Chapter XVI

IT Offshoring:
A German Perspective

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Abstract

Increasing competition in globalized markets drives IT offshoring worldwide. In the United States, the relocation of IT activities and processes to low-wage countries like India is already an established business practice, resulting in their leading position in the field of IT offshoring. However, at present, offshoring is gaining increasing recognition in European countries like Germany. A number of German major enterprises are already involved in or are planning offshoring initiatives, while numerous small and medium enterprises (SMEs) are currently considering how best to take advantage of offshoring. In consideration of this development, the following chapter examines company- and economy-related drivers and economic effects of the rising trend to IT offshoring in Germany as well as possible responses by German companies and policy makers.
Introduction

Excellent skills and sufficient capacities in low-wage countries (e.g., India), along with an increasing cost pressure due to global competition, have fortified the business trend to IT offshoring. U.S. companies, for instance, have outsourced IT projects to low-wage countries since the late ’80s. Nowadays, in the United States, it is automatically assumed during large bid invitations that a service provider achieves its cost advantage, at least partially, by the use of offshore resources.

At present, established business practices from overseas are finding growing recognition in Europe. According to Farrell (2004a), 40% of Western Europe’s 500 largest companies have already begun moving IT service jobs abroad. In Germany, more and more companies have reported on offshoring services in the past months. As an example, German companies’ spending on research and development in foreign countries averaged out at 23 billion euros per year between 1995 and 1999, which jumped to approximately 35 billion euros per year in 2000, thereby showing a rising tendency (Mertens, 2004).

As a result of the growing IT offshoring trend in Germany, the fear of job losses on a grand scale has encountered strong resistance to offshoring in the German public. The announcement by numerous companies to relocate a remarkable share of their jobs to countries in Asia and Eastern Europe intensified these fears even more. For instance, in July 2003, IBM published plans to move a great number of their jobs offshore until 2015. Siemens, which already operates a software development center in Bangalore (India), also plans to expand their offshoring and nearshoring activities (Boes & Schwemmle, 2004).

According to Boes and Schwemmle (2004), 10,000 highly skilled IT service jobs are jeopardized by offshoring in Germany alone. Therefore, the discussion about offshoring attracts vast attention, both in the United States and in Germany. In the U.S. election campaign, for instance, IT offshoring was a major topic and triggered a new wave of protectionism. Even in Germany, parts of the political left-wingers encouraged protectionism in an attempt to prevent the relocation of IT service jobs to countries like India or Russia (Schaaf, 2004).

The current debate about IT offshoring invokes emotional responses in Germany. According to Schaaf (2004), the public perception of IT offshoring and the real facts about offshoring strongly diverge from one another.

Before possible impacts of IT offshoring on the German economy can be discussed in the following, a common understanding of the term “offshoring” has to be assured. According to Schaaf (2004), IT offshoring refers to the relocation of IT activities and processes to foreign countries, mainly low-wage countries. The different types of IT offshoring are illustrated in Figure 1. In many cases, offshoring projects are performed by external service providers (“offshore outsourcing”). However, in some instances, offshoring services can also be rendered by subsidiaries, joint ventures or strategic alliances (“captive offshore outsourcing”).

The following section examines the economic effects of IT offshoring in Germany and possible responses by German companies and policy makers. To start off, section two
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