

Guidebook by Prayag Consulting

Germany's market potential for Indian offshoring companies



July 2005



No.19, BHCS Layout
Bannerghatta Road
BTM 2nd Stage
Bangalore - 560076
India

Ph: (91) 80 26680216
Fax: (91) 80 26683433
Email: info@prayag.com
www.prayag.com

Table of content

1. Executive summary.....	4
2. Introduction.....	5
3. Scope and methodology.....	6
4. German market analysis	7
4.1 Economic overview	7
4.2 Market segmentation.....	8
4.3 Specific characteristics	9
5. German IT market.....	11
5.1 Market profile.....	11
5.2 Major IT players in Germany	14
5.3 IT centres in Germany	16
6. German offshoring market.....	17
6.1 Market mapping	17
6.2 Offshoring – The Indo-German scenario.....	20
7. Key findings	23
7.1 Assessment of Indian offshore companies	23
7.2 The German market – Challenges and opportunities	26
7.3 Indo-German relation – The challenges	27
8. Conclusion.....	28
Bibliography.....	29

1. EXECUTIVE SUMMARY

The German economy, which has been facing trouble since years is trying to gather momentum. The government has to initiate reforms to fight the high unemployment rate, a rapidly aging population, high social security outlays and an inflexible job market. Despite the economic problems Germany's expenditure on IT is growing. Offshoring has become one of the key areas in terms of IT focus. Studies predict that almost all large firms that haven't joined the offshore bandwagon will have an offshoring roadmap in the next few years. Germany, not being an exception has selected India to be its major offshoring destination.

Although labour costs in India are increasing and new competitors are emerging, India will still be able to retain its position as a low price, high quality and efficient offshoring destination. The country will remain Germany's preferred offshoring partner in the near future. Beside the low costs and the high quality Germans especially appreciate the flexible and well-educated workforce. On the other hand, India still can improve in terms of infrastructure and structured methods of working.

Indian firms have to be aware of the emerging competition from Eastern European countries. It is predictable that these countries will play a major role for Germany due to their local and cultural advantages. However, experts believe that language and cultural barriers will not be a major bottleneck in the relation between India and Germany.

Another important finding is that Germans strive for a strong and long-term relationship. The focus is not project based but on a sustainable business relationship. Moreover, personal involvement, control and transparency during all process stages are important to German companies.

2. | INTRODUCTION

Germany is still faced with one of their biggest economic crisis in their 60-year-old history. This diluted the attention towards IT investments and led to procrastination. However, after a few years of cutback and stagnation, German firms recognized that they need innovative IT services to stay competitive in the future. Although offshoring is not a common practice in Germany as in other countries like USA and UK, the percentage of IT services which were outsourced to foreign countries has increased during the last few years. With a market share of 12.9 percent, in terms of Total Contract Value of offshoring to India in 2004, Germany ranks number three and is about to become an important player in worldwide offshoring.¹

This study has been undertaken to analyze the potential of the German IT market in terms of offshoring to India. It focuses on the software and IT services segments in Germany. Other supporting areas of IT, like telecommunications or hardware, are beyond the purview of this study.

At first, the theoretical framework of the study has been discussed under scope and methodology. The analysis of the German market describes Germany's economic situation, key players and specific characteristics. Thereafter, the study introspects the German IT and offshoring market to map the offshoring activities being undertaken in Germany.

The conclusions of the interviews together with the findings from different secondary data lead to the key findings of the study. Finally, a brief outlook on the future of offshoring from Germany to India has been talked about.

¹ Merrill Lynch report: Indian IT services, 01/2005

3. SCOPE AND METHODOLOGY

The information provided in this paper is based on web research as well as interviews with Indian and German executives. Personal interviews with managers of Indian offshore companies helped to understand their experiences and expectations of the Indian companies from their potential German business partners. Besides that, interviews with German executives illustrate the German point of view regarding offshoring to India.

The interviews were conducted face-to-face in Bangalore and via telephone with people in Mumbai (Bombay) and Germany. Perspectives that evolved out of interactions with Indians and Germans have been included in this study. The objective of these interviews were to investigate the existing mutual business activities, gain information about their experiences and find out specific characteristics regarding offshoring from Germany to India.

To understand both sides of the coin, the respondent-mix comprised of professionals associated with German companies as well as executives from Indian companies involved in offshoring business. The German companies addressed belong to sectors like manufacturing, financial services and IT consulting with a worldwide turnover between €100 million and €20 billion. The Indian companies targeted have a turnover between €15 million and €1.25 billion per year.

4. GERMAN MARKET ANALYSIS

4.1 ECONOMIC OVERVIEW

Population (million)	82.4
Labour force (million)	42.63 (2004)
GDP (trillion US\$)	2,362 at PPP (2004)
GDP per capita (US\$)	28,700 at PPP (2004)
Inflation rate	1.6% (2004)
Unemployment rate	10.6% (2004)
Indirect tax	16% (VAT)
Currency	Euro

Figure 1: CIA: The World Factbook - Germany, 29/06/2005

With a growth of 1.7 percent in 2004 Germany's economy is one of the slowest growing economies in the European Union. The integration and the setup of former Eastern Germany continues to be a costly process with about \$70 billion and is often used as an excuse for the problems. However, this is only one reason why Germany hasn't been able to make a turnaround so far. The country is facing high unemployment, an aging population, high social security outlays, strict working regulations and insufficient education, just to name a few. The current governmental coalition of Social Democrats and Greens have started the reform program "Agenda 2010" but without much success so far. That's why Chancellor Gerhard Schröder gained support for his bid to hold early parliamentary elections when the Bundestag held a vote of confidence on July 1, 2005.

