructure and equipment investments. Instead, it offers state-of-the-art furnished offshore development centers to develop high quality IT solutions.
- **Protection from operational nightmares:** Outsourcing guards you from the operational nightmares and reduces your apprehension to train professionals and retain them.
- **Improves efficiency:** Outsourcing elevates your IT capacity by hiring the best offshore vendors. The technical competence is enhanced by many folds since you are working with the best IT professionals.

Consequently, Outsourcing is the best alternative to get the highest ROI and remain in step with the competition by receiving the highest quality IT solutions. But, when it comes to outsourcing to an overseas vendor, are you confident that it will stretch your budget and not end up with a big hole in your pocket? Let's analyze a few pitfalls of outsourcing, which you need to be cautious.

❖ **Pitfalls in Offshore software Development:**

- **Lower quality than expected:** There is a possibility in outsourcing that you might end up wondering - was that a profitable bargain or not- because you have lost on the quality front in the offshore process. To avoid such mishaps, you need to be cautious while choosing an Offshore Partner. Therefore, to avoid such misfortune, get the sample codes checked by experts, analyze their coding standards, investigate into their bug tracking systems etc.
- **Poor project management:** It has been observed that outsourcing also impedes the quality and turn around time of the project. So, you can have an onsite executive who can regularly monitor the progress and keep a tab on the scheduled time lines.
- **Sub-contracting:** Sub-contracting is another evil in this process as the overseas service provider may exaggerate its skills and finally subcontracts it. Therefore, it is always advisable to cross check the company's profile, its success stories, references given and other credentials.
- **Communication gaps:** This is a typical problem observed in an overseas-outsourced project. Further, language and cultural differences add more to this. To sort this, you need to agree on certain fixed standards of communication which are easy to follow by both the parties.
- **Emphasis on projects:** Offshore Software Partners always place great emphasis on most advantageous projects. In order to avoid getting neglected its better to freeze time schedule and milestones in advance and follow them stringently. It is advised to document the penalty in case the Offshore Software Partner fails to meet the deadlines. Likewise incentives can also be worked out in case of on time completion of a project.
- **Greater transparency and well laid out contract:** Finally, if anything goes wrong in your professional relation with the Offshore Software Partner, you should have well laid out contract that lists everything transparently, to ensure that the loss of time, money and resources are minimized.

❖ **Challenges :**

**Project management** is always a challenge in outsourcing and may involve even much more effort and risk for a company if the project is carried out by another company in a different country. Although, everyone clearly understands the benefits of offshore software outsourcing, many companies hesitate to go offshore because of the following fears:

- Language problems and miscommunication which arises from a lack of common language between the offshore team and the customer;
- Opacity of the developments at the offshore site because of lack of formal and regular communication;
- Insufficient level of control over offshore development team;
- Poor or lack of local acceptance tests that result in supplying poor and defective deliverables to the customer;
- Poor IT management and environment at the offshore site.

### 1.9 **Role of Philippines Software Industry Association (PSIA) in Offshore Development**

The Philippines Software Association (PSIA) was formed in 1988. Its main purpose then was to organize the Philippine software industry and help member organizations achieve their business objectives. Since its inception, it has been involved in several missions to sell the Philippines as the preferred destination for software development services. PSIA is recognized by government and other external parties as the representative of the software industry in the country. PSA (now PSIA) has developed several policies with the government to make Philippines competitive in the software services worldwide. Currently, the country has three main software organizations: the Philippine Software Industry Association, CebuSoft and Association of Solution Integrators in Davao.

As per the discussion of Philippine Software Industry 2010 "flight plan", the Philippines is capable to making a great impression on the international market, showing its decisiveness in becoming an outsourcing location of choice, especially in call centers and business process outsourcing. However, in the software development field, it has been seen that most outsourcers have opted for India more than any other countries, especially for high-end mission critical projects.

According to the knowledge worker the Philippine software industry has been existent in the past three decades with more or less 400 companies. Its 2004 revenue is pegged at \$340 million. With an estimated labor size of 10,000 workers, the estimated revenue per software developer is at \$34,000.

What makes this service sector special is that it represents the age of the knowledge worker. In this age, the most valuable assets are the workers and their productivity. Intellectual capital is supreme as wealth is migrating from money and things to people.

