

BEYOND THE SAVINGS

Offshoring the Problem — How the Outsourcing Wave Exported Cost but Imported Risk

A Practitioner's Perspective on the Hidden Consequences of IT Outsourcing



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1. The Promise That Was Too Clean

The logic was seductive. Labour arbitrage between London and Bangalore, between New York and Hyderabad, could reduce IT development and maintenance costs by forty to sixty per cent. The analyst firms said so. The management consultancies built entire practices around it. The board presentations wrote themselves: same work, lower cost, immediate margin improvement.

By 2003, the outsourcing wave had moved from early adopter territory into the mainstream. Financial services, telecommunications, utilities, government – every sector with a significant IT estate was either outsourcing already or building a business case to start. The contracts were enormous. Multi-year, multi-million-pound agreements with the major Indian IT services firms – Infosys, Wipro, TCS, Satyam – and with the global systems integrators who acted as intermediaries. Gartner estimated that the global IT outsourcing market would exceed \$170 billion by 2005. The momentum felt irreversible.

And yet, eighteen months into the wave, a different picture is emerging. Not in the analyst reports or the vendor case studies, but in the programme offices and the operations teams of the organisations that signed those contracts. The savings are real – but so are the costs that nobody put in the business case.

2. What the Business Case Did Not Include

The typical outsourcing business case is a model of selective accounting. It captures the obvious: current headcount cost minus projected offshore cost equals saving. It may include transition costs – the expense of knowledge transfer, parallel running, and redundancy payments. The more sophisticated cases factor in a productivity dip during the first year.

What they almost never capture is the cost of the organisational capability that walks out the door.

We did not outsource the work – we outsourced our ability to understand it. The knowledge of how systems actually behave, why they were built that way, and what happens when you change them now lives in a different organisation, in a different country, operating under a different set of incentives.

This is not a theoretical concern. Across the organisations that have moved significant portions of their IT operations offshore over the past two years, a consistent pattern is emerging:

- Specification costs have exploded. Work that was previously done through informal conversation between a business analyst and a developer who sat three desks apart now requires detailed written specifications, review cycles, and sign-off processes. The overhead of making tacit knowledge explicit — of writing down what everyone used to simply know — is substantial and ongoing. It does not diminish with time; if anything, it increases as the remaining onshore staff lose familiarity with the systems.
- Incident resolution times have lengthened. When a production system fails at two in the morning, the person who understands it is no longer reachable by walking down the corridor. The escalation path now crosses time zones, language barriers, and contractual boundaries. The vendor's incentive is to resolve the incident within the SLA — not to resolve it as fast as possible. These are not the same thing.
- Change delivery has become more brittle. The feedback loops that made iterative development possible — a developer testing an assumption with a user, a quick adjustment based on a corridor conversation — have been replaced by formal change request processes. Every modification requires documentation, estimation, approval, and scheduling. The organisation has not become more disciplined; it has become slower.
- Vendor management has become a discipline unto itself. Organisations that outsourced to reduce headcount have discovered that they need a new layer of staff to manage the outsourcing relationship: contract managers, service delivery managers, quality assurance teams, and commercial analysts. The net headcount reduction is significantly smaller than the business case projected.

3. The Knowledge Drain Nobody Measured

The most damaging consequence of the outsourcing wave is the one that will take longest to become visible. When an organisation transfers its IT operations to a third party, it does not simply move tasks — it transfers institutional knowledge. The understanding of why a system was designed a particular way, which business rules are encoded in logic rather than documentation, where the fragile dependencies lie, what was tried before and failed — all of this resides in the heads of the people who built and maintained the systems.

Redundancy programmes and natural attrition are now removing these people from the organisation. Some are taking early retirement. Others are moving to the vendor firms themselves, where their knowledge commands a premium. A few are staying on in retained teams, but their roles have shifted from doing the work to overseeing the work — a fundamentally different skill that not all of them possess.

