

Saimaa University of Applied Sciences  
Faculty of Business Administration, Lappeenranta  
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**IMPROVEMENT OF OUTSOURCING  
INFORMATION TECHNOLOGY SERVICES FROM  
OTHER COUNTRIES TO FINLAND**

Bachelor's Thesis 2011

## ABSTRACT

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This thesis examines the possible suggestions for improving outsourcing of information technology (IT) services from other countries (Russia and Estonia) to Finland. The objective of this study is to describe the general view of the trendy concept of IT outsourcing and represent information of different IT outsourcing markets, more specifically of Finland, Estonia and Russia.

The study's primary purpose is to study two case companies with a background of the current market situation and suggest concrete points of improvement of outsourcing IT services from other countries to Finland.

In the theoretical chapter, the concepts and theories of IT outsourcing, a service provider, and different IT outsourcing markets are defined. Also this chapter includes the background information of the two case companies and represents a comparison of Russian (non-European) and Estonian (European) outsourcing.

The data collection method of this thesis is a questionnaire. The experimental part of the study describes the questionnaire. The questionnaire was designed on the basis of the today's companies performance.

The final information has been analyzed from the questionnaires' answers and the important findings have been presented.

In the conclusion section of the thesis, the research conclusion and recommendations have been presented for the two case companies.

Key words: IT Outsourcing, IT Outsourcing Markets, Service Provider

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# **1 INTRODUCTION**

The main objectives of every company are to promote a profitable and sustainable business activity that meets the customers' needs, and to gain the competitive advantage. To achieve these objectives very often companies deliver some of their functions to an external provider. This process is called outsourcing. This study focused mainly on information technology (IT) outsourcing, as this kind of outsourcing is widespread in many countries now (e.g. Estonia, Russia).

## **1.1 Background**

Over the past few years IT outsourcing has become a popular trend. With the outsourcing, a large amount of resources and attention that might fall on the shoulders of management professionals can be used for more important, broader issues within the company. What benefits does the company get from IT outsourcing and how to improve outsourcing of IT services? This research tries to answer these questions.

According to a Russian analytic and consulting company, In4media, outsourcing to Russia becomes more and more popular. The commercial market of IT outsourcing has grown by 21% in 2010. It is expected that in 2011 the current growth rates will increase to 25-30%.(Abramov 2011).

Another popular outsourcing center is Estonia. High quality of services and cost effective production attract customers to Estonia – a traditional outsourcing centre for the Northern European countries. It is relatively easy to do business in Estonia because of its political and economic environment. (IT outsourcing news from Central and Eastern Europe 2010).

Many IT specialists from Russia and Estonia are outsourced to work in Finland. That is why it is important to analyze reasons for IT outsourcing from other countries to Finland.

## **1.2 Topics of the research**

The purpose of this study is to study two case companies, Tieto (Russia-Finland) and VMP (Estonia), with a background of the current market situation,

and understand why outsourcing IT services from other countries to Finland has become more and more popular.

One of the objectives of this study is to describe the general view of the trendy concept of IT outsourcing. Outsourcing has already become an acknowledged method of increasing the efficiency of a company's work worldwide. The top-level analytic agencies confirm that a long-term outsourcing strategy is necessary for successful competitive business development and adaptation to swiftly changing market conditions.

The thesis will include a description of IT outsourcing, that will help us to understand the importance of IT outsourcing and show how the whole process works. The study also compares the difference in providing IT outsourcing in Russia (non-European Union country) and Estonia (European Union country).

The results of the research might give some recommendations for the companies to improve their business in the outsourcing field.

### **1.3 Choice of research method**

The study consists of the theoretical study and the experimental research of the IT outsourcing as a phenomenon. The theoretical data will make the whole concept of IT outsourcing clearer, show the statistics and help to make conclusions. The Internet and literature will provide the information.

The experimental part of the study will consist of the description of questions to two case companies (Tieto and VMP), reasons for asking them, and an analysis of the answers. The questions for both companies will be the same.

Conclusions will be made by comparing the theory and the results of the experimental study.

### **1.4 Scope of the study**

In this study the theoretical definitions of IT outsourcing will be used as the theoretical basis. They are discussed in the beginning of the study. These

definitions are needed to make the whole picture of the process of outsourcing IT services clearer.

This research will concentrate only on IT services, other types of outsourcing will not be included in this research. As this thesis focuses on economical aspects of IT-outsourcing, no technical point of views will be discussed.

The research suggests concrete points of improvement for outsourcing IT services from other countries to Finland. This study is limited to certain countries, and describes how the outsourcing of IT services is carried out in the European Union and non-European Union countries, more specifically in Russia, Estonia and Finland.

The organizations interviewed are located in Estonia and Russia. The main activity of these companies is outsourcing. The study compares the IT - outsourcing also in EU and non-EU countries. This study will also give recommendations for improving the IT outsourcing.

### **1.5 Structure of the study**

This thesis contains six main chapters. The structure is presented in Figure 1. The theoretical section of the thesis is divided into seven chapters, including a general definition of the terms related to IT outsourcing. The theoretical part also includes brief historical background of IT outsourcing which will show how outsourcing of IT services was developed. This chapter clarifies typical IT outsourcing services and the size of the IT Outsourcing market. This information represents the importance of IT outsourcing in our time. This chapter contains information about advantages and disadvantages of IT outsourcing and clarifies how the whole process of choosing a service provider is carried out.

The third part presents information of different IT outsourcing markets. For this research these markets are Russia, Estonia and Finland. This chapter illustrates the present situation of IT outsourcing markets in different countries.

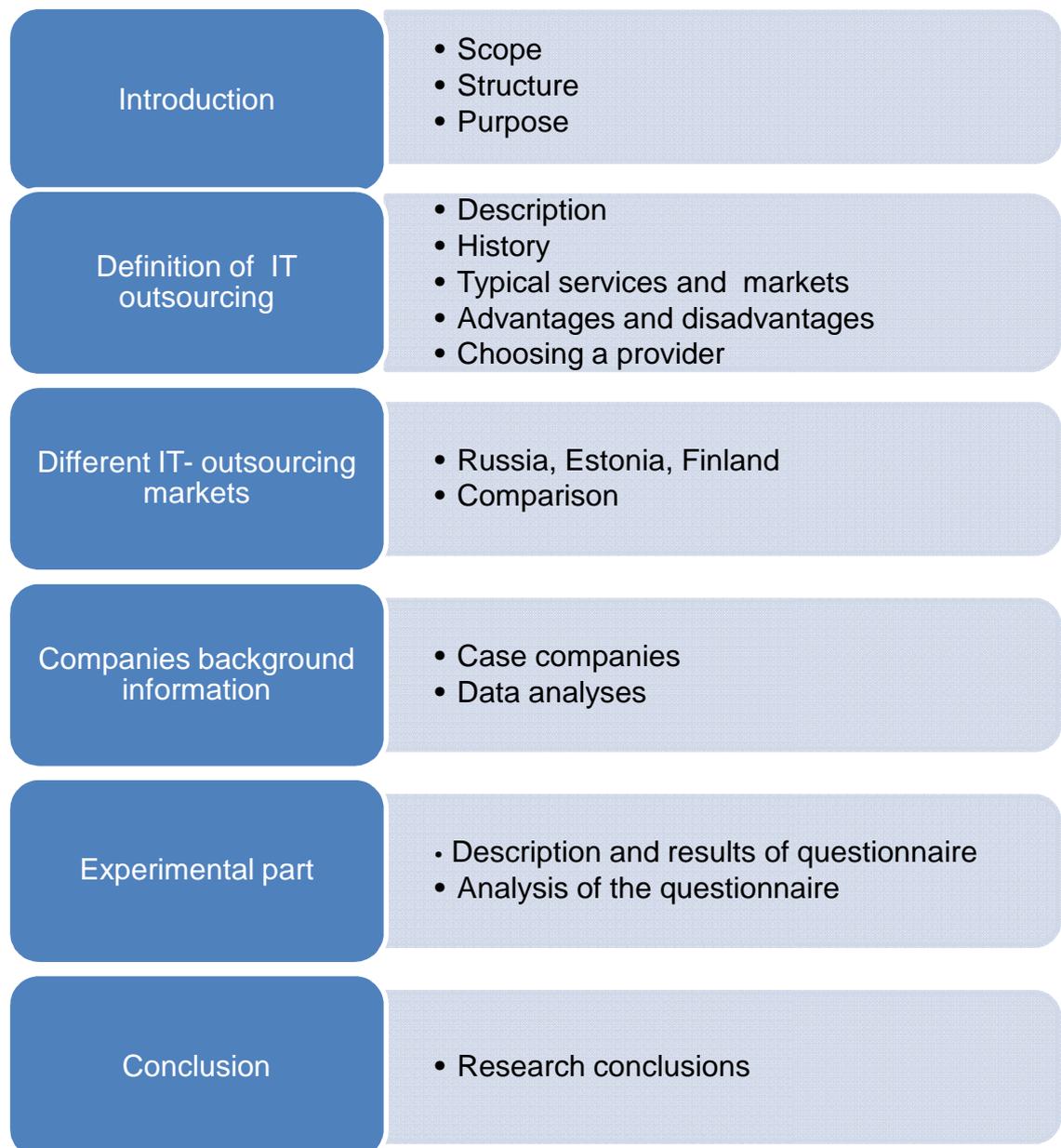
The fourth part of the thesis is devoted to two companies' background information (Barona and VMP). This chapter clarifies products and services,

