

# WHAT'S COOKING AT OPD?

Offshore Product Development or OPD has been in the limelight for quite some time as a new chapter in the Indian IT success story

PUNE, INDIA: Year 2004. A Nasscom-Mckinsey analysis had predicted the opportunity in the products and technology services space would be worth \$8-11 billion by 2008. Year 2007. Nasscom estimates that OPD exports will grow from the current \$2 billion to over \$7 billion by 2010.

**Back to year 2004.** For companies and geeks around the world, Indian IT prowess was synonymous to application development, coding or testing. The global platter was ripe but India was still delivering the starters (testing), the mocktails (applications) or the desserts (maintenance and support). The main course (core product development) was still not under India's IT province. But some adventurous and plucky chefs woke up to the challenge, that was at the same time, a delicious opportunity. If companies could offshore peripheral work, why not the products too? And so began the experiments with a new recipe-OPD or Offshore Product Development. So has the recipe worked?

## Whipping up the right mixture

There is no arguing the fact that India is well equipped to handle the OPD challenge. Challenge it is, for it is not without its own set of reservations. Product development is no small feat. It needs the upper-tier of development skills, domain grip, insight into the end-requirements and time-to-market imperatives. More than that, it is not easy for a company to

let go of its life-blood and entrust a third party for its core work. No matter how much one talks about one's track record in OPD, unless it is evidently demonstrated that an OPD vendor is more of a partner in the product, it is not easy to win and sustain business.

As Shirish Deodhar, senior vice president for Symphony Services, a formidable player in the OPD market that has clocked a CAGR of 190 per cent over the last four years, reasons, "Reservations are not absent. Any time there is an off shoring transaction from the US, the operational level needs time and proof to go over the initial resistance. But when India is able to deliver, the hitches are ironed out."

With over 80 customers and 225 Products Under Management (PUM), he surely has enough experience to support that. Symphony, for instance, has over 1650 deliveries to its credit with 644 deliveries last year. Ten releases last year constituted de la crème 'white board to market' category. "We are doing a couple of major releases per week and some minor ones on a per day basis," he says. The score of 400 minor releases and 225 major ones is enough of a glimpse but more what tickles one's curiosity is that 10 per cent of its PUM belongs to the complete ownership league, where Symphony has traversed the whole hog, from design to support stages of a product. "This is an example of maturing of the market. This wasn't the case earlier," Deodhar says.

Persistent Systems that has added 64 new customers (including license sales) in FY07 and reported consolidated revenues of \$70 million in FY07 is another upbeat player in this market. Almost a pioneer over the past seventeen years, with a CAGR of 60 per cent over the last three years, its delivery record shows 170 global software companies, including companies in the start-up phase and has undertaken over 1200 product releases.

Dr. Anand Deshpande, chairman and managing director of Persistent Systems, cites the Nasscom & Booz Allen Hamilton report for a flavour of how tantalizing the market is. Outsourced Engineering and Design Segment is set to touch \$40 billion by 2020 while total Offshoring spend to grow to \$150-225 billion by 2020. "These figures are proof enough of the upswing the industry has witnessed in the past few years and how it is expected to grow in the future."

## Still catching up

For many, however, there's more to be done and a realistic assessment points out other chinks in the armor. Customers still do not completely and easily perceive the difference between a generic provider and an OPD provider. Bhoovarahan Thirumalai, EVP and co-founder of Aspire Systems, another player in OPD that claims nearly 80 per cent growth, opines that customers are still 'offshoring', not 'outsourcing product development'.

"The differentiation is even more confusing - from a customer's perspective - when the generic IT service providers-including the tier-1 companies claiming to specialize in the OPD space. So, while OPD companies have reported impressive growth - the generic growth of the industry matches with that. The larger players in OPD have reported around 40 per cent revenue growth-in fact one public company in the OPD space has reported a 35 per cent increase in revenue but only a 5 per cent

increase in profit. But, that growth is in line with what Infy or TCS have reported, at a much smaller base. What that means is-it is the 'offshoring' buzz, that is giving the growth, and OPD buzz is still catching up," says Thirumalai.

His argument is simple. The momentum to grow beyond the speed of generic offshoring industry will be with companies that perfect the art of product engineering-not just from the technical angle, but also from the overall packaging angle.

## The pie has changed

Throughout the OPD journey treaded by India so far, the roster of work has visibly changed. This is palpable not only in the complexity of the work that is coming to India but also in the strategic thrust that clients put behind it and of course, the deal sizes which have enlarged the pie.

"Clients are no more just putting a toe in the water but they are ready to jump in the pool. Not only that, when they come to India now, they already have a plan, a transformational mindset," Deodhar says as he points at how the market has changed from transactional to strategic nature.