A widely accepted principle of German economic strategy has been the openness of its economy, that is, its free trade policy. This results in an export share of 37.8 percent of its GDP (2004).²

² CIA: The World Factbook Germany, 22/06/2005

SOCIAL ASPECTS

89.5 percent of the 36 million gainfully employed persons in the Federal Republic of Germany are wage and salary earners, i.e. employees, civil servants, and trainees or apprentices. In addition, there are 3.3 million self-employed.

Employers and employees negotiate collective agreements without interference from the government. The state sets the general conditions by legislation, but it does not lay down how much workers should be paid. This and many other matters – for example holidays – are left to the "social partners", i.e. the trade unions and employers' associations, to negotiate themselves.

4.2 MARKET SEGMENTATION

The mainstay of the German economy is their industry with about one third contribution to the GDP. The 49,000 industrial undertakings employ almost 6.4 million staff and realize a turnover of almost €1.3 trillion in total. 98 percent of the industry firms belong to the SMEs (small and medium-sized enterprises).

Alongside industry, the services sector also plays an outstanding role and has become larger than industry with 68 percent contribution to the GDP. A German peculiarity and traditional core of economic life is the crafts trade. With around 863,000 businesses, it is Germany's most varied economic sector, employing 14 per cent of Germany's 36 million workers. German industry is very diversified and in many sectors it is a global leader. Germany is the world's third largest automobile producer, with more than 70 per cent of vehicles produced here, intended for export. Machine and plant construction, in which most German industrial undertakings are involved, also holds lot of importance.

Germany is also a world leader in the financial and chemical industry. Furthermore, among Germany's most innovative sectors with above average growth rates are those of technologies for the use of renewable energies as well as information technology and bio-technology.

Of the German firms, the larger German multinationals such as Allianz, Bayer, BMW, DaimlerChrysler, Siemens, and Volkswagen are recognized internationally.

SMEs DOMINATE

In contrast to these global players the 3.4 million SMEs (in German called “Mittelstand”) have always predominated in Germany. These companies which earn an annual turnover of less than €50 million and employ less than 500 employees account for 43.2 percent of total revenues.

SMEs (Small & Medium Enterprises) in Germany

- ▶ Make up 99.7 % of all German companies
- ▶ Realize 43.2 % of all taxable revenues
- ▶ Contribute 48.8 % to the Gross value added of all companies
- ▶ Provide 69.7 % of all jobs
- ▶ Provide 80 % of all apprenticeship training positions

Figure 2: SME, based on German Ministry of Economy and Labour, 07/2005

4.3 SPECIFIC CHARACTERISTICS

The German market has always been a quite difficult one to enter for Indian software companies. The two countries can not look back on a long relationship because of historical connections like the UK and India. In addition, Germany does not have an economic and political openness like the US that allows easily establishing business or political relations. That’s why it is very important for Indian firms to understand the principal characteristics of the German market.

LANGUAGE AND CULTURE

The vast use of German language in domestic IT processes is still a major obstacle for transferring IT processes to offshore countries. Although English plays a dominant role in the IT business, a lot of German employees don’t have expertise in speaking English. Xenophobia to a certain extent is also a deterrent to the whole process. The mentality in Germany can be described as orthodox and more risk averse than English-speaking countries. That’s why German firms are more likely to look at outsourcing possibilities in Germany or Europe at first. They also prefer indirectly sourcing offshore services through an “occidental”

third service provider. IT service firms like IBM and Accenture, which have strong experience in offshoring services, profit from the Germans' cautious approach.

TRADE UNIONS AND POLITICAL INFLUENCE

Germany is known for its strong labour regulations. The powerful position in economic affairs of both trade unions and the government makes it difficult for companies to justify and enforce the shifting of hundreds or thousands of jobs to foreign countries.

The largest labor organization in the Federal Republic is the German Trade Union Federation ("Deutscher Gewerkschaftsbund or DGB") with about 7.9 million members (at the end of 2001). The DGB is nationwide. It comprises 8 unions within its federal structure. This allows a greater flexibility with respect to regional economic developments.

The German trade unions are not connected with any particular party or church. No one can be forced to join a union. The closed shop system (which, according to agreements between employers and unions, allows only union members to be employed) is alien to Germany. The degree of unionization (i.e. the proportion of workers who are members of unions in certain industries) varies greatly but averages less than 50 percent and is further decreasing.

Beside the unions, the government has a major influence on the economy. Despite their openness for foreign trade, governments usually tend to be more protectionists.

EMPLOYERS' ASSOCIATIONS

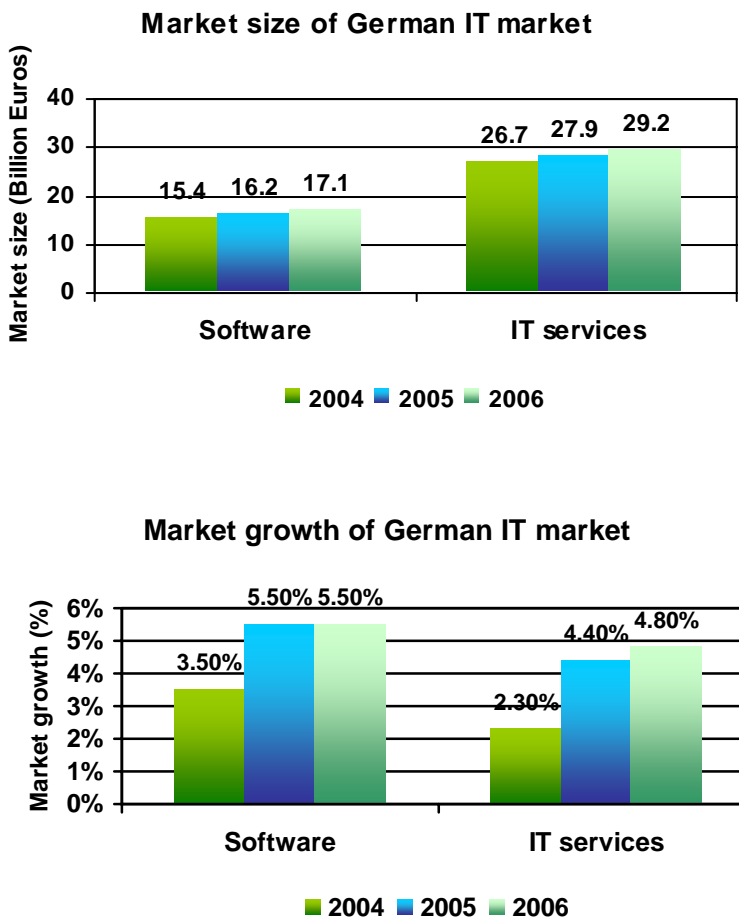
The employers have joined to form regional associations, which – like the DGB unions – are based on the principle of "one industry, one association". The central organization of the employers' associations is the Confederation of German Employers' Associations ("Bundesvereinigung der Deutschen Arbeitgeberverbände or BDA"). The BDA covers all branches of business – from industry, crafts and trades, commerce, banking and insurance to agriculture and transport.

