

HIRING IN-HOUSE VS. OUTSOURCING FOR RECRUITERS

Your Software Development Team



Software is “eating the world”

The need for software across all industries is incredible, and it seems every industry has become ‘tech’ in some way or another. Silicon Valley has revitalized the Wild West in just a decade, but this new version is different. It’s hip, young, and less physically demanding. But it’s not just the cool factor that’s driving the mass migration and subsequent skyrocketing in the cost of living.

The salary for developers has become enticing, as well, and with opportunities come opportunists. Just like the real Gold Rush of the mid-19th century, masses of people are trying to figure out how to come west and become a part of the bonanza. This is great news for most in the industry, but not all. With this globalization and expansion of the software industry, recruiting software developers has become a more complicated and costly task.

Every job seeker these days seems to be a developer of some sort. More and more are tailoring their resumes toward tech, however they can. Unfortunately for software development recruiters, not all candidates are created equal, and separating quality prospects from the rest can be a costly endeavor. Dramatic increases in the price of employment in Silicon Valley and everything that goes with it have created difficulties for employers wanting to keep their costs down and still function optimally. This is bad news on an individual basis.

In the ‘greater good’ sense, however, these conditions may have opened up doors for a more efficient practice, as it has forced tech companies to look outward in the talent search process.

So we know that this has been a successful model for some tech companies, but how does the cost-benefit analysis of this trend pan out for you or clients? Should you be looking outward with the early adopters, or should you stay focused on nurturing your team at home?

When making these crucial decisions about your recruitment practices, whether for your own company or for another, consider how this jump would affect some of the core concepts of your recruitment process: ease, efficiency, productivity, and of course – **the bottom line**.



Recruiting In-House is Difficult

As a software development recruiter, you may have a nagging feeling that there are just not enough qualified programmers available to fulfill your needs as a growing company. Well guess what – you are not alone. It is important to recognize, however, that the problem is not one of supply, but rather of demand. There is a feeding frenzy in the tech industry and when it comes to the labor market, the spoils to be taken are for the kids graduating from university – not for the tech recruiters.

Employers' need for quality developers is increasing at such a high rate that competition for the best laborers has left many recruiters struggling to compete. According to The Firehouse Project CTO and co-founder, Ken Mazaika, *"there has never been a better time to be a developer,"* and this is making your job as a recruiter that much more difficult.

Outsourcing the recruitment process

This shift in balance from employers to job seekers presents a problem in a process that was already challenging, and the immediate reaction of some companies overwhelmed with positions to fill is simply to outsource the entire recruitment process.

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But before you go that route, consider the following problems with recruitment agencies:

Agency problems

This may be the most important problem, under which lie all of the other issues. How do you know if the recruitment agency has your best interest over another client, who offers better incentives to your shared agent?

The structure of compensation with recruitment agents is an inherent setback to begin with. Agents are most often paid a percentage of the hire's first-year salary, for each hire they acquire. They are incentivized by quantity, not quality, as there are really no built-in incentives for the agent to ensure the value of the hire, other than return business from you. In fact, if you look at it from a mathematical perspective, the agent gains more from inadequate hires, as they are more likely to result in turnover, which means more business for the recruiting agent.

Absence of transparency in your agent's client portfolio

Without knowing the salaries of the other positions for which your agent is recruiting, you don't know if your share of recruitment agents' income is substantial enough for them to consider you worth their time. It is only natural for someone that is paid through commission to focus more on those prospects with a higher income potential, and the difference can be relatively great from the agent's perspective.

For example, if your agent is looking for an entry-level developer for your company (annual base pay \$66,000) and your agent's other client is looking for a developer with 15+ years of experience (annual base pay \$100,000), the difference between you, at a 25% commission rate, is \$8,500.

Recruitment agencies are expensive

Right off the bat – in the case you utilize a recruitment agency's services, you need to be prepared to hand over 15-30% of the sought-after employee's annual salary.