customers, and the markets of these companies. This chapter also contains a description of IT outsourcing from Tieto and VMP. The purpose of this part will be to give the reader the possibility to compare Russian (non-European Union) and Estonian (European Union) outsourcing.

The Experimental part describes the questions and the results of the questionnaire. Finally, there will be an analysis of the answers from the two case companies, which will help to make a conclusion.

The conclusion presents the results and the recommendations about how to improve the outsourcing of IT services.

Figure 1. Structure of the study



## **2 GENERAL DEFINITION OF THE TERMS RELATED TO IT OUTSOURCING**

There are many different definitions of IT outsourcing, but all of them are similar. In this chapter will be given one of these definitions.

### **2.1 Description of outsourcing of IT services**

Today it is very difficult to find a company which wouldn't use information technology in their daily work. Tasks such as equipment maintenance and customization, software installation, and maintenance worthy of notice in virtually every company, regardless of size, type of activity and number of employees. While having rapid growth, it is really important to expand the range of used information technology. For a small business, it is very expensive and time-consuming to ensure adequate levels of business development. Therefore, many companies are looking for cost-effective ways to solve this problem. One option is to send technical questions to a third party where these services are the key business. This is called outsourcing. So let's try to understand what the outsourcing of IT services means.

One of the definitions of IT outsourcing is given by Elizabeth Sparrow (Successful IT outsourcing 2003, pp.1-2) as: " the practice of handing over the planning, management and operation of certain functions to an independent third party, under the terms of a formalized service level agreement".

There are many types of outsourcing. Initially, the outsourcing was developed in auditing and consulting companies. But the impetuous development of IT technologies led to the creation of the new sort of this concept – the outsourcing of IT-services (Hijazi 2005). Now IT outsourcing has become one of the most popular business processes. Why is this so?

In order to survive in the competitive market, a company has to work with a huge amount of heterogeneous data. With today's conditions on the market, then there is shortage of highly-qualified personnel, and IT outsourcing helps the company to deal with huge amounts of information.

IT outsourcing helps the company to concentrate on its key business, save expenses on IT-solutions, and be assured that they get high-quality service from competent specialists in the IT sphere.

## **2.2 History of IT outsourcing**

When first computers appeared it was very expensive to support business functions. Many organizations couldn't afford to own or use their own computers. The first computer bureaus were established in the 1960's. These bureaus sold mainframe time to other organizations for data processing. This business proved to be very successful. It was the first example of IT outsourcing. (Sparrow 2003, p.2).

In the 1970's, the first minicomputers and later microcomputers were introduced. Hardware became affordable and even small companies considered purchasing their own IT assets. Soon, due to standard software packages, organizations were able to set up their own systems with little programming effort. Companies invested lots of money to update their hardware and application systems as having modern computers was very prestigious. (Sparrow 2003, p.2).

With the growth of IT companies outsourcing became a necessity. Managers didn't pay so much attention to technical details of the IT infrastructure any more. They were more engaged in the outcome of their investments in IT.

According to Elizabeth Sparrow (2003), "the first major outsourcing initiative to receive worldwide publicity came in 1989 when Eastman Kodak hired outsiders to buy, operate and maintain its information processing system".

In the late 1980s/1990s, many national governments wanted to make radical changes as they encouraged public sector organizations to adopt the efficient techniques of the private sector. Computer Sciences Corporation (CSC), EDS, and IBM were the main companies at that time which settled the largest bargains. (Sparrow 2003, pp.4-5).

During the dotcom boom, many small and medium-sized IT outsourcing businesses emerged. Their services were much cheaper and faster. (Sparrow 2003, p.5).

In the IT market today there are many different IT outsourcing companies who can offer a wide range of services. This market is rather big and continues to grow from day to day.

### 2.3 Typical IT services

IT Outsourcing suggests a variety of IT services. In Weill and Vitale research (Weill & Vitale 2001) there is a list of the seventy IT infrastructure services needed for e-business. It consists of nine categories. (See Table 1)

№	Areas	Infrastructure services
1.	Applications Infrastructure	a) internet access for employees b) development of e-mail d) applications management for e-business (common standards) e) service payment transactions (Electronic funds transfer), etc.
2.	Communications Management	a) communication networks services b) electronic data exchange with suppliers and clients of the firm c) electronic support of group work, etc.
3.	Data Management	a) management key information regardless of application b) consultation on data management c) information storage, etc.
4.	IT Management	a) tools for mass data processing b) information systems project management c) Service Level Agreement, etc.
5.	Security	a) information system security policy b) recovery planning for business applications in case of failure, etc.
6.	Architecture and Standards	a) development of data standards (communication standards, application standards, operation standards) b) application of I data standards (communication standards, application standards, operation standards) etc.
7.	E-Channel Management	a) e-shop b) web-sites c) mobile communication, etc.

8.	IT Research and Development	a) identifying and testing new technologies for business b) evaluation of proposals to introduce new information systems
9.	IT Education and Training	a) training and using IT b) executive management training for value creation through the use of IT

Table 1. IT infrastructure services for e-business. (Weill & Vitale 2001, p.80).

The company decides which IT services it will outsource. It can be for a market competitive advantage. In Weill and Vitale research (2001, p.77) there is an example of IT infrastructure services needed in building a new Web-based housing loan system. It turned out that a particular bank needed to have several IT infrastructure services: mainframe, server processing, customer database, etc. to reduce significantly the time and cost to build the loan system. The most popular IT functions to outsource have been defined by Olavsrud (2010). (See Figure 2)

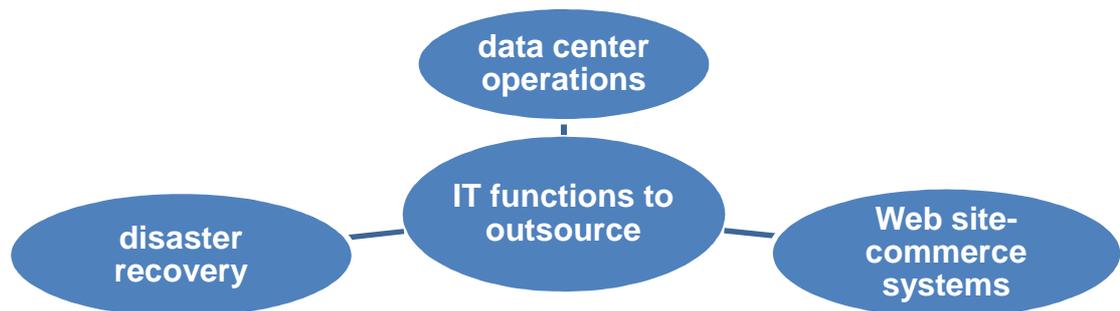


Figure 2. The most popular IT functions to outsource. (Olavsrud 2010).

Among the fastest growing outsourced IT functions are: Help desk, desktop support, data center operations, and Web site/e-commerce systems. IT outsourcing can be especially beneficial to small and medium enterprises. Large organizations usually outsource the help desk. Application maintenance, application development and data network operations service providers are making the smallest outsourcing gains. Application development is still the most frequently outsourced function. (Olavsrud 2010).

## 2.4 Size of the IT outsourcing market

The trendy concept of IT outsourcing continues to grow from year to year. Most of the outsourced business is located in developing countries like India. The reason is that the work force is a lot cheaper compared to developed countries. If someone can do the same work for less money why not hire?