About 80 percent of entrepreneurs are members of an employers' association – a much larger proportion than in the case of employees. The BDA represents

them only in their role as employers, i.e. as negotiating partners of the trade unions. All other interests – taxation or economic policy, for instance – are taken care of by other business organizations such as the Federation of German Industries (“Bundesverband der Deutschen Industrie or BDI”).

5. GERMAN IT MARKET

5.1 MARKET PROFILE



Despite the economic trouble a bullish mood is prevalent in the German IT market. According to the latest quarterly sentiment indicator published by Bitkom, an association of 1.300 IT firms in Germany, almost all companies expect an increasing growth in the year 2005. Both software and IT services will constantly grow with about 5 percent this and next year. The graphs depict the spending and growth rate in 2004 as well as the forecasted rates and expenses for 2005 and 2006.

Figure 3: Market size and market growth of the German IT market, based on Bitkom, 03/2005

A study published by CapGemini predicts a slower growth and only a mid-term rise in budgets.³ The IT consulting company found out that the IT executives expect stagnating or slowly rising expenses in the next two years. Though, half of the respondents think that in 2009 the firms will start spending more again.

³ CapGemini: IT Trends 2005, 02/2005

LACKING EXPERTS

The IT services and software industry in Germany will register an increase in staff this year for the first time since the year 2000. According to Bitkom's estimation, the companies will hire 12,000 new employees.

	2002	2003	2004	2005 (est.)
Employees in IT services and software industry	375,000	365,000	364,000	376,000
Annual percentage change		-3%	0%	3%

Figure 4: Employees in IT services and software industry 2002-2005, based on Bitkom, 2005

Despite the current need for new employees the first-year students studying IT related subjects decreased in the last years.

	2002	2003	2004	2005 (est.)
First-year students IT related subjects	33,000	33,600	28,600	27,000
Annual percentage change		2%	-15%	-6%

Figure 5: First-year students IT related subjects 2002-2005, based on Bitkom, 2005

Thus a lack of IT specialists and engineers is apparent. In a Bitkom survey at the end of 2004, 16 percent of the German companies stated that they can't find enough experts.⁴

TRENDS

After years of drastic cutback in capital expenditure, German firms are back with fresh investments being made to renew their systems. There is an upsurge in demand for better IT security and companies will continue to make investments. SAP implementation and maintenance forms another area of priority for the firms. In addition, companies will also tend to invest more in mobile and wireless applications. Mobile solutions for sales, marketing, customer service and production often have been developed and realized, but there is still a big demand for new concepts in logistics. Other important tasks will be new software for an optimized Customer Relationship Management (CRM) and investments in Enterprise Resource Planning (ERP), Total Cost of Ownership (TCO), and Enterprise Application Integration (EAI).

⁴ BITKOM: Daten zur Informationsgesellschaft 2005

5.2 MAJOR IT PLAYERS IN GERMANY

SOFTWARE COMPANIES

During the new economy boom, many software start-ups were set up in Germany, but only a handful survived the winds of change in 2001. The following table lists the 25 biggest software companies in Germany with their turnovers. All the companies in this ranking earn at least 60 percent of their turnover from producing, selling and maintaining of their standard software.

	Company name	Location	Total turnover (million Euros)	Turnover in Germany (million Euros)	Employees
1	SAP AG	Walldorf	7,514.0	1,780.00	32,205
2	Microsoft Deutschland GmbH	Unterschleißheim	1,800.00	1,800.00	1,850
3	Oracle Deutschland GmbH	München	475.6	475.6	1,300
4	Software AG	Darmstadt	411.4	66	2,438
5	Infor Global Solutions	München	380.4	208.4	2,200
6	CA Computer Associates GmbH	Darmstadt	145	145	510
7	Mensch und Maschine Software AG	Wessling	135.5	41.5	355
8	SAS Institute GmbH	Heidelberg	128.5	128.5	700
9	PSI AG	Berlin	115.2	99.8	1,149
10	Novell GmbH	Düsseldorf	115	115	260
11	BMC Software GmbH	Düsseldorf	112	112	240
12	Beta Systems Software AG	Berlin	100.8	50	1,022
13	Nemetschek AG	München	97	47	756
14	SoftM Software & Beratung AG	München	87.5	81.1	476
15	FJH AG	München	70	60	900
16	Interflex Datensysteme GmbH & Co. KG	Stuttgart	56	38.6	411
17	CSB-System AG	Geilenkirchen	52.1	33.5	470
18	Sage Software GmbH & Co. KG	Frankfurt, Main	52	51	430
19	Microsoft Business Solutions Deutschland GmbH	Hamburg	48.8	48.8	105
20	Intershop Communications AG	Jena	45.1	14	260
21	Peoplesoft GmbH	Unterföhring	45	45	200
22	MIS AG	Darmstadt	44.7	28.7	450
23	Intentia Deutschland GmbH	Hilden	40.5	40.5	325
24	P&I Personal & Informatik AG	Wiesbaden	40.1	35.5	239
25	Cognos GmbH	Frankfurt, Main	37	37	130

Figure 6: 25 biggest software companies in Germany 2004, based on Lünendonk GmbH, 25/05/2005

IT SERVICES COMPANIES

US companies dominate the German IT services market space. The undisputable market leader IBM Global Services realized a turnover of €966 million in 2004, followed by Accenture with €586 million on rank three. In Germany, many IT companies are IT spin-offs of large firms like Lufthansa Systems Group GmbH which holds rank two with €628 million.