Pre-tech boom, recruitment agencies were more of a necessity. Hiring back then was a more manual and specialized process. In line with the principles of division of labor and specialization, this high cost made more sense to absorb. In this day and age, however, your in-house recruiter has access to the same job boards and information as does a recruitment agency.

Furthermore, while the cost to hire these recruitment agencies remain more or less the same over time, the agencies own in-house costs have decreased with improvements in technology and increase in access to information, but these savings are not passed down to the client.

Outsourcing your developers:

There are upsides to outsourcing, of course, but they may not be in the recruitment process itself. A better alternative may be cutting (or leaving) out the middleman, and looking to outsource your software developers themselves.

If you are hesitant to adopt this business model, that's okay. There are many reasons for one to hesitate about what may feel like a shift away from orthodox business practices, and you are right to be cautious. Maybe your instinct is to keep the entire team under one roof, where it can be streamlined, and quality control can be maintained from within the office. This hesitation to relinquish direct control of your business to a third-party agent parallels the case of outsourcing the recruitment process. But the agency problems of the recruitment agent are much easier to remedy with the software developer.



Let's take a look at some of the differences:

1 First of all, software development work produces output of which the quality is more readily apparent than that of a hiring recruiter. The levels of collaboration between a developer and its contracted company are more likely to be high enough to permit the contracting company to be aware of progress during the process. With employment recruiters, the quality (or lack-thereof) of their job can remain dormant for some time.

2 Second, there is generally a lot more work put into software development than there is into employment recruiting, which incentivizes the contractor to seek long-term relationships. Whereas an employment recruiter can find a quick-fix hire and then move on to other clients that will pay the same.

3 Third, the relationship between payment and production is more transparent. You see your contracted developers work both during and after the process. With a contracted recruiter, you have no idea what prospects are out there that they are passing on, missing, or giving to higher-priority clients.

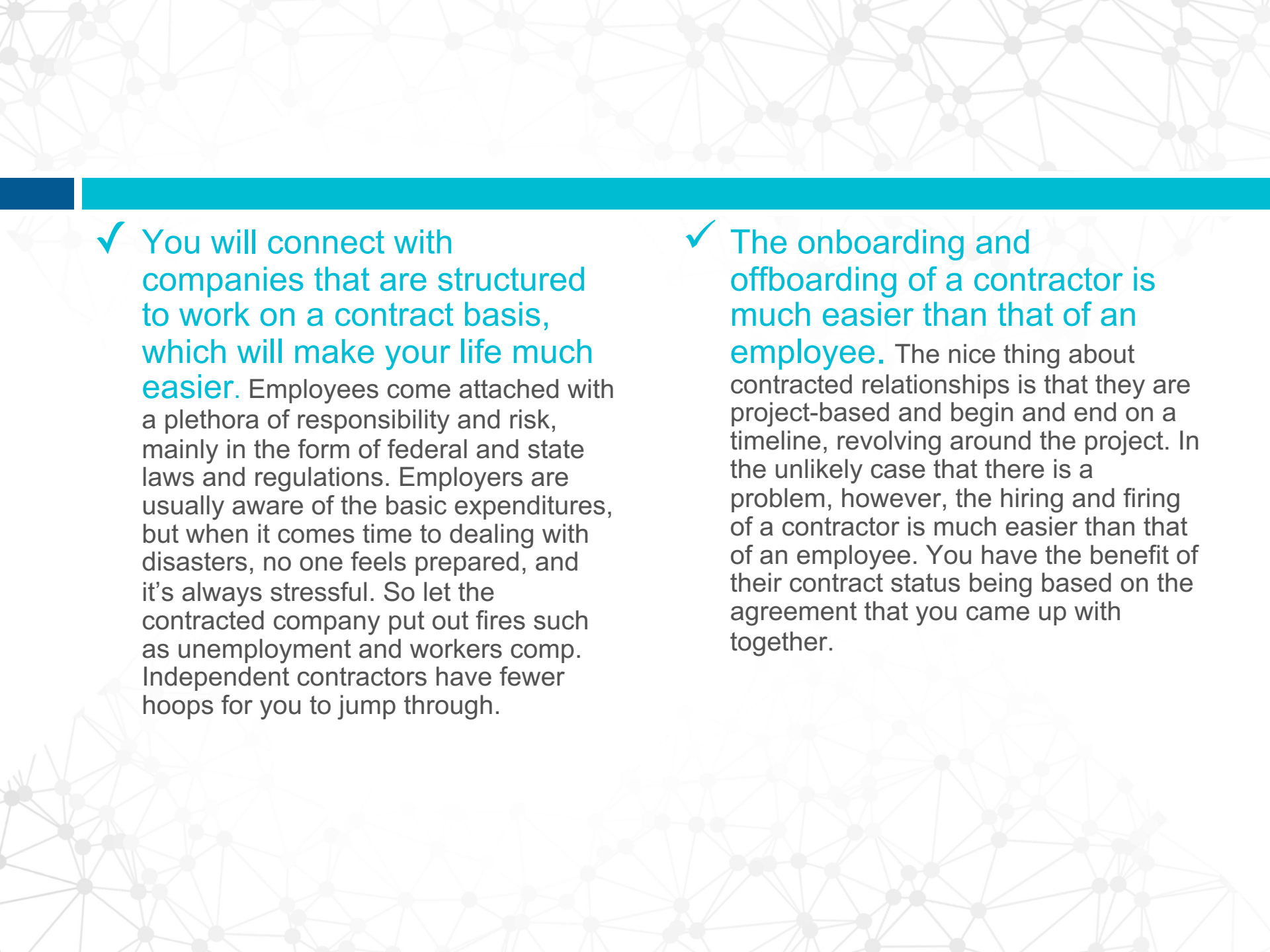
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It's normal to be hesitant