The global market for software is huge. The Philippines already has its foot in the door and have every opportunity to bag projects in this area. For software development companies, software processes certification is becoming a requirement in the selection process, especially in big projects. The International market intelligence on project opportunities and future needs are necessary for development of capacity building programs. Proactive marketing needs to be done, but must be industry-association driven, through resource pooling and publishing of success stories. Having access to incentives, grants, and loans will be critical to sustain the energy and momentum of these efforts.

The private sector must work closely with the Board of Investments and Export Development Council to continuously check-and-balance the sector strategy for growth and supply the necessary data for effective decision-making. Lack of data sharing contributed to slow growth of the sector in the past.

Following are the main targets set by the Philippines Software Industry Association to be completed by 2010:

- To establish Fifty (50) software development companies with international quality standards
- To locate 50 foreign-based software companies in the Philippines
- To enhance the “Brand Philippines”
- To hire 100,000 skilled software professionals
- To increase Intellectual Property compliance for software industry by 3% annually
- To increase government software investment by 10% annually
- To create social and physical infrastructure

## **1.10 Philippines’ Prospect in Offshore Software Development**

### **U.S.A Market**

The Philippines has over 300 software development companies, the biggest segment in the Philippine services industry in terms of players. Although countries like India, China and Southeast Asia still continue to be the most attractive locations for “offshoring” of IT services, Philippines has its own advantages when it comes to outsourcing.

The Philippines is the third largest English speaking nation in the world outside the United Kingdom and the US. Aside from proficiency in the English language and close affinity with the West, Filipino IT professionals are highly trainable with a learning curve of six to eight weeks. Philippines, despite continuing political instability and infrastructure weaknesses, continue to benefit from the global exposure and English language skills of its workforce. It is easier for Philippine BPO providers to service U.S clients because of language and cultural affinity but there are still more markets to conquer when it comes to business process outsourcing.

CITEM reports the cost savings in the Philippines are 30 to 50 percent over the US operations. Based on data from an international human resource consultancy firm CITEM reported that labor rates in Philippine were most competitive among 32 countries surveyed for the same IT skills.

### **Japan Market**

The shortfall of skilled engineers and rising cost of information technology (IT) services in Japan present an opportunity for the Philippines' IT outsourcing services firms.

Aiming to become the offshore destination in Asia, the Philippines is currently intensifying its marketing efforts in software outsourcing in Japan. Philippine software industry is trying to boost exports by diversifying product and service offerings.

The Center for International Trade Expositions and Missions (CITEM) reported that in a survey of overseas transactions in July 2004, the Philippines was one of the top 10 offshore destinations preferred by Japanese software companies. Currently, majority of Philippine-based software service providers are subsidiaries of large Japanese companies such as Fujitsu, Canon, EPSON, and NEC.

The country's geographical proximity, international business sense and abundance of young software engineers, position the Philippines as a potential market for Japanese companies seeking an offshore destination.

The Philippines has made inroads in the Japanese software market and has grown by 34% from 2002 to 2003. Subsequently, even the Japanese offshore market has grown substantially in last 5 years. In 2003, Japan represented a \$400 million outsourcing market.

### **1.11 The Philippines : Low Cost, but Higher Risk**

After India, the Philippines is probably the second most popular destination when it comes to pure offshore outsourcing. With a \$1 billion outsourcing industry, the country is known for its applications development and maintenance, contact centers, business process outsourcing and content conversion. The Philippines' popularity is contributed by its English proficiency, a highly skilled workforce (380,000 college graduates annually), developing telecommunications infrastructure and low cost. However, some researchers and

critics rank the Philippines behind other Asia-Pacific countries such as Singapore because of lack of native IT companies and political instability.