The following list shows the 25 largest companies that offer more than 60 percent of their turnover with IT consulting, development of customized software solutions and system integration.

	Company name	Location	Total turnover (million Euros)	Turnover in Germany (million Euros)	Employees
1	IBM Business Consulting Services	Stuttgart	966	966	NA
2	Lufthansa Systems Group GmbH	Kelsterbach	628	628	4,500
3	Accenture GmbH	Kronberg	586	586	3,603
4	CSC Ploenzke AG	Wiesbaden	571	404	4,900
5	gedas AG	Berlin	567	150	4,930
6	Capgemini Deutschland Holding GmbH	Berlin	477	477	3,256
7	BearingPoint GmbH	Frankfurt, Main	400	400	2,600
8	Atos Origin GmbH	Stuttgart	380	380	3,500
9	SAP SI Systems Integration AG	Dresden	336	269	2,200
10	IDS Scheer AG	Saarbrücken	280.2	111.2	2,132
11	Deutsche Post ITSolutions GmbH	Bonn	216	216	1,300
12	msg Systems AG	Ismaning	203	185.3	1,900
13	ESG Elektroniksystem- und Logistik-GmbH	München	175	170	1,030
14	Softlab GmbH	München	165	135	1,180
15	IT-Services and Solutions GmbH	Chemnitz	151	151	1,200
16	LogicaCMG Deutschland GmbH & Co. KG	Hamburg	136	136	1,500
17	itelligence AG	Bielefeld	131	64.9	936
18	GFT Technologies AG	St. Georgen	125.5	84.3	1,039
19	sd&m Software Design & Management AG	München	125	125	950
20	Unilog Holding GmbH	Tübingen	125	125	1,100
21	Materna GmbH	Dortmund	120	108	1,100
22	Unisys Deutschland GmbH	Sulzbach	106	106	462
23	SerCon Service Consulting GmbH	Böblingen	85	85	950
24	C1 Group GmbH	Hamburg	76.3	76	629
25	entory AG	Karlsruhe	67.4	61.5	485

Figure 7: 25 biggest consulting and system integration companies in Germany 2004, based on Lünendonk GmbH, 25/05/2005

5.3 IT CENTRES IN GERMANY

MUNICH IS LEADING

Munich is Germany's biggest technology and IT hub. According to a study compiled by the municipality of Munich and the chamber of commerce the Munich region's ICT (Information and Communication Technologies) sector is comprised of 22,500 companies.⁵ By the end of 2003, these companies had a total workforce of 395,000 and generating revenues to the mark of €70 billion. IT multi-nationals like Microsoft and Oracle have their European headquarters in Munich.

The city is not only characterised by a large density of IT companies, but also of a proximity to user sectors and suppliers. Large corporations like Siemens, BMW, or Allianz are headquartered here.

OTHER IMPORTANT DESTINATIONS

The South-West of Germany around the city of Stuttgart is also known as one of the most dynamic locations for IT companies. Global players such as Bosch, DaimlerChrysler, Hewlett-Packard, IBM, and Porsche are located in this area. Frankfurt, situated in the middle of Germany, is an international hub of air, road and rail transport. Moreover, it occupies a leading financial position in Europe with the Frankfurt stock exchange, the European Central Bank and principal financial organizations.

Other important regions in Germany are Heidelberg, Düsseldorf and Berlin.

FORMER EASTERN GERMANY CATCHES UP

Since a couple of years, former Eastern Germany has become a lucrative option for IT investors. Especially Saxony with the cities Dresden and Leipzig has managed to attract microelectronics companies like AMD or Infineon. In addition, the region has become a centre of automotive manufacturing. Volkswagen, Porsche and BMW run production facilities there.

⁵ Municipality of Munich, 07/2005

6. GERMAN OFFSHORING MARKET

6.1 MARKET MAPPING

IT services vendors like Accenture or IBM have been catering to offshore services for more than ten years in Germany. While these suppliers have strong experience in this field, it was only in the late 90s that the buyers exhibited their interest for outsourcing to foreign countries.

The opportunity of offshoring was hardly recognized by the German public until the end of 2003 when Siemens announced to offshore some thousands of jobs. A large public response followed, caused by the fear of many losing their jobs. The German companies were also apprehensive to give away the responsibility over whole business processes to foreign countries.

Compared to USA and UK, Germany features a slow start of offshoring activities. According to a study by A.T. Kearney in 2004, about 5 percent of Germany's IT budget goes into foreign countries, whereas the companies in the USA spend 20 percent for offshoring.⁶ Almost all German companies think about offshoring, but don't have concrete strategy.

The MetaGroup represents a more optimistic scenario. The experts think that in the near future about 20 percent of the IT budget will go to offshore projects. By the end of 2006, 90 percent of the large concerns will have implemented an offshoring strategy.

⁶ A.T. Kearney: Offshoring threatens 130,000 German IT jobs, 18/02/2004

COST REDUCTION – THE DRIVER

A study conducted by Bitkom and Deutsche Bank among 267 vendors and 305 buyers of offshore services in Germany arrived at the conclusion that cost reduction is the predominant reason for German firms to outsource processes.