Another big change is in the perspective from the client's side. More cutting-edge work is now happening from India. As Deodhar explains, "Instead of asking an Indian company to do something, clients are now saying that teach us what we may do. This change is backed by their reckoning that while a client might just do ten releases in a given period, as an OPD vendor we are doing 1600 at the same time and hence our spectrum of work and expertise is no less." Another ripe market, in Deodhar's estimate, is emerging fast and wide-the software enabled business, where the company already has over 12 customers. "It is an exploding market. From Google to ebay to even traditional companies are

looking at in-house products for their internal requirements. From \$6 billion in 2006 it is projected to go up to \$20 billion in 2011. We are increasing our action here."

Persistent on the other hand is increasing its action space from traditional strongholds like infrastructure ISV, application ISVs, telecom, life sciences and business intelligence to verticals like communication, media and entertainment. Deshpande shares, "There is an interesting category of players such as the next generation platform players on the internet, and other B2B, and B2C plays; here the platform is the product. We are also actively involved with some established players in this space as well as next generation web 2.0 plays."

A look into Aspire's basket reveals a change in the mix as product engineering practices are culminating as frameworks. "We will be making a lot more 'engineering' announcements in the days to come by - consolidating the difference of OPD and excellence of Product Engineering versus generic offshoring," says Thirumalai.

In fact, of late, many other Indian players have announced releases in the area of frameworks, with NIIT, Synechron and Cognizant to name a few. Frameworks constitute a new strategy where service companies tap their experience in applications and services and churn out reusable components that can be used as ingredients in turn, by other companies. Something similar to the OEM market that Indian manufacturing space witnessed before it started producing made-in-India fare. Synechron had sometime back entered the market with two Strategic Solution Frameworks (SSFs) for the mortgage banking industry while it had plans for insurance and capital market verticals as well. Similarly, Cognizant has in its basket frameworks on RFID and SOA.

Agile or rapid development, which has been considered as an antithesis (sometimes - even as antidote to offshoring) is witnessing change too. "These processes are getting more and more adapted in the offshoring scenario. OPD companies are spearheading this effort," Thirumalai adds.

## Changes in the menu

As Indian OPD players get mature and bigger, the servings are also maturing on the product development value chain. OPD is happening both in core and non-core areas. Deshpande explains the chain citing the four phases of outsourcing. "The first phase is what we call cost arbitrage, the second phase is process efficiency, the third phase is design for manufacturing (DFM) and the fourth is Original Design for Manufacture (ODM). The twist from a software product perspective on all of this is that a product line may encompass varying degrees of the above, and hence it is more of a continuous evolution as opposed to discrete phases."

"Cost arbitrage means that companies are looking for places to get cheap labor. So they essentially do the same thing that they are doing somewhere else and put as many people as are required to do the job as long as it costs less. In the process efficiency stage the company realizes that it does not need a large workforce and can instead be more efficient by doing some rearranging or tuning of processes. The next step is design for manufacturing. Here companies start to innovate on products and processes. In this context, the software industry in India has evolved from cost arbitrage to process efficiency, where software developers are looking to be more efficient, have their processes in place and in turn reduce cost and time to market and finally innovate on services and offerings." Persistent, he cites again, has segmented the market into small/start-up/mid size ISVs and mature ISVs. "This has enabled us to focus

separately on these segments and cater to their requirements accordingly. For example, we help early stage companies encountering challenges of rapid prototyping for POCs, agile development, dynamically evolving requirements and development and testing across multiple platforms. We have initiated the Design for Manufacturing strategy through our service offering called 'Go-To-Live' which is targeted specifically at emerging software vendors and vendors looking for imminent time to market advantages."

## Starters

Overall the industry is maturing. So, there is a lot of energy and action in growth and mature products as opposed to start-ups, thinks Aspire's Thirumalai. "But, many start-ups are definitely doing their product development in India - with OPD firms. We have had the opportunity of working on a handful of first version work in Aspire."

His explanation goes thus, "Out of \$5 billion invested by VCs in 2006 in 865 deals as announced by National Venture Capitalist Association, only 1.2 billion was invested in 234 new companies as first time - or seed capital. This leaves the other funding sources including private equity and plough-back of profits that growing and mature companies invest in R&D. Also, consider the fact that start-ups put less investment on product engineering than growth and mature stage companies."

So, product engineering investment and hence OPD revenues will continue to be majorly towards growing and mature companies as opposed to start-up firms. "Whoever is reporting more start-up sided revenues - is not playing in the larger market," he quips.

Symphony Services kitty has 60 per cent of its 80 customers belonging to the enterprise class while the rest are early-stage start-ups. Most of the products are from the US while only four to five customers are from other regions. The tide has also changed when it comes to sunrise and sunset products. Previously it was more of cross-platform support or maintenance, but now product ownership is increasingly conspicuous.

## 'Captiv'ated

There's one more sea change happening. The captives for development that many companies set up for work of the OPD flavour are also coming into the fold of pure play OPD vendors. "More and more companies are saying that take my captive over. Close to 1000 employees from several captives have moved to Symphony and more captives want to integrate with Symphony," shares Deodhar.