The size of the IT outsourcing market is rather big. If we take a look at Vertical Market Segmentation, outsourcing will be among the largest global vertical markets. (Strategic outsourcing, global trends 2003). (See Figure 3)

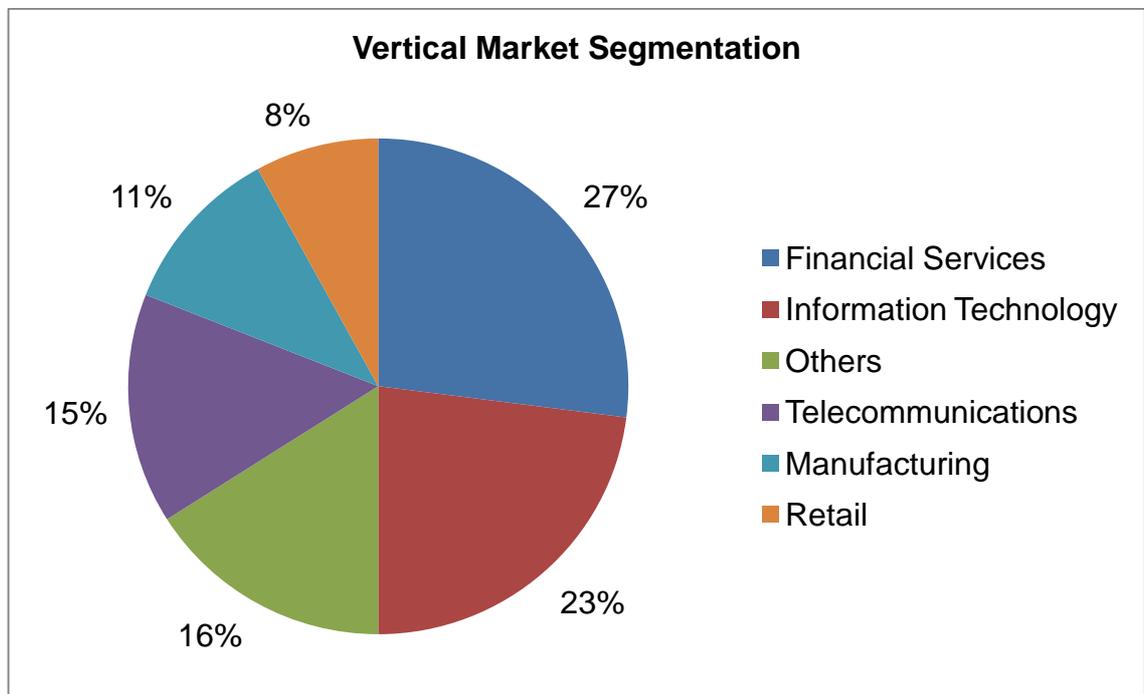


Figure 3. Vertical Market Segmentation. (Strategic outsourcing, global trends 2003).

The figures show that all major sectors are involved in outsourcing, although financial services are on the winning side , but IT outsourcing takes a second place in the outsourcing market.

According to XMG Global senior analyst Vincent Altez (XMG Global ICT Research and Advisory 2009), the global outsourcing market ended 2009 with a

total revenue of US\$373 billion, or 14.4% higher than the US\$326 billion recorded in 2008.

Analysts estimate further growth of the top three offshore countries, namely: India, China and the Philippines. In 2009 India had 44.8% market share of the world outsourcing market, the market share of China was 22.9% and Philippines had 6.9%. According to analysts, the positive trend of IT outsourcing will continue, because many companies are trying to recover after the negative impact of the global economic crisis. (XMG Global ICT Research and Advisory 2009).

A leading international research and consultancy firm, Gartner, made a list of the world's top 30 destinations for IT outsourcing in the year 2008.

The firm used 10 criteria:

1. language
2. government support
3. labor pool
4. infrastructure
5. educational system
6. cost
7. political and economic environment
8. cultural compatibility
9. global and legal maturity
10. data and intellectual property (IP) security and privacy

The leading IT outsourcing destinations are: the undisputed leader in offshore services — India — and the greatest challenger in terms of potential scale — China. Others are Argentina, Brazil, Canada, Romania, the Czech Republic, Poland and others. (Gartner 2008). If comparing with the statistics of 2004, central IT outsourcing markets are the same. (Frost & Sullivan 2005). (See Figure 4)

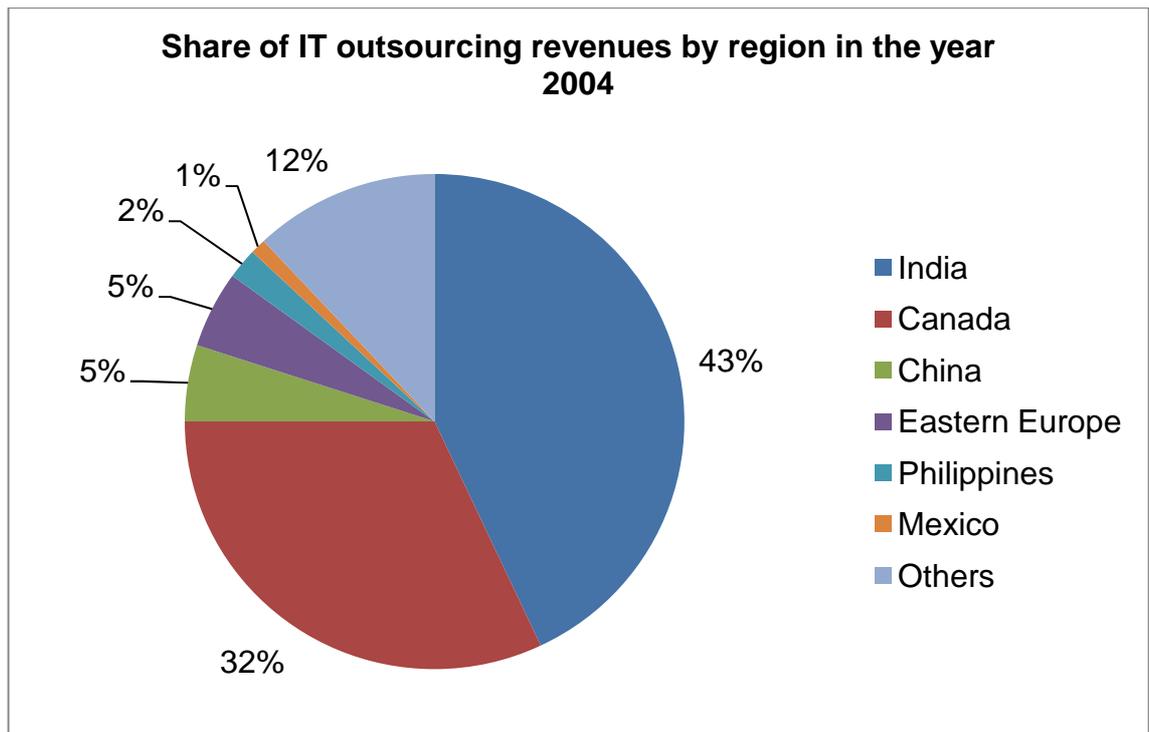


Figure 4. Share of IT outsourcing revenues by region in the year 2004.

Only one thing that has changed is that Canada doesn't have that big market share anymore. According to Gartner research (Gartner 2008): "The key evaluation criterion of cost was where Canada fared the worst ("fair") compared with "good" or "very good" ratings for all other countries in the region." At the same time, Canada still has an attractive IT outsourcing market.

## 2.5 Reasons for IT outsourcing

There are numerous reasons for outsourcing IT services. These reasons can vary a lot. The incentives for outsourcing are discussed in this chapter.

### 2.5.1 Focus on core business

For many companies it is difficult to focus on its core business. Richard Poole, business director at the technical agency, Conchango, explained that the bigger the company, the harder it is to focus on its core operations. (Brooks 2004).

IT outsourcing helps companies to focus more on development efforts, and thus have a competitive advantage over other companies. After delegating IT

services to a vendor company, it can be easier to make the right strategic decisions that directly affects the work, because there is more time to concentrate on core functions within the company. (Kamel 2003, pp.117-118). Companies get the opportunity to concentrate all their resources on their core business to add additional value to products or services they offer.

### **2.5.2 Cost savings**

Cost savings is one of the most important objectives in the whole process of IT outsourcing. Cullen & Willcocks (2003, p.17) have said that "over half of organizations across the globe are outsourcing at least 20% of their IT budgets".