The result is an organisation that is progressively losing the ability to make informed decisions about its own technology estate. It cannot accurately assess the risk of a proposed change, because the people who understood the risk have gone. It cannot challenge a vendor's estimate, because it no longer has the technical depth to know whether the estimate is reasonable. It cannot set strategic direction for its systems architecture, because the architectural knowledge now belongs to a supplier whose commercial interest may not align with the client's long-term needs.

*“The organisation that cannot challenge its vendor's estimates
has already lost control of its programme costs — it simply does
not know it yet.”*

4. The Programme Management Consequence

For those of us who manage programmes, the outsourcing wave is creating a particular challenge that deserves honest examination. The skill set required to manage an outsourced programme is fundamentally different from the skill set required to manage an internal one.

Internal programme management is, at its core, a leadership discipline. The programme manager motivates teams, resolves conflicts, makes trade-off decisions, and maintains momentum through direct engagement with the people doing the work. The relationship is hierarchical but human.

Outsourced programme management is a commercial discipline. The programme manager manages a contract, monitors SLAs, negotiates change requests, and escalates disputes through governance forums. The relationship is contractual and adversarial — not because either party intends it to be, but because the incentive structures make it so. The vendor is incentivised to maximise revenue from changes and to deliver the minimum that satisfies the contract. The client is incentivised to extract maximum value from the fixed price. Every interaction carries a commercial subtext.

Internal Programme Management	Outsourced Programme Management
Direct authority over delivery teams	Indirect influence through contract levers
Trade-offs resolved through judgement	Trade-offs resolved through commercial negotiation
Risk managed through team knowledge	Risk managed through SLA measurement
Changes absorbed through team flexibility	Changes processed through formal change control
Success = delivered outcomes	Success = contractual compliance

The generation of programme managers now being trained in outsourced environments is learning the second set of skills, not the first. They are becoming expert at contract management, vendor governance, and commercial negotiation. These are valuable skills. But they are not the skills that will be needed when — not if — organisations recognise that they have outsourced too much and need to rebuild internal capability.

5. What Should Concern Us Now

None of this is an argument against outsourcing. There are functions and activities where external delivery makes clear sense — commodity infrastructure management, standardised testing, high-volume transaction processing. The economics are sound and the risks are manageable.

The argument is against the indiscriminating application of outsourcing as a cost reduction strategy, driven by business cases that measure what is easy to count and ignore what is difficult to value.

Three questions should be on every programme board's agenda for any outsourcing initiative currently in flight or under consideration:

1. What knowledge are we transferring, and can we afford to lose it? Not all knowledge is equal. The ability to process a batch run can be transferred with minimal risk. The understanding of why the batch run was designed that way, and what happens to downstream systems when it changes, is a different matter entirely. Organisations need a rigorous assessment of which knowledge is commodity and which is strategic — and they need to make that assessment before the people who hold the strategic knowledge have left.
2. What is our true retained capability, and is it sufficient? The retained organisation — the team that stays behind to manage the vendor relationship — is often sized by cost rather than by need. A skeleton team of contract managers and service delivery leads may be commercially efficient, but it is operationally dangerous if it lacks the technical depth to challenge vendor decisions, assess risk, or set architectural direction.
3. What is our exit strategy? The contracts being signed today are typically five to seven years in duration. The implicit assumption is that the relationship will continue indefinitely. But markets change, vendors merge, service quality degrades, and strategic priorities shift. An organisation that has transferred its operational knowledge to a vendor and then allowed its internal capability to atrophy has no credible exit option. The switching cost is not just commercial — it is intellectual. Rebuilding the knowledge that was lost may take years and cost more than the outsourcing saved.

6. The Uncomfortable Truth

The outsourcing wave will not reverse. The economics are too compelling and the institutional momentum too great. But the organisations that emerge from this period in the strongest position will be those that outsourced with precision rather than ambition — that distinguished between the work they could safely externalise and the knowledge they could not afford to lose.

The uncomfortable truth is that many organisations made that distinction too late, or not at all. The savings on this year's profit and loss statement are real. The cost of rebuilding the capability that was given away will appear on someone else's budget, in some future year, under a different programme name. By then, it will be called a transformation — not a recovery.