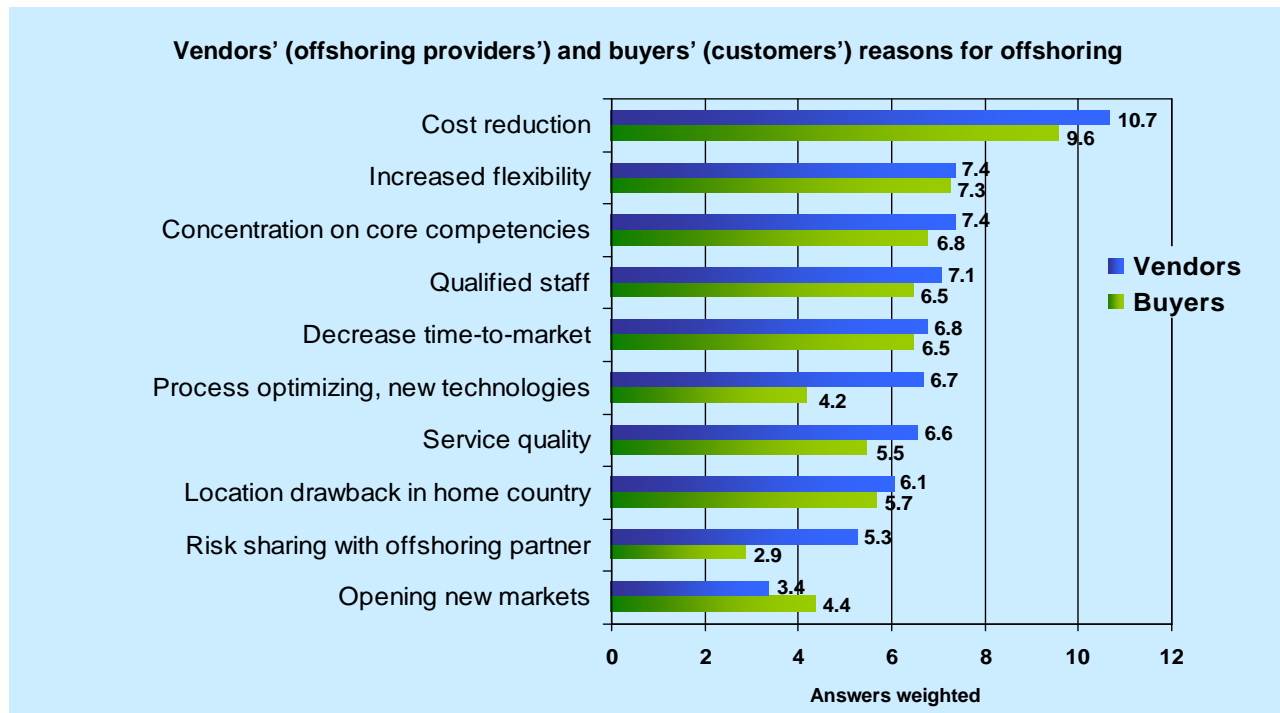


Figure 8: Vendors' (offshoring providers') and buyers' (customers') reasons for offshoring, based on Bitkom/DB Research, 14/06/2005

Cost benefit stands to be the most potential mutual value proposition for both the suppliers and buyers in terms of offshoring services. The survey showed that increased flexibility and concentration on core competencies, along with access to well-educated personnel comprises the other major determining factors.

EMERGING COMPETITOR: EASTERN EUROPE

Although India is the most important offshoring partner for Germany, German companies expect the Eastern European countries to emerge as potential markets, within the next few years. According to the research of Deutsche Bank and Bitkom in 2005, German companies have more inclination towards their Eastern neighbours. 46 out of 305 buyers interviewed already claim upon offshore services, 18 plan to buy these, and 28 expect that “nearshoring” will become interesting to them within the next five years. Regarding India, the corresponding statements are 49, 7 and 14. The numbers show that India still has the status and advantage of a “first-mover” in the market, but the countries in Eastern Europe will turn to be more attractive for Germany.