Taking into account the fact that IT is one of the most expensive functions of an organization to set up and manage (Barthélemy 2001), it becomes clear why so many companies are using IT outsourcing. For companies, it is profitable to transfer some IT services to a service provider. In a survey made by the Outsourcing Institute, companies noted that they saw a 9% reduction in costs through using IT outsourcing. (Lederer et al 1998).

At the same time, outsourcing will not be profitable if the main purpose of this process is only cost savings, because in this case the company usually loses control on outsourced operations. According to Paul Smith (Simpson 2007), Global Managing Director, Outsourcing and Software Development, Harvey Nash, "It is clear that IT outsourcing is here to stay. No longer seen as just a cost-cutting exercise, more and more businesses are now reaping the strategic benefits and allocating their budgets accordingly."

There must be long term goals for both the customer and the vendor and both sides should find benefits in this process and contribute to the development of a partnership between them. Choosing the right outsourcing partnership form guarantees the continued success of the company. (Berkling et al 2009, p.34).

### **2.5.3 Improvements in service and quality level**

The technological environments change quickly, and the company has to keep up with the latest things. The outsourcing vendor will be able to provide more proficient services. Outsourcing is the easiest procedure when the company needs special technical skills or have to make quicker deliveries to customers.(Lederer et al 1998).

Companies usually enter outsourcing when they are confident that their service provider will offer high-class service (Sparrow 2003, p.22). Companies' non-core business functions will be performed efficiently by its outsourcing provider, while core functions can be efficiently carried out in-house. According to Norris Overton (Lederer et al 1998) , vice president of reengineering for AMTRAK, "partnering with an organization with world-class capabilities can offer access to new technology, tools, and techniques that the organization may not currently possess: better career opportunities for personnel who might move to the outsourcing provider, more structured methodologies, procedures, and documentation; competitive advantage through expanded skills."

### **2.5.4 Flexibility and control**

To adapt to a rapidly changing market, companies need good flexibility and control of the actions. This flexibility and control can be achieved by outsourcing. The capability of an internal IT function is limited by the skills of its IT staff and the technology. It is also difficult for companies to control the changing environment. These problems can be solved by outsourcing, as the outsourcing IT company provides the company a wide range of skills, resources etc. In this way companies can find a solution to a problem faster if circumstances on the market change (e.g. change on demand) , because everything is under control (Lederer et al 1998). If a company maximizes both flexibility and control it will maximize its competitive advantage.

### **2.5.5 New business development**

With IT outsourcing, new business opportunities arise for the company, because the company has more time to focus on strategic development rather than spending too much time on solving operational problems (Sparrow 2003, p.19).

As the market demand changes rapidly and the environment becomes more competitive, companies have to focus on their business development as a way to gain competitive advantage. Outsourcing helps companies to keep pace with new technologies, skills etc., while internal staff can concentrate on development issues within the company. (Lederer et al 1998).

### **2.6 Reasons against IT outsourcing**

IT outsourcing has benefits, but there are a number of reasons why a company should avoid outsourcing.

#### **2.6.1 Loss of flexibility and control**

Flexibility is very important for the future company development, and the outsourcing very likely restrains the flexibility of IT services. This is because the outsourcing provides only services that are specified in the contract. So the flexibility of moving to new technologies can be lost and if not lost, the service provider may ask for additional charge, because the company will move to new, more cost-effective technology. According to Wiley & Sons (1995): "Without the flexibility of having an internal IT capability, it might prove difficult (and/or expensive) to have the vendor provide a changed set of IT services." (Lederer et al 1998).

With the IT outsourcing the company loses privacy for the outsourced services, and it becomes impossible for the company to control all the processes of the service provider for the outsourced IT services (Tho 2005, p.15). To avoid such problems the company has to ask for frequent reports and analyze the evolution of the outsourced service constantly.

### **2.6.2 Costs**

A company using first time IT outsourcing might not be aware of costs associated with contracting, transitioning data to the vendor, software license transfer fees, etc. Companies don't expect such costs. It is impossible to specify all the details in the contract. As a result, companies have less savings than they expected. Such costs are also called unexpected costs and management costs.(Bahli & Rivard 2003, according to Schniederjans M. 2007, p.252).

Very often companies find out that their primary vendor is not working on their projects, but has found another unknown small company do it. This occurs because IT vendors often subcontract portions of their work to smaller companies. A survey shows that 36% of outsourcing contracts involve subcontracting. In this case there is always the possibility to forbid the use of subcontracting. It must be stated in the contract (Informationweek 1997, according to Lederer et al, 1998). According to Barthelemy (2001), in a survey of 50 companies, 14% of outsourcing operations were unsuccessful. (Schniederjans M. 2007, p.252).

John Wiley & Sons (1995) suggests that companies think about whether they can achieve the same results without outsourcing. Maybe the company can reduce IT costs through data center consolidation, resource optimization etc. (Lederer et al 1998).

### **2.6.3 Loss of technical expertise**

While using outsourcing of IT services, the company is in jeopardy of losing at least some of its technical expertise. IT outsourcing decisions are usually decisions that result in long-term contracts. But IT develops so rapidly that outsourcing actually locks companies into older technologies (Lederer et al 1998). Client's employees can't adapt to new technologies. As a result, the company can't develop IT services by itself to meet the demand of the technology environment. (Schniederjans & Schniederjans 2007, p.252).

#### **2.6.4 Security risks**

When the company manages an internal IT department it can be confident that the IT department works only for this company. Serious security problems may arise with a service provider. The more access to a company's data base is given to a vendor, the greater the probability is that confidential information can be leaked. The company cannot know that its service provider may also work for the company which is a direct competitor. (Beulen et al 2006, p.24).

For any company it is important to clearly define the confidentiality objectives in the agreement.

#### **2.7 Choosing a service provider**

Outsourcing certain services and functions is one way a company finds benefits for its business. There are several important considerations to take into account before using the help of IT providers.

##### **2.7.1 Determining the future prospects**

Every company has its strategy, objectives and goals. According to the strategy and goals, the company outsources the services which will meet further development perspectives.

Before outsourcing certain services the company has to identify which functions are needed to be outsourced for the company's successful future performance. The company asks itself several questions, for example: " Will the IT service provider grow with the company?". The company is usually interested in finding out if the outsourcing provider is planning to increase the number of services in future. The vendor should provide continuous support to the company and develop with it (Jenkins 2010).

The company has to understand whether it should select total or partial outsourcing. In that case company evaluate the total costs of outsourcing function, determine reasons for and against outsourcing. (Cleland & Ireland 2006, p.290).

For the company, outsourcing is an opportunity to grow and build new capital, and to become more productive and competitive. After determining these options, the company should make the decision about which services it should outsource.

### 2.7.2 Evaluation

Some outsourcing vendors are so cautious about their reputation that it is very difficult to find reliable information about the services they provide, and the company can make a wrong choice not knowing all the facts about the outsourcing providers. The problem is that there are no special standards which regulate this business. The company has to take great care when making such decisions. (Managing Accounts Payable 2009).

There are some standard criteria to start the evaluation. They are described in Table 2.

No	Criteria for selecting	Description
1.	General profile	<ul style="list-style-type: none"> <li>• Name of Service Provider</li> <li>• Location</li> <li>• Domain expertise</li> <li>• Years of experience in domain</li> <li>• Membership - organisations such as National Association of Software and Service Companies etc.</li> </ul>
2.	Clients	<ul style="list-style-type: none"> <li>• Client-base in regions</li> <li>• Previous and current clients of service provider</li> <li>• Client referrals/testimonials etc.</li> </ul>
3.	Technology and Processes	<ul style="list-style-type: none"> <li>• Software, Integrated Suites</li> <li>• Database systems</li> <li>• Secure development environment</li> <li>• Communication technologies such as email, chat, video-conferencing software, etc.</li> </ul>
4.	Human Capital	<ul style="list-style-type: none"> <li>• Profile of managers including qualification and experience</li> <li>• Number of employees</li> <li>• Qualifications and skill-set of employees, experience of employees</li> </ul>

5.	Infrastructure	<ul style="list-style-type: none"> <li>• Office space</li> <li>• Hardware requirements including servers, workstations, peripherals</li> <li>• Telecommunication links such as broadband internet and phone links</li> </ul>
6.	Pricing	<ul style="list-style-type: none"> <li>• Cost of solution</li> <li>• Terms of payment</li> </ul>
7.	Cultural Fit	<ul style="list-style-type: none"> <li>• Workplace ethics</li> <li>• Responsiveness to client needs</li> <li>• Cultural differences including language</li> </ul>

Table 2. Criteria for vendor evaluation. (How to evaluate Outsourcing Service Providers 2008)

The first criteria the company begins to evaluate about the service provider is its general profile. In this step the most important evaluation factors can be location and domain expertise. Some experts confirm that it is better when a service provider is focused on certain services. In other words it is operating in restricted domains.(How to evaluate Outsourcing Service Providers 2008).