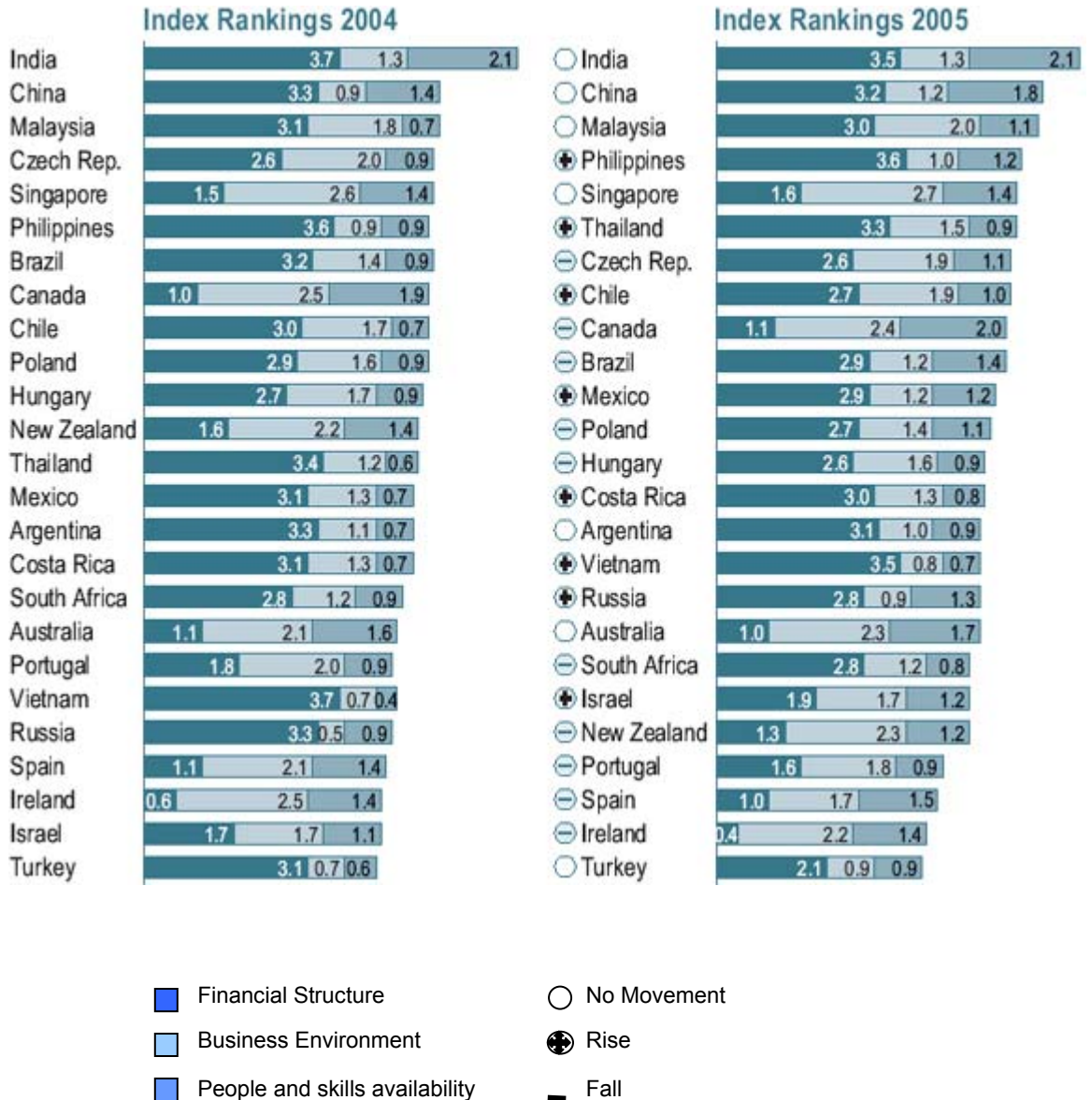
In the past decade, the Philippines have been dealing with militant Muslim insurgents which has had a destabilizing effect on the nation's ability to attract and sustain foreign capital investment, and thus poses serious threats to the economy. But these threats are limited to the Philippines' southern islands and have not affected IT setups in Manila.

A survey of A.T. Kearney Global Services Location Index 2005 shows the current outsourcing structure of the following countries:

