Outsourcing Across Cultures

By Lothar Katz

When investigating “The Hidden Costs of Offshore Outsourcing”*, CIO Magazine listed six factors causing costs that most companies overlook when preparing for new outsourcing engagements. Any guesses which one they found most relevant, with associated costs that could exceed 25 percent of a deal’s total volume?

The answer: *“The Cultural Cost”*, defined as productivity lags caused by cultural obstacles. Such productivity losses are often hidden because they are hard to identify upfront without sufficient experience, because they depend on a number of influences that in themselves are difficult to assess, and because offshore outsourcing vendors inevitably won’t bring any of them up when negotiating agreements. It is of interest, though not surprising, to note the wide range of the potential cost impact, ranging from 3 to 27 percent of total cost.

Unidentified costs of this magnitude are a CFO’s nightmare. Their impact could prove engagements that initially looked attractive disastrous. Making outsourcing successful requires preparing for this kind of challenge and learning how to master it, which raises two questions: what causes such productivity losses and what can be done to minimize them?

1. Communication

Misunderstandings inevitably reduce productivity. Working across cultures, misunderstandings are much likelier to occur due to the additional challenges of language, distance, and cultural paradigms. Where an American team member may openly flag issues, an Indian one may not. Successful offshore outsourcing requires leaders who competently bridge these gaps, communicating effectively and in culturally appropriate ways.

2. Learning Curve

How quickly an offshore team can be brought up to speed depends on a number of factors, several of which depend on the cultural context. Previous experience and overall levels of expertise play a role, as does the level of alignment between client and vendor processes and practices. Identifying and resolving compatibility issues upfront is essential for a smooth transition of an in-house process to an outsourcing vendor. However, even when managed well, productivity drops of about 20 percent in the first year or two are almost inevitable.

3. Work Efficiency

Once a team has moved down the initial learning curve, its continuous work efficiency depends on a variety of factors. Cultural influences dominate or at least bias most of them and therefore require careful consideration. Forcing foreign vendors to use systems, processes, procedures, and communication channels that are misaligned with their cultural preferences tends to affect their work efficiency and lower their productivity. For example, while introducing rigid milestones and requiring regular reviews can be effective with Western work teams, the approach may stimulate Asians to delay even small decisions and address problems only during the reviews instead of when they first surface. Maintaining the highest work efficiency requires carefully analyzing best practices on both sides and implementing work procedures that balance cultural preferences with overall workflow requirements.

4. Talent Retention

Mostly overlooked in early offshore engagements, workforce turnover has now become a substantial problem in many premier outsourcing destinations. India's and China's bustling business centers, from Bangalore and Mumbai to Shanghai and Shenzhen, report attrition rates that sometimes exceed 50 percent, which can dramatically lower the productivity of even the best teams. Vendors are trying to address the issue by doubling up resources and improving employee training, but few of them have the vision and experience required to address it proactively, retaining key talent among their workforce. As their client, you will need to make it your own job to ensure that adequate employee motivation and retention programs be put in place in order to minimize the impact turnover might have on productivity. Again, this requires a thorough understanding of local practices and values.

Conclusion

Simply put, CIO Magazine's findings tell you this: when engaging in outsourcing across borders, you may be able to keep productivity hits small if you can identify cultural influences upfront and manage them competently. Otherwise, the price you will be paying may be steep – and you won't see it before it hits you.

(*) CIO Magazine, *The Hidden Costs of Offshore Outsourcing*, www.cio.com/archive/090103/money.html

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