When evaluating clients, technology, human capital, pricing of a service provider, the company should make a clear picture about the vendor's reputation and solutions provided for the client problems. A cultural fit is a very significant aspect, because the more similar culture both parties (client and vendor) have, the greater the success outsourcing services will be. (How to evaluate Outsourcing Service Providers 2008).

### 2.7.3 Negotiations

In the next negotiation step, the company defines the duties of both parties, in other words to share responsibilities. For example, the company defines what resources will be supplied by the company and outsourcing provider, determine issues of governance, etc.(Schniederjans et al 2005, p.57).

To establish a pricing system is very important. Both sides have to state prices for the basic service agreement, for overtime work, and for extra services the vendor may provide.(Schniederjans et al 2005, p.63).

The company has to establish a timetable that will indicate the deadlines within which the vendor performs its work. Both sides should establish flexibility procedures, i.e. determine reasons for change in the outsourcing agreement. Also, some analysts are confident that there should be a bonus system in the contract. It will motivate the provider to perform better and faster. (Schniederjans et al 2005, p.57).

The risks in the contract must be identified, and actions of both parties in the case of possible problems must be agreed upon.

#### **2.7.4 Contract signature**

After all the issues are specified, the company may sign a contract with an outsourcing provider. In a contract must be prescribed all the aspects of and the deadline for the contract.

### 3 DIFFERENT IT OUTSOURCING MARKETS (RUSSIA, ESTONIA AND FINLAND)

There are many different IT outsourcing service providers to choose from. This chapter will describe three IT outsourcing markets: Russia, Estonia and Finland.

#### 3.1 IT outsourcing in Russia

Many independent sources acknowledge that the Russian software market has strengthened its positions in the global market. Some research companies reported different trends in the Russian software development market. The most popular trends are shown in Figure 5.

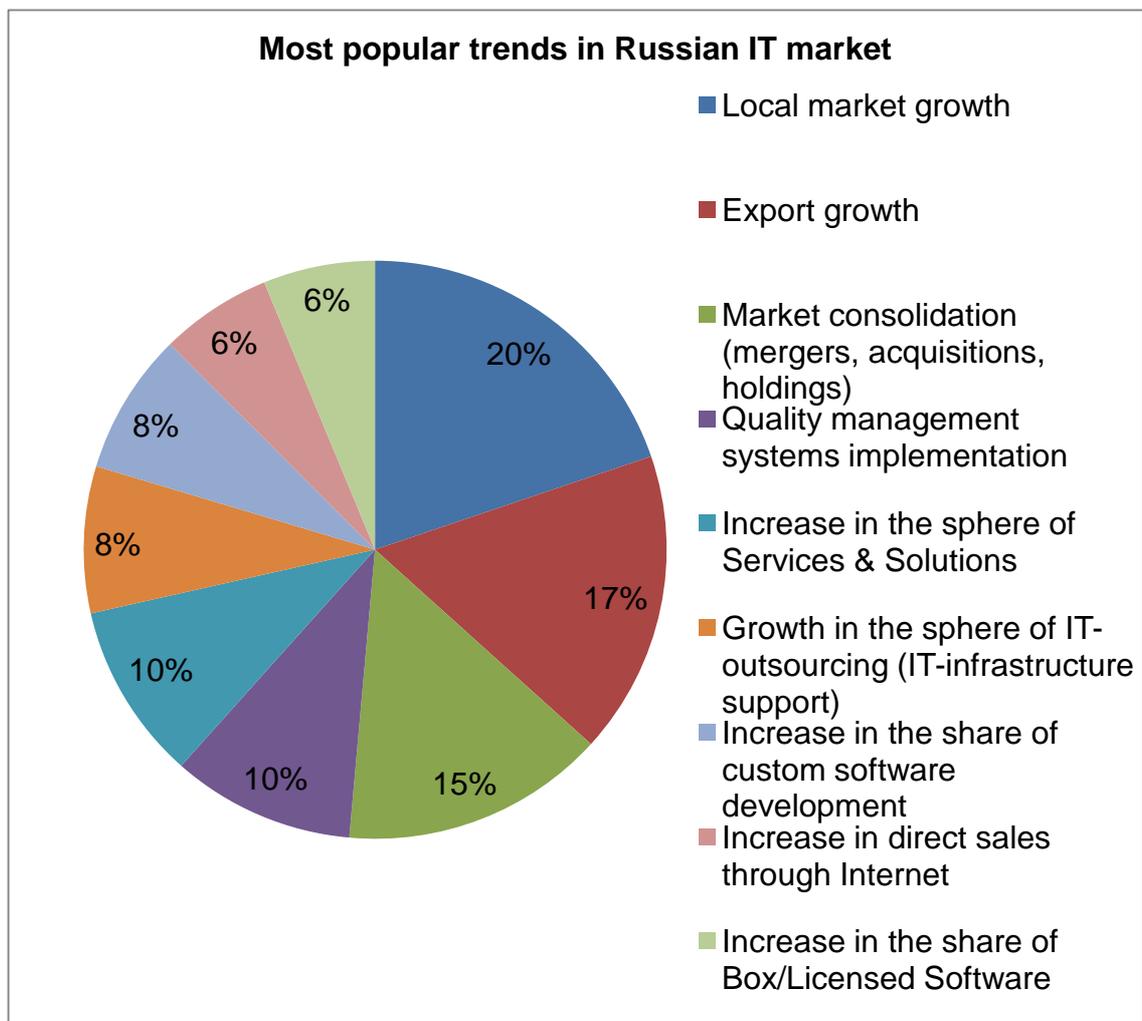


Figure 5. Companies' opinions concerning the main trends in Russian software development. (RusSoft Company 2007).

Local market growth has occurred because the volume of direct investment in Russia has grown rapidly over the last two years. Government policy has changed for the better. Now companies have greater support from the government. Cooperation with the Russian customers became as profitable as with foreign. (RusSoft Company 2007).

Due to political stability and the government's projects on the strategic development of the IT sector, the Russian outsourcing market has become very popular in the last years. The growth of export is one of the main trends in the Russian IT market. (What You Should Know about Outsourcing to Russia 2005).

According to many analysts, Russian IT outsourcing is one of the most rapidly growing segments of the Russian market. Another positive trend is the growing index of implementation of quality management systems and competence in the labor market. Russian outsourcing companies were among the first in Europe to get the CMM/CMMI Level 5 certification to prove the quality of their services. (What You Should Know about Outsourcing to Russia 2005).

The Russian outsourcing market has many IT advantages, but many experts think that the main reason why Russia is an attractive outsourcing area is that this country has high quality personnel. Russia has the third highest per capita number of scientists and engineers in the world. (Sahay et al 2003, p.17).

The Russian IT market is well known for complex programming and application development. Another reason why the Russian IT market is so popular is the cost factor. It is still comparatively inexpensive to outsource IT functions to Russia. (Mechitov 2009, pp.132-133).

The Russian software market has, however, some problems. According to Stephen Lane, an analyst at Aberdeen Group Inc.(Trombly 2003): "The biggest problem with the Russian government and its influence on the country's business culture is a lack of overall business transparency, a complex bureaucracy and restrictive tax, customs and immigration laws. "The

government's financial support in the IT sector is very small in Russia compared with India and China. (Trombly 2003).

Russia is not one of the "big three" software producers, but its market is developing quickly. The McKinsey Global Institute estimates 50-60 % growth per year of the Russian outsourcing programming sector in the early twenty-first century. Such large firms like IBM, Boeing, Motorola, Intel, and Microsoft already operate in Russia. (Sahay et al 2003, p.16).

### **3.2 IT outsourcing in Estonia**

There are three main clusters of Central and Eastern Europe countries with similar market conditions for IT outsourcing. The first cluster includes the leading countries in the IT infrastructure support. The second cluster represents countries with developing markets for IT outsourcing. Countries with recently established markets are in the third cluster.