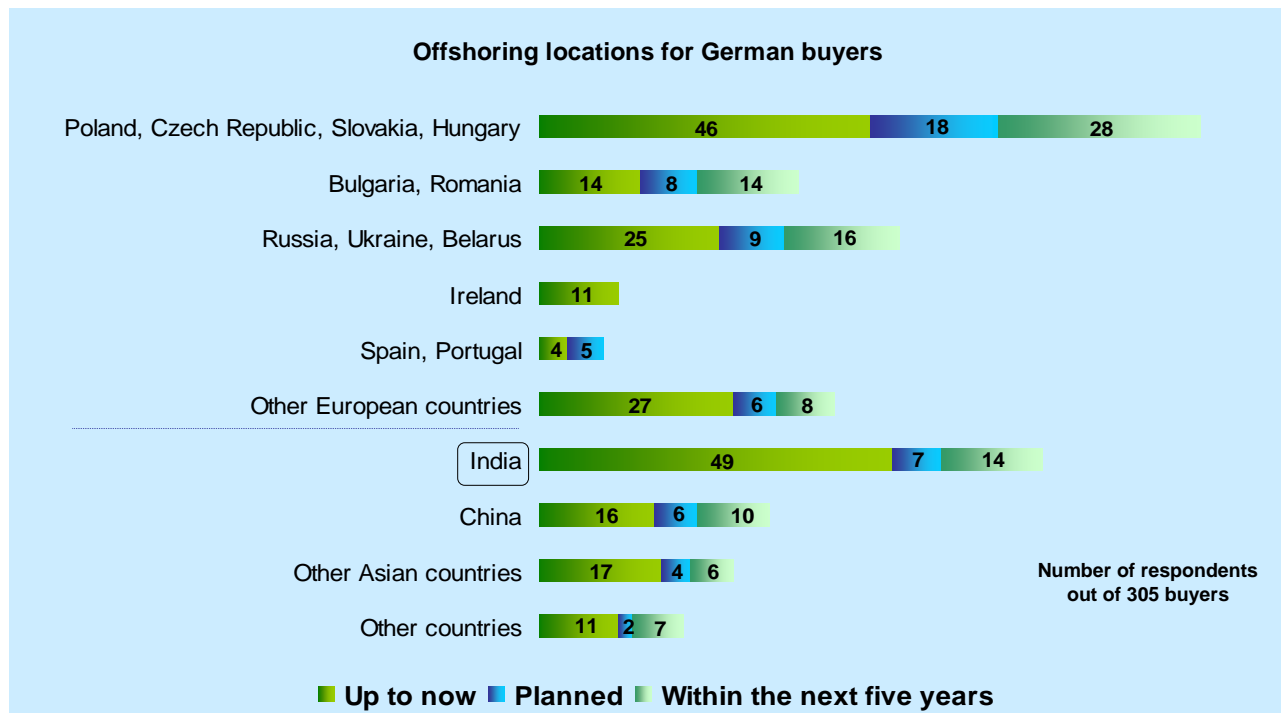


Figure 9: Offshoring locations for German offshoring buyers, based on Bitkom/DB Research, 14/06/2005

The firms, which opt for offshore services continue focusing on India as the number one location in the future. However, they also predict that “nearshoring” to Eastern European countries will have the biggest growth rate within the next five years. Also China seems to become more attractive.

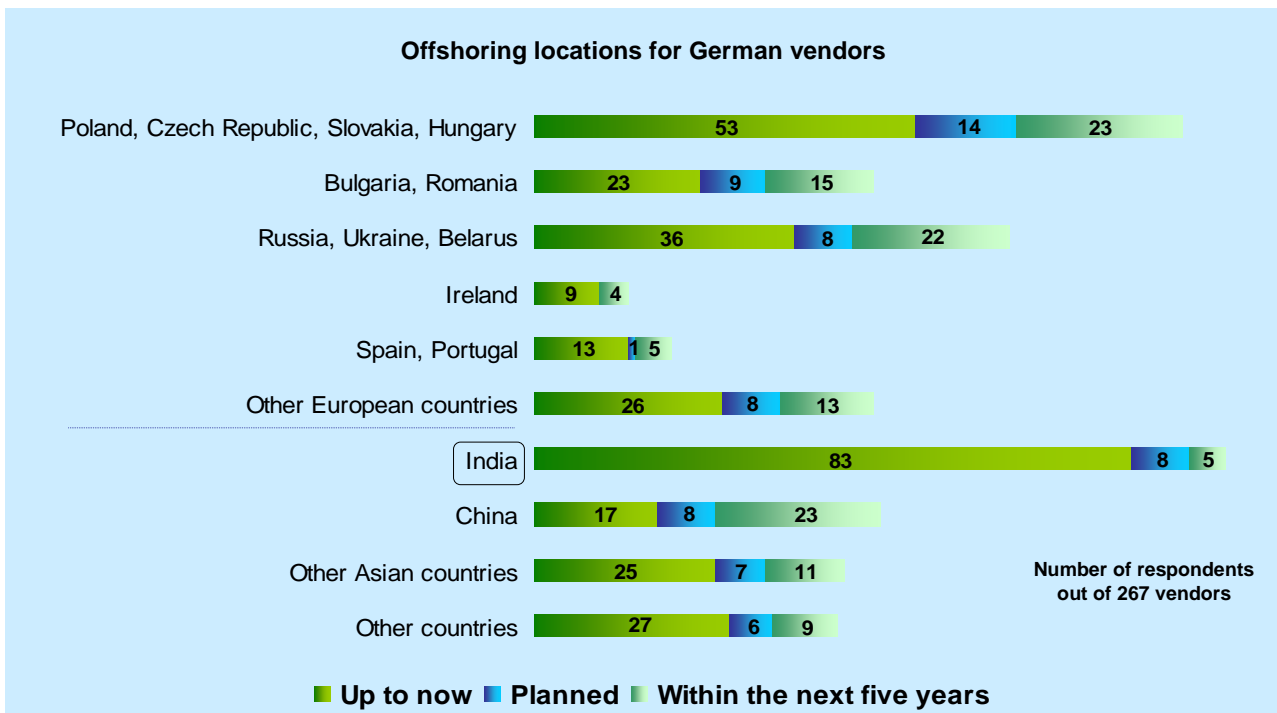


Figure 10: Offshoring locations for German offshoring vendors, based on Bitkom/DB Research, 14/06/2005

6.2 OFFSHORING - THE INDO-GERMAN SCENARIO

The sluggishness in the German market has hindered the collaboration with India as an offshore destination; however, the market is slowly becoming cognizant of the benefits of offshoring to India. German pioneers like Siemens, Bosch or SAP operate their own captives in India since years and following success stories also demonstrate the efficiency and advantages of outsourcing to India.

On the other side, Indian software companies were growing very fast in the last few years and they had to serve the huge US and UK markets first. Now, that the US and UK markets become more and more saturated Indian firms have to venture new destinations to expand their business activities. Most of them now

have sufficient funds, capacities and expertise for intensively targeting the German market.

INDIA LEADS...

With comprehensive experience and acceptable costs, India still is the country of choice for offshore activities. India covers almost 90 percent of the offshoring trade volume of Western-Europe. Germany already is India's third largest IT services offshoring partner with a Total Contract Value of \$9.02 billion and a market share of 12.5 percent.