Aspire nods in agreement. That trend is gaining definite traction. "Aspire Systems is yet to announce deals in this direction, but we are working in that direction, and will see action there," adds Thirumalai.

Captives of some ISVs have matured as Deshpande puts it. "They undertake more high-value work and are beginning to outsource peripheral functions to third party vendors. This helps them to save costs and maintain a healthy bottomline."

## Minding one's Ps and Qs

What effectively turns the tide of OPD in India's favour is the degree to which factors, that are almost the clinchers in any PD deal, are managed – Patents (or IP) and Quality.

Symphony's Deodhar stresses that OPD's real shine is witnessed in terms of the core IP work being entrusted. "We got 12 patents filed by our customers. Here our engineers were the authors. More than the number of patentable ideas, it's important to ascertain how many actually got converted to an IP. The growing confidence that IP is safe in India solves a critical issue. People thus no more offshore products just for the cost factor. Market has, for sure, matured."

## The next inflection point

So what would be the next point of interest in the OPD curve? The next inflection point is not isolated for OPD firms, it is the inflection point that the ISVs need, as per Aspire's Thirumalai. "Software vendors need to have much better product engineering practices. After all, out of the total 600 odd billions spent on IT in the world, software vendors are able to command only one-third market-share. That is because a lot of our customers' customers are 'building' custom applications, as opposed to 'buying' our customers (ISV's) product solutions. That needs to change, and in any other industry - take for examples shirts - 'ready-made' has almost replaced 'custom-made'. And, that is not just a question of standardization, but also availability, customization, scalability, flexibility - the same attributes that software products have to possess compared to custom-made software applications."

From the existing established ISVs' perspective, this will involve re-engineering of code-bases, he explains. "That is a huge investment and that has a slow ROI. ISVs are more bothered about their immediate releases than about the long-term code-discipline. This critical balance and the ability of OPD firms in convincing the ISVs to follow stricter engineering practices, in my opinion, is the next inflection point," he iterates.

## A pinch of salt

Doubts and debates do not fail to haunt the OPD house. There's a speculated inhibition from the client side in outsourcing product development to India, specially with regards to SaaS (Software as a Service) genre of software given the factors of internal team collaboration, proximity and regular feedback from end-customers, the creativity versus conformance dilemma. What implications, if any, do these factors have on OPD business?

Thirumalai shrugs it off. "That can be far from true, we have done so much work for ISVs who have been in the SaaS genre. The increasing maturity in processes and collaboration technologies - which creates the ability to deliver using as dynamic and creative oriented development process as Agile - from an offshore center - an art that is being perfected by OPD companies - is a great answer. If this dilemma exists, I am sure it will be short-lived and will go away soon."

Hence, he believes that be it SaaS or any license model - the product needs to be developed. It needs to be engineered perfectly in the most economical way. "And, OPD firms provide the means. There is no stopping that." Persistent's Deshpande discounts the concern explaining SaaS as just another delivery vehicle, which for software has gone through many changes from tapes to CDs to download, and now as a service. "SaaS is just another vehicle and so the process of software development do not change much. While it does need close collaboration and regular feedback from end-users, this can be easily managed in an outsourced environment. Internet is a great equalizer in that respect. Even the end user studies can be done better and more objectively in an outsourced environment."

## From cooks to chefs: Learning from mistakes

It has been a market of lessons for Indian OPD experts. As Deodhar from Symphony takes a leaf out from his box, "Quantification of value is one area that needs to be worked upon. It's not just important to deliver but it is also equally important to package it for clients. We could have done that better." But better late than never. Symphony has started what they call as an Innovation Score card that serves as a report card for performance and execution.

Another aspect of learning in Thirumalai's estimates is that OPD service providers are tempted to provide services to meet customer needs. "To go beyond that and making a difference in their product engineering practices is a huge effort. It requires strategic investments from both customers and the vendors. We have been emerging in that field, and we have been able to work with a few of our customers to go beyond day-to-day and look at longer term sustainability." That is a huge lesson, he feels.

And is there a threat from competition, specially when it comes to other Asian countries? There are some talks on India's weakness in Engineering versus China's strength as Thirumalai observes. "Unbelievable as it may sound but that was the pitch from a couple of Chinese companies in a recent conference. India is good at coding while China is better in engineering was their message. The need of the hour is strengthening product engineering practices."

Deodhar from Symphony says, "India has a ten year lead and has demonstrated a big edge. For some countries that are at par with this edge, scale is still an issue. So India has no major concern or worry, but then the gap can never be taken for granted," he objectively cautions.

Nothing of course, can be taken for granted in India's OPD story now. As Thirumalai from Aspire sums it up well, "Go beyond being a 'server' or a 'cook', and move on to become a 'Chef'. That is exactly what OPD firms need to do." So are the chefs ready? ■■■