Estonia represents the second cluster. In this cluster there are countries like Bulgaria, Serbia, F.Y.R., Estonia, Slovakia and Lithuania. According to the CEE IT Outsourcing Review (2010) these countries have "similar growth in IT services exports; increased outsourcing services consumption in the internal market; and growth in the number of providers with foreign capital or partly funded by foreign capital". There is a trend of increasing the number of skilled specialists in these countries. Figure 6. represents the modern trends in the IT outsourcing industry in Estonia.

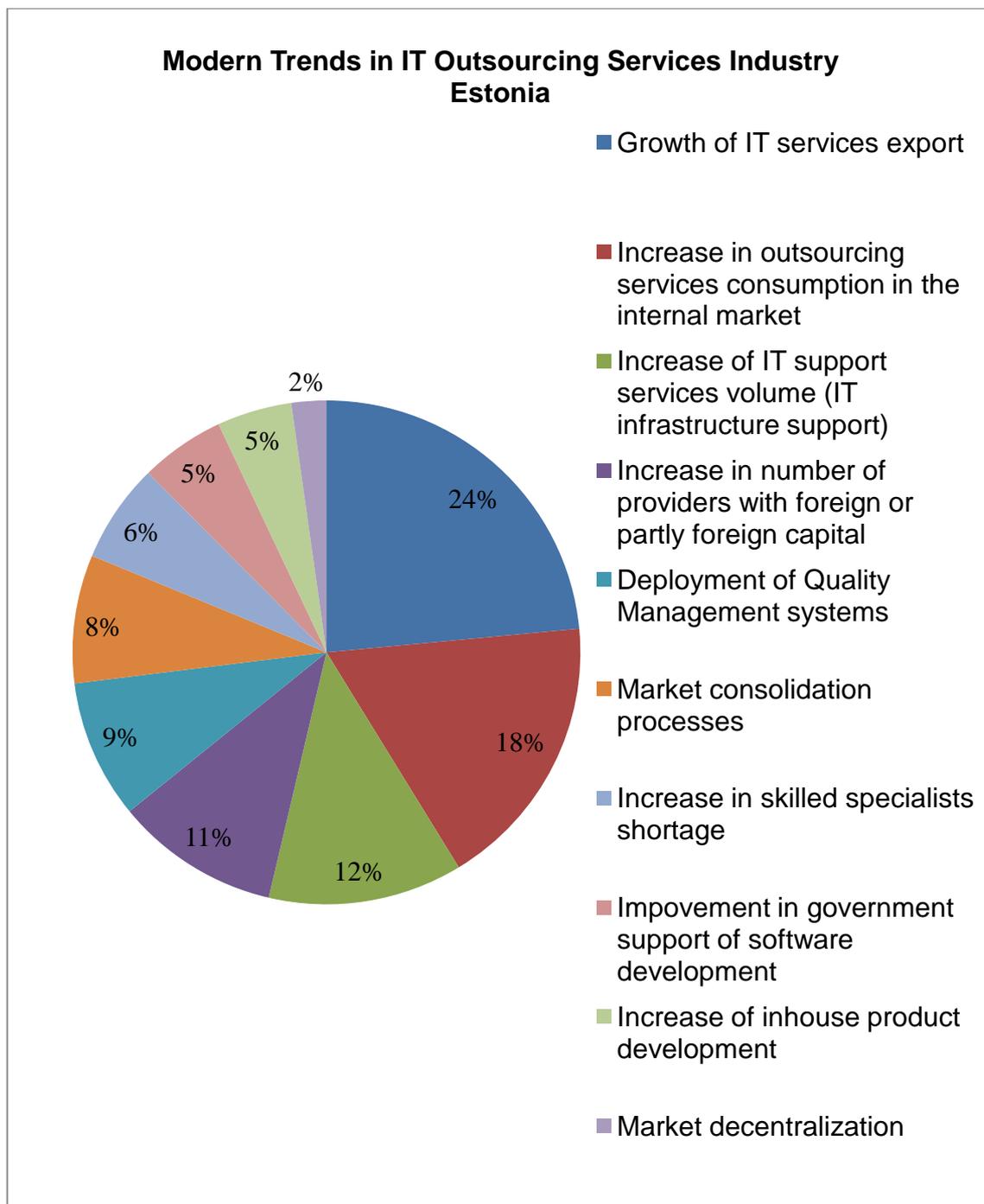


Figure 6. Modern Trends in IT Outsourcing Services Industry - Estonia. (IT Outsourcing Review 2010).

A growth of IT services export is due to high foreign demand. According to Kalvet T. et al (2002, p.20) " most of the rise can be assigned to a single company's activity - Elcoteq Ltd provides 83% of the total Estonian information and telecommunications technology exports and 96% of the telecommunications equipment exports as the statistics for the year 2000

indicates". The largest trade partners for Estonian information and telecommunications technology industry are Finland and Sweden. (Kalvet et al 2002, p.20).

Increase in outsourcing services consumption in the internal market is derived by the government initiatives and local institutions. Liberal government policy and public initiatives in the fields of eLearning and eGovernment contribute to further development of the software industry in Estonia. (Kalvet et al 2002, p.21).

### **3.3 IT outsourcing in Finland**

Finland is a small European country, so the market for IT services is relatively small. Despite this fact, Finland has a very developed IT services infrastructure using modern technologies.(Uday et al 1997, p.290).

The major trends of the Finnish outsourcing market are presented in the report provided by two professors from Finland, Jesus B.& Ilomäki M.(Guo 2005, p.1).

These trends are:

1. Focus on IT outsourcing market by a broader set of players;
2. Increase in managed services;
3. The need to integrate utility computing as part of IT outsourcing;
4. Lack of penetration by offshore players;
5. Building global offshore outsourcing capabilities;
6. Slow shift toward provisioning utility computing.

According to Mr.Belle (Guo 2005, p.2), the IT outsourcing market in Finland has good growth opportunities. Most companies expect to increase their external IT expenses and to reduce their internal IT costs.

The professor noticed that there are some problems concerning outsourcing in Finland. The first problem is connected with the small internal market for software. The reason for this problem is the small size of the country. Other

problems include inability to develop products jointly with local customers and an undeveloped venture capital market. (Guo 2005, p.2).

### **3.4 Comparison of IT outsourcing in Russia, Estonia and Finland**

Sweden's largest technical news magazine, "Ny Teknik", quotes sources within the Gartner Group confirming that in spite of the fact that India is the leading country in IT-outsourcing it has serious competitors, among them Estonia and Russia.(Estonia's advanced IT environment and future outlook gets further recognition 2004).

Russia and Estonia have great potential for IT outsourcing. People in these countries are very well trained and outsourcing there is rather cost-effective. There are common modern trends in IT outsourcing in Russia and Estonia. Both countries have growth of IT services export and local market growth. These countries have high foreign demand and they are ready to implement complex projects.

Finland is the country where the IT industry plays a very important role in economic development. Russia and Estonia can offer a broad scale of IT services for the Nordic businesses. Many Finnish companies outsource some or all of their IT services, because with IT outsourcing they can cut production costs. From Finland's point of view, Russia and Estonia provide some specific benefits as these countries are geographically the closest development centers to Finland.

## **4 COMPANIES BACKGROUND INFORMATION**

There are two IT outsourcing companies: Tieto Corporation, operating in Russia and the VMP Group, operating in Estonia. The difference between the Tieto Corporation and the VMP Group is that the Tieto Corporation is an IT service company and the VMP Group is a human resources provider. The Tieto company is very famous and operates in many international markets. Compared to the Tieto Corporation, the VMP Group has not so many markets, but in spite of this fact is also well known. Both these companies have strong positions in Finland.

### **4.1 Tieto Corporation**

The TietoEnator Corporation was formed by the combination of the Tieto Corporation in Finland and Enator AB in Sweden in 1999. In 2008, the company changed its name to "Tieto". The official name of the company is now "Tieto Corporation". It is one of the largest IT services companies in Europe.

#### **4.1.1 Customers and market**

The Tieto Corporation is the leading IT service company in Northern Europe. The company operates in America (Canada, USA), Asia (China, India, Malaysia) and in Europe (Estonia, Finland, Germany, Russia and 13 more countries). Tieto's main markets are the Nordic countries, Russia and Poland. In addition, the company serves their customers globally in certain areas of expertise and have industry-specific activities in selected countries.(Tieto 2011).