Rank	Country	Financial structure	People and skills availability	Business environment	Total score
1	India	3.47	2.14	1.26	6.87
2	China	3.21	1.76	1.17	6.14
3	Malaysia	2.95	1.12	2.00	6.07
4	Philippines	3.58	1.16	1.05	5.78
5	Singapore	1.62	1.44	2.67	5.73
6	Thailand	3.27	0.94	1.51	5.72
7	Czech Republic	2.57	1.12	1.90	5.58
8	Chile	2.73	0.97	1.87	5.58
9	Canada	1.10	2.03	2.40	5.52
10	Brazil	2.91	1.36	1.23	5.50
11	United States	0.54	2.74	2.22	5.49
12	Egypt	3.55	0.95	0.98	5.47
13	Indonesia	3.51	1.06	0.89	5.47
14	Jordan	3.02	0.91	1.43	5.35
15	Bulgaria	3.29	0.86	1.11	5.27
16	Slovakia	2.72	0.96	1.55	5.24
17	Mexico	2.87	1.16	1.19	5.22
18	Poland	2.67	1.06	1.44	5.16
19	Hungary	2.61	0.88	1.63	5.13
20	United Arab Emirates	2.66	0.61	1.85	5.12
21	Costa Rica	2.96	0.79	1.34	5.09
22	Ghana	3.57	0.58	0.93	5.08
23	Argentina	3.14	0.93	0.98	5.05
24	Romania	3.07	0.92	1.05	5.03
25	Jamaica	2.92	1.01	1.10	5.03
26	Vietnam	3.55	0.69	0.76	5.00
27	Russia	2.83	1.31	0.85	4.99
28	United Kingdom	0.46	2.12	2.41	4.99
29	Australia	0.97	1.66	2.29	4.91
30	Tunisia	2.97	0.69	1.20	4.86
31	Germany	0.50	2.10	2.23	4.84
32	South Africa	2.76	0.81	1.24	4.81
33	Israel	1.86	1.22	1.67	4.75
34	New Zealand	1.28	1.19	2.28	4.74
35	France	0.40	2.24	2.05	4.69
36	Panama	2.90	0.65	1.10	4.65
37	Portugal	1.60	0.88	1.80	4.28
38	Spain	0.96	1.50	1.67	4.12
39	Ireland	0.42	1.41	2.25	4.07
40	Turkey	2.14	0.91	0.92	3.97

Note : The weight distribution for the three categories is 40:30:30. The financial structure is rated on a scale of 0 to 4, and the categories for people and skills availability and business environment are on a scale of 0 to 3.

The following graph shows comparison of 25 countries included in both the 2004 and 2005 index:



## 1.12 Conclusion

The Philippines' can enter into the global software market as a low-cost high quality provider of software services. The service costs a fraction of what it may cost to have the same job done in the US, Japan, or Europe.

Recent market research shows that the programming and coding rates have gone high especially in India which leaves a viable option for Philippines. But at the same time the emergence of countries like China or Vietnam as alternative sources of programming services will continue to put downward pressure on software development rates. With their potential to scale and relatively lower salary structures, it will be very difficult to compete with them solely on the basis of cost over the long term.

Today, the global software industry is not an example of a price elastic market. Lowering costs does not necessarily ensure more business and certainly does not mean more profit. On one hand costs are important but on the other hand, certain segments of the market are even willing to pay a premium for an assurance of quality and reliability.

The Philippine software development industry has reached a level of maturity that allows us to compete, in terms of not only cost, but also competence and expertise. This provides us an opportunity to differentiate ourselves from our competitors and create competitive advantages - in terms of quality, expertise, and reliability - that are more sustainable and less easy to replicate than cost.

Here are some ideas on how we can create and communicate our sustainable advantages:

- ❖ Local software companies must continue to invest in improving their quality processes. Currently, more than 50 local companies have obtained CMM-I /ISO certification. Certification is a long and expensive process but the number of local companies who have already started aligning with international quality standards (through documentation, process improvements, business assessment, etc.) would be significant.
- ❖ The companies should focus and encourage on having more and more certified professionals. It is one of the important criteria the companies look for before selecting a offshore software service provider.
- ❖ The local companies have to start focusing on domain or will have to create technological niches. Especially, for start-up companies, it always seems very tempting to engage themselves in several fields for the want of losing any opportunity that falls in their way. However, this often forces such companies to compete solely on the basis of cost. By being much focused on what it offers and excelling at delivery, a local company is able to position itself more successfully, optimize resources more efficiently, and increase its profitability.
- ❖ To be successful in the offshore market the marketing presentation plays a major role. While cost-effectiveness remains an important factor to outsource work offshore, we must provide more

compelling reasons to choose the Philippines over other providers. And no reason could be more compelling than a compilation of success stories and customer testimonials which revolves around quality and reliability. "Brand Philippines" should primarily harp on quality and reliability.

Of course, all of the above need to be done in conjunction with other initiatives like continuous capability building, intellectual property protection, and so on.

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