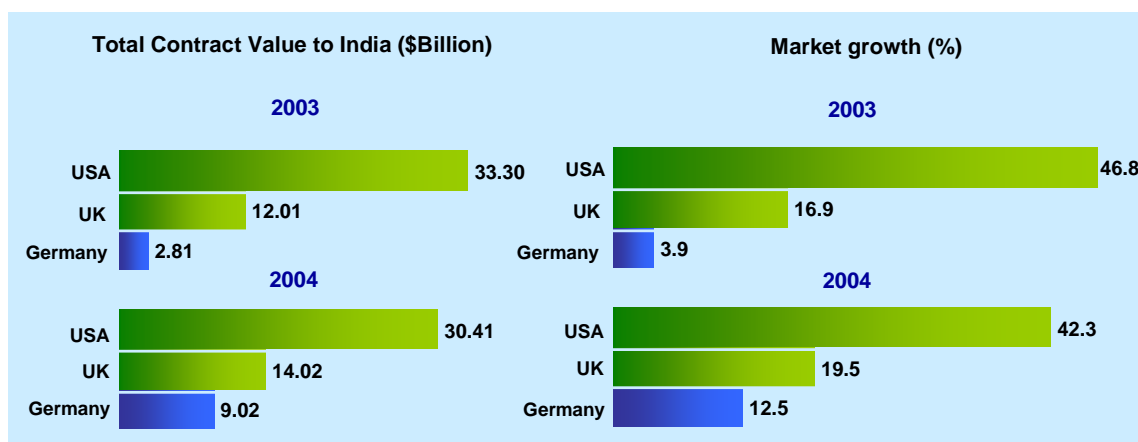


Figure 11: Total Contract Value to India (TCV) and market share of TCV, based on Merrill Lynch report-Indian IT services, 01/2005

INDIA EYES GERMAN MARKET

The offshore scenario undergoes a transformation from “push” to “pull”. Firstly, it was Germany, which initiated the “push” in terms of outsourcing followed by the “pull” from the Indian counterparts.

Indian vendors like Wipro and Infosys are formulating different strategies to intensively target the German market, as a part of their business expansion plan. Some experts predict that Indian firms will buy into big European IT service providers or even acquire them.⁷ Tata Consultancy Services (TCS), for example, takes acquisition of subsidiaries of large German firms into consideration.⁸ If Lufthansa sources out their IT provider Lufthansa Systems Group, TCS would be

⁷ Computerwoche: All statistics militate in favour of India, 11/08/2004

⁸ Financial Times Deutschland: Indian IT consultants push to Germany, 23/11/2004

a bidder. Another possibility would be to acquire a relatively small niche player with specialized workforce. Each Indian company has to identify the German partner that suits best to its' requirements. Wipro, for instance, lately announced that it is also looking for a potential acquisition candidate in Germany.⁹ They need people with consulting and program management experience who are able to develop customized solutions.

Other companies focus on their own local subsidiaries. One of them is Hexaware, a Mumbai-based vendor, which has set up a proximity centre at Bad Homburg, on the outskirts of Frankfurt, which seats about 50-60 employees.

⁹ Computerwoche: Wipro wants to buy in Germany, 21/06/2005

7. KEY FINDINGS

7.1 ASSESSMENT OF INDIAN OFFSHORE COMPANIES

► STRENGTHS



Cost benefits India offers favourable conditions with the best price-performance ratio. Although the wages have been increasing, they still remain at a favourable level. An Indian IT team leader with two to three years of experience earns €8,429¹⁰ per year on average, whereas the annual average salary for an IT expert in Germany is €56,000.¹¹

Talent pool / scalability Indian offshoring companies are able to recruit a large amount of well-trained people in a very short period of time. Both Indians and Germans agree that the high education level give the country a competitive advantage, especially in the technology field. Every year, the educational system graduates two million proficient English speakers with strong technical and quantitative skills.

Expertise One of India's biggest strengths is their sound experience in offshoring. India has been a large-scale offshore destination for more than a decade and has developed a strong expertise in a broad range of IT services, from software development to consulting. This, indeed, was not an accident. India owes his cutting edge position mainly to his well-educated staff.

¹⁰ NeoIT: Offshore & Nearshore ITO Salary Report 2004, 05/2005

¹¹ Kienbaum Consultants International GmbH, 01/07/2005

Flexibility Most of the Indian companies offer a flexible shift work, some even with 24/7 work capacity. Due to strict labour regulations with a fixed labour time, German companies can benefit a lot from outsourcing to India providing flexible work. The time difference between India and Germany can be an advantage, too, but plays a secondary role with 3.5 hours in summer and 4.5 hours in winter.

Quality India has come of age to emerge as a potential offshore destination. Leaving behind its legacy of cost advantage, it has moved on to focus on the qualitative aspects of the business. The ever-growing number of ISO 9001 and CMM Level 5 certifications confirms the high quality standards in India. Some German IT executives admit that the Indian developers often surpass their German counterparts in terms of quality performance.

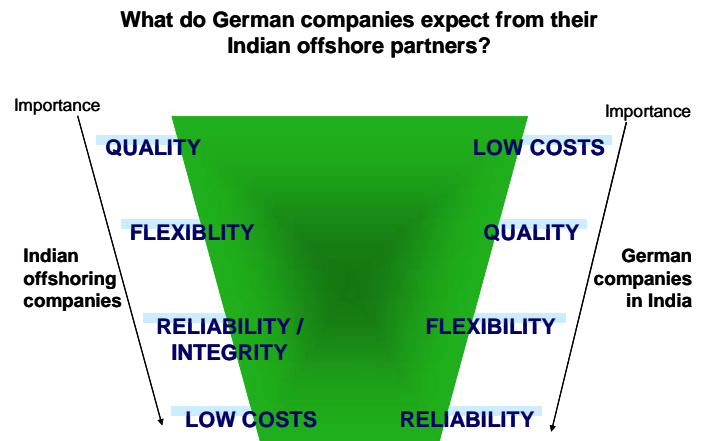
▶ **WEAKNESSES**

Infrastructure Germans do have a concern regarding the Indian infrastructure. The power supply and telecommunication system has to be improved and stabilized. Furthermore, the streets, airports and the transportation system should be ameliorated.