The company operates a total of about 15 data centers, the majority of them in Finland and Sweden. Tieto Corporation has more than 17000 experts. The company's aim is to become a leading service provider creating the best service experience in IT. (Tieto 2011).

Tieto's customers are large and medium-sized organizations in various sectors. These sectors include: Telecom and media, Finance, Industry sectors.

#### **4.1.2 Product and services**

Tieto Corporation serves a variety of industries, including energy, manufacturing and automotive. (Tieto 2011).

Tieto Corporation provides services such as:

- Industry solutions- provide solutions to industry-specific needs;
- Enterprise solutions- offerings, such as Future Office and Financial Value Chain, which help companies to run their daily operations smoothly and integrate corporate-wide information processes;
- Managed services - maintaining, developing and enhancing existing applications under a long-term contract;
- Product engineering solutions - design, development and maintenance of software for customers' products.

#### **4.2 VMP Group**

The VMP company was set up in 1988, and its name was "Varamiespalvelu". This name was closely associated with the staff leasing. The company has strengthened its expertise in this chosen industry. The result is that the company now has a new brand name - VMP Group, and nowadays it also offers its customers a broad range of services supporting their core business.

##### **4.2.1 Customers and market**

The VMP Group is one of Finland's biggest providers of personnel services and is supported by the nation's most extensive service network.

The VMP Group operates through its franchises in Finland, Sweden, Estonia and Spain. The group also has an office in Romania specializing in the supply of employees with foreign backgrounds, and an office in Britain specializing in the supply of IT professionals.

Most of company's clients require Finnish or Swedish language skills. This is why company open job application forms and the job opportunities database are found only in these languages.

The VMP Group is a member of the Association of Support Service Industries belonging to the Confederation of Finnish Industries. (VMP Group 2011).

#### **4.2.2 Product and services**

The VMP Group has a broad range of service products that allows it to provide its customers with services in a large number of areas. The company offers its customers a broad range of solutions supporting business operations, including outsourcing (e.g.IT outsourcing), training, staff leasing and recruiting.

The VMP Group gives employees an opportunity to find both a temporary or a permanent job. It depends on the employees whether they accept the work offered. With VMP, employees can arrange work according their current situations in life. All VMP services are without cost to jobseekers. (VMP Group 2011).

#### **4.3 Comparison of Russia (non-European Union) and Estonia (European Union) outsourcing**

There are no obvious differences in the provision of IT services of the two companies Tieto Corporation and VMP Group. In spite of this, some studies show that the European Union companies have a different approach to IT outsourcing than non-European Union companies. According to the Rossbach study (Rossbach et al 2010, p.8) there are several differences in European Union and non-European Union outsourcing. European Union IT companies often have different growth strategies than their non-European Union competitors. For the European Union IT companies, the most important factors for success and growth are reliability and trust. The non-European Union IT companies take a more aggressive approach. The aggressive approach is in the willingness of the non-European Union IT companies to experiment. These companies prefer first to sell, and only then to develop, according to the customers. The non-European Union companies show great flexibility, even in pricing, in order to make a quick sale.

The European Union IT companies, on the contrary, first develop innovations until they are market-ready, and only after that start intensive market

development. The European Union companies try to gain customer trust through reliability and continuity. (Rossbach et al 2010, p.8).

There are some tax-related details that must be taken into consideration when working with non-European Union partners. This can make some problems concerning paperwork in the projects.

These differences, of course, do not characterize the difference of the European Union and non-European Union IT outsourcing companies. They are only examples of how European Union IT outsourcing differs from the non-European Union. The most important thing is that IT outsourcing should be efficient. It must give customer-companies a competitive advantage and help to cut costs.

In spite of the fact that Russia is a non-European Union country, and Estonia a European Union country they have similarities in software outsourcing:

- 1) Both software markets in Russia and Estonia continue to grow;
- 2) These countries are competitive due to cultural proximity, frequently common language (especially in the case of near-shoring locations, e.g.), and niche market expertise;
- 3) Due to continued growth of IT outsourcing markets, Russia and Estonia IT markets become more demanding and critical to government policies. Each government needs to provide more information and financial support to the software market.

## **5 EXPERIMENTAL PART**

The data collection method of this thesis is the questionnaire. It will be described in this chapter.

### **5.1 Description of questionnaire**

In order to collect sufficient and reliable information, 10 questions were sent to the Tieto Corporation and the VMP Group. Most of these questions are about how the companies operate, their organizational structure, etc.

The first question is about the relationship between the company and people working for the company. The company can hire people or they can work freelance. When the company hires people, it has to set up a contract with this person. If the person works freelance, it means that he/she is not an employee of the company, and doesn't have to be licensed or insured. They just have to be a person that can do the project. The companies evaluate the type of relationship by this question. Both companies operate very well, so it means that they have the right relationship with their employees.

The second question describes types of contracts which the companies have. It can be long term or short term agreement.

The next question shows how the companies find and select individuals. This is maybe not a very good question, because VMP Group is a human resources provider themselves. It might not need the help of recruiting agencies, while Tieto Corporation can find individuals through the VMP Group. It is difficult to analyze the answers on this question. Selection criteria can be different in these companies because VMP Group can select individuals depending on other companies needs while Tieto Corporation can select depending on projects it has.

The sixth question is maybe the most important question in this questionnaire. It describes the relationship between the boundaries. More specifically the relationship between the Tieto Corporation in Finland and the Tieto Corporation in Russia (the same with VMP Group). Companies can help each other to find

individuals or exchange people. The answers on this question will help to make suggestions for improving outsourcing of IT services from other countries to Finland.

The seventh question is about company performance. Companies should answer what kinds of difficulties they have and have there been any delays. Analyzing the answers on these questions will help to make a conclusion about what should the company do to avoid such problems.

The next question is about the organizational structure of the companies. Companies are different in their activities as Tieto Corporation is an IT service company and VMP Group is a human resources provider. It is interesting to see whether the companies have different organizational structures if their activities are different.

The ninth question shows differences in providing IT outsourcing services by Tieto Corporation (VMP Group) and other companies. This question tries to find out what can be done differently in the IT outsourcing companies.

The last question is about IT services which are the most popular now and which will be popular in the future. The answers will show the present and future situation in IT services demand.

## 5.2 Results of questionnaire

The VMP Group and the Tieto Corporation have answered the questionnaire. The answers to the questions are presented in Table 3.

No	Questions	Tieto's answers	VMP's answers
1.	What type of contract and relationship do you have with your people?	Hires people, sets up a the regular full time work contracts or also part-time contracts for duration of the project	Uses different types of contracts, mostly the regular full time work contracts, but sometimes also part-time contracts. Where it is possible and reasonable also uses not the labor-union contracts but executive contract

2.	Do you prefer long-term or short-term contracts?	Depends on projects, more preferable the permanent agreements	Company would like to sign the permanent agreements but it's impossible due to the nature of its customers' wishes and the nature of their short term project.
3.	What kind of system do you have for finding appropriate persons?	For hiring channels uses internet based online search communities and recruiting agencies	For hiring channels uses 80% of internet based online search communities and the company has several co-operating partners in the field of on-line search companies. Most likely the best channel and method is direct recommendations – one employee recommends to his/her friends
4.	What are the selection criteria?	Different	The selection of suitable candidates always varies and is guided by the customer's needs
5.	Are there any things you could have done differently in Estonia vs. Finland (Russia vs. Finland)?	Different mentality. Different ways of doing business.	It would have been better if the company would have created more efficiently its own candidates CV bank, but these on-line personnel search markets are different between Estonia and Finland. In Estonia the on-line personnel search market is more developed than in Finland.
6.	What kind of relationship is between VMP in Estonia (Tieto in Russia) and VMP in Finland?(Tieto in Finland) In what way the units help each other to find individuals or do they exchange people?	Tieto in Russia has good relations with Tieto in Finland. To find individuals companies use internal site - intranet.	VMP Group OÜ in Estonia is a Finnish subsidiary company, it is owned 100% by Finnish mother company. On daily basis it communicates on the need to know basis, but basically it is independent organization and it is has fully individual sales and profit budgets with own organization. The staffing to Finland has been rather occasional in

			the past but since this year the company intends to increase and systemize the posting of Estonian workers to Finland and why not vice versa also if required. Technically it is a signed contract, persons in both countries who communicate among each other and carry out the staffing projects.
7.	What kind of difficulties does the company face? Have there been any delays for the company?	Different	Didn't understand the meaning of this question, naturally there are difficulties in every company life and they should be a natural part of the company's development.
8.	Describe an organization structure of the company?	The company has matrix organization structure, based on the principle of multiple (often double) subordination.	In Estonia the company has appr. 150 seconded employees in various tasks and they have quite various durations of the agreements. Company's so called own organization consists of 7 executive employees who are responsible for the daily activities of the company. The company has 7 different offices in Estonia.
9.	What kind of differences are there between you and other outsourcing companies?	Can't answering	No differences in the field of responsibility and delivery of different tasks, the major difference is that the VMP company has much wider scope of services. It offers almost every kind of service not only accounting or IT support, but it can also offering different kind of warehousing services, assembly. Basically the company is able to offer very broad scale of services in the outsourcing field.

10.	What kind of IT services are the most popular now? In your opinion, which services will be the most popular in future?	All kinds of IT services are popular at present time. In future cloud services will be popular (the provision of computational resources on demand via a computer network, such as applications, databases, file services, etc.).	The company is offering different kinds of IT services (Insurance handling services for Finnish partner and data input and inspection services for the local energy company). Every service can be outsourced and is reasonable to at least consider to be outsourced due to the fact that constantly more attention should be focused in managing the core businesses of different companies and therefore to be able to specialize more all side activities could be outsourced.
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Table 3. Answers to the questionnaire.

### 5.3 Analysis of the answers

Having analyzed the answers it became obvious that some of the questions were not formulated well. The most unclear question for the companies was question number 7. Neither of the companies could give a clear answer about which problems the company has. It is possible that the question wasn't formulated correctly. It seems to be difficult to give a clear answer to this question. VMP company was right in saying that there are difficulties in every company's life and should be a natural part of the company's development. The question has to be outlined as: "What kind of difficulties does the company face during the crisis period?" or "What kind of difficulties does the company face in finding appropriate persons?"

Question number 4 as expected seems to be unnecessary in this questionnaire. It is difficult to make any comparison of the answers. The companies have different activities, so they have different selection criteria for their candidates. The VMP Group is a human resources provider, so it selects individuals depending on other companies needs. The Tieto Corporation didn't give a clear

answer, but it can be assumed that the Tieto Corporation can select individuals depending on projects it has.

Analyzing question number 1, it becomes clear that both companies prefer the regular full time work contracts. Sometimes companies use part-time contracts and where it is possible not the labor union contracts, but executive contracts. Question number 2 leads to the conclusion that the companies prefer to sign permanent agreements. The answers indicate that the type of contract depends on company's activity. In the Tieto's Corporation the contracts could be both long-term and short-term, while in the VMP Group this is impossible due to the nature of its customers wishes and the nature of their short- term projects.

According to the question number 3, to find the appropriate person both companies use internet based online search communities. It is obvious, because this kind of system for finding appropriate person is widespread now. It is easy and fast to use this kind of system. Sometimes companies use direct recommendations – one employee recommends to his/her friends.

Question number 5 shows that different mentalities play a very important part in ways of doing business. Companies with the same activities may do business differently in different countries. VMP Group operates in Estonia as well as in Finland, but due to different mentalities, on-line personnel search markets are different between Estonia and Finland.

Analyzing question number 6, it becomes clear that companies try to have good relations with the company's branch business. To help offices to find individuals companies can use internal sites - intranet. This way of cooperation is very popular among different branch businesses. Another way of cooperation is using the help of signed contract persons in both countries who communicate with each other and carry out the staffing projects. VMP Group and Tieto Corporation have different types of cooperation with their branch businesses. Both companies operate well, so the cooperation must be efficient.

According to question 8, every company can have different organizational structures depending on its activity, geographical region, and products. An organizational structure shows the organization of work in the company.

Organizational structure is very important for the company's future performance. Planning an organization structure helps the company to determine what kind of people it needs to hire to achieve its goals. Tieto's organizational structure is very complex while VMP's is not so complex. When companies operate well, it means that they have organizational structures that suit their needs.

Question number 9 perhaps not correct, as the Tieto Corporation couldn't answer. The question has to be specified as: " Are there any differences in the scope of services between your company and other IT outsourcing companies?" Analyzing the VMP's answer it is clear that among the differences that can be between the companies are differences in the scope of services.

The final question confirmed once again that IT outsourcing is very popular now. All IT outsourcing services are in demand now. In the future, cloud services may be popular, so companies have to pay attention to this kind of IT service.

## 6 CONCLUSION

The results of surveys such as the one presented in this research are useful in assisting IT outsourcing companies in being able to define what can be done better in their business.

It is understood from the theoretical literature that the outsourcing of IT services from other countries to Finland is very popular. Having analyzed the current situation in three markets (Russia, Estonia and Finland), and reasons for IT outsourcing, it is obvious that for Finnish companies it is reasonable to outsource IT services to Russia and Estonia. The main reasons for IT outsourcing are lower costs and higher productivity. Due to significantly higher labor costs in Finland, it is cost effective to outsource IT services to neighboring countries, such as Estonia and Russia. These countries have high foreign demand and they are ready to implement complex projects.

The purpose of the study was to find improvement suggestions for VMP Group and Tieto Corporation to make their business more profitable and effective. To improve outsourcing of IT services from Russia and Estonia to Finland, companies have to pay much attention to their cooperation with the offices in Finland. In spite of the fact that companies have good relations with their branch businesses, they forget that ways of doing business are different in different countries. This makes the cooperation between companies in Russia (Estonia) and Finland complicated. Companies have to have more joint projects in order to strengthen cooperation. It is reasonable to exchange experience periodically. This will help companies to operate more efficiently, improve service quality, e.g. it will help to improve the on-line personnel search market in Finland so that it becomes as developed as in Estonia.

The company's ways of doing business does not differ much in Russia and Estonia, in spite of the fact that Russia is a non-European Union country and Estonia a European Union country, these countries have similarities in software outsourcing. Both companies, the Tieto Corporation and VMP Group, try to have regular full time work contracts and prefer to sign permanent agreements. This fact shows that companies try to do everything to be a reliable company.

With the long-term contracts the company can plan its development for years in advance. The longer contracts thus provide some stability for the company and its employee.

Another suggestion for the companies is that they shouldn't forget that new service models have a key role in customers' IT strategies. To improve IT outsourcing from Russia and Estonia to Finland, companies in Russia and Estonia have to pay much attention to cloud computing as it is expected that this kind of IT service will be the most popular in future. In any case, it is important for companies to have a wide choice of services because market conditions and service needs can change at any time.

One of the suggestions for the companies would be to create a joint management team. It is needed to maintain quality of services, to scan the global market of IT service providers and to be in constant communication with branch companies.

The suggestions which are given in this study are important for the companies' future performance. The IT outsourcing market is very competitive now, because of the popularity of IT services. Suggestions for improvement outsourcing of IT services from Russia and Estonia to Finland help companies to strengthen their positions in the global IT market and be more competitive.

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## **APPENDIX 1**

The context of E-Mail

Dear Sir/Madam:

My name is Marina Shumanskaya and I'm double-degree student at Saimaa University of Applied Sciences, Faculty of Business Administration. I'm from Saint-Petersburg.

I'm writing to you with the request to help me with my theses. The topic of my theses is IMPROVEMENT OF OUTSOURCING IT SERVICES FROM OTHER COUNTRIES TO FINLAND. I have a small questionnaire for your company. These questions will help me to make a conclusion concerning the topic of my theses. Hope you will answer to them. I will look forward to your answer.

Greatly Thanks and Best regard,

Marina Shumanskaya

## **APPENDIX 2**

Questionnaire:

- 1) What type of contract and relationship do you have with your people? (e.g. do you hire people permanently or do they work as freelancers?)
- 2) Do you prefer long -term or short- term contracts?
- 3) Can you describe what kind of system do you have for finding appropriate persons?
- 4) What are the selection criteria?
- 5) Are there any things you could have done differently in Russia (Estonia) vs. Finland?
- 6) What kind of relationship is between Tieto in Russia (VMP in Estonia) and Tieto in Finland (VMP in Finland)? In what way the units help each other to find individuals or do they exchange people?
- 7) What kind of difficulties does the company face? Have there been any delays for the company?
- 8) Describe an organization structure of the company?
- 9) Can you tell what kind of differences are there between you and other outsourcing companies?
- 10) What kind of IT services are the most popular now? In your opinion, which services will be the most popular in future?