Work culture According to German executives Indians sometimes show a different method in terms of organizing their duties and responsibilities. Despite their great expertise many employees still can get better in structuring their tasks and complying with time schedules.

▶ EXPECTATIONS

Being asked what German companies expect most from their Indian offshoring partner, the perceptions diverged. While Indian managers believe that quality, flexibility and reliability come before low costs, the interviewed Germans think that cost savings still is the major expectation of an offshore partner, followed by quality, flexibility and reliability. Other aspects like knowledge of the German language and domain expertise are also important, but are usually taken for granted.



▶ QUALITY

German firms attach great importance to quality. Large organizations, which have already started offshoring practices, appreciate the quality of the Indian partners. Smaller companies, which haven't made the first move, are a bit sceptical about the quality standard. The expectations indeed can vary from industry to industry. The automotive industry, for instance, is known for its claim for very high quality.

7.2 THE GERMAN MARKET - CHALLENGES AND OPPORTUNITIES

▶ GERMAN MARKET IS OPENING UP

The offshoring business in Germany starts from a rudimentary level. However, the respondents prognosticate that the potential will increase in the future. Many managers used to be reluctant towards the new practice, but their opinion has changed in the last six months. IT consultants recognize that their German clients now are more open towards offshoring. A broad consensus exists that the turnover with, as well as the demand for offshore services will significantly increase in the next few years.

▶ LOCAL PRESENCE

German and Indian companies believe that a local presence is a must to be successful in the German market. The proximity to the client helps to overcome the Germans' reservation towards offshoring. Thus, Localization will play a vital role in establishing presence in the German market space.

▶ COMPETITION

Eastern Europe – The Rising Force The opinion in terms of competition from outside Germany differs a little between Germans and Indians. Germans believe that Eastern Europe will play a major role as a German offshoring destination due to proximity and cultural similarities. This will not happen in the very near future though. By contrast, Indian offshore companies don't value the significance of "nearshoring" so high, although they are recognizing their increasing importance. Indians are confident that they can keep their position as a market leader in Germany due to their long experience and establishment.

It can be foreseen that the development in Germany regarding preferred outsourcing locations will turn out to be at least in parts different from the

Anglo-Saxon area. In fact, India will still play an important role as an offshoring region. The pool of established firms with long experience and highly qualified staff at low prices is too big. However in the long run, Eastern European countries will become more important due to their cultural, linguistic and regional proximity, which will facilitate the collaboration. Indian companies should therefore be aware of the emerging competitors and use the opportunity of acclimatizing to the German market. Once an Indian offshoring provider works together with a German company, a long-term business alliance is feasible.

7.3 INDO-GERMAN RELATION – THE CHALLENGES

▶ POTENTIAL BARRIERS

Culture Cultural differences between the two countries don't represent a big obstacle. The work that is outsourced to India often includes standardized processes that can be done from anywhere in the world. From a German perspective, India is one of the Asian cultures that seems easily “accessible” compared to other countries. In addition, the Indian culture is very open-minded and closer to the European mentality. The historical background and the language contribute to this appreciation.

Language Although English is commonly spoken throughout most IT departments in Germany, comprehensibility still can cause problems during the offshoring process. Moreover, many business users are not familiar with using English in daily work. The requirements for software or other analysis documents are also often written in German. Indian companies therefore have to integrate German speaking staff in the project teams. However, the language distinction is only a limited drawback. In the meantime, many Indian students have also studied German in school or at university, or some have even studied in Germany.

▶ LONG-TERM RELATIONSHIP

Both parties, German and Indian companies, think that Germans rely on a long-term relationship. Once the first contract has been placed, follow-up orders are likely to follow. On the other hand, signing a contract with German companies can be more difficult than with US or UK companies.

▶ INTEGRATION

Another significant characteristic of the German market would be the Germans' strong belief in co-creation. Compared to other nations like USA or UK, German firms want to be more involved in the development process. Not only the finished product is important, but also the integration of the client during the whole project period. That's why intensive communication and transparency is somewhat mandatory.

8. CONCLUSION

In summary, Indian companies are facing a variety of challenges in the German IT market. Contrary to USA and UK, Germany has a different opinion towards offshore activities and political and cultural obstacles further decelerate the integration process. Despite these barriers the successful cost-cutting examples will lead to a broad acceptance of the offshore model as an alternative IT sourcing method. The current economic pressure to enforce efficiency gains will lead to an internationalization of Germany's IT practice and will open it up for offshore activities. Once a company has built the knowledge capital for lower-cost IT sourcing, the replication capability and the flexible deployment of offshore capacities will prove to be a valuable asset.

Bibliography

3a Strategy, Sourcing von IT-Services im Offshore Verfahren

AMR Research, <http://www.amrresearch.com>

A.T. Kearney, Making offshore decisions

A.T. Kearney, Selecting IT activities for offshore locations

Bitkom, Daten zur Informationsgesellschaft 2005

CapGemini, IT Trends 2005

CapGemini, The outsourcing report 2004

CIA, <http://www.cia.gov>

Computerwoche, <http://www.computerwoche.de>

Deutsche Bank and Bitkom, Offshoring-Report 2005

ECIN – Electronic commerce info net, <http://www.ecin.de>

Federal Foreign Office (Auswärtiges Amt), <http://www.tatsachen-ueber-deutschland.de>

Federal Ministry of Economics and Labour (Bundesministerium für Wirtschaft und Arbeit), <http://www.bmwa.bund.de>

Financial Express, www.financialexpress.com

Financial Times Deutschland, <http://www.ftd.de>

Handelsblatt, www.handelsblatt.de

Merrill Lynch, Merrill Lynch report – Indian IT services

Municipality of Munich, www.muenchen.de

Nasscom, Strategic Review 2004

Nasscom, www.nasscom.org

NeoIT, Offshore and nearshore ITO salary report 2004