It is reasonable to be prudent, but before you fall victim to stagnation, remember that you work in an industry that thrives off of constant evolution, and **consider the following benefits** of leaving your comfort zone and working with an outsourced development team.

- ✓ **The employees of your contracted development team are already vetted.** While your own internal hiring process would require months to fill an entry-level position (much more for tech), your contracted development team is ready to go. The legwork is done, and you have a self-sufficient source of developers at your beck and call. Their employee profile is vetted, tailored and ready to work for you.

- ✓ **Your outsourced developers have the specialized knowledge for which you are searching.** They may have learned it in university, in-house at a previous firm, at their current company, or even from one of your direct competitors. The point is that they have it, and you don't have to train them for it. Rather than scrutinizing millions of applicants for that specific skill that you need, and then trying to scale it, go straight to the contractor company that does it exclusively.



✓ You will connect with companies that are structured to work on a contract basis, which will make your life much easier. Employees come attached with a plethora of responsibility and risk, mainly in the form of federal and state laws and regulations. Employers are usually aware of the basic expenditures, but when it comes time to dealing with disasters, no one feels prepared, and it's always stressful. So let the contracted company put out fires such as unemployment and workers comp. Independent contractors have fewer hoops for you to jump through.

✓ The onboarding and offboarding of a contractor is much easier than that of an employee. The nice thing about contracted relationships is that they are project-based and begin and end on a timeline, revolving around the project. In the unlikely case that there is a problem, however, the hiring and firing of a contractor is much easier than that of an employee. You have the benefit of their contract status being based on the agreement that you came up with together.

Recruiting In-House is Inefficient

Over all else, it is often cheaper to work with **contactors**. Skip out on expensive hiring and training costs, pay as needed rather than the bimonthly salary, and forget about benefits. If you're in tech, you're probably already exposed to the incredible savings that you can exploit by decreasing the overhead of office presence. This may be one of the most often overlooked benefits of working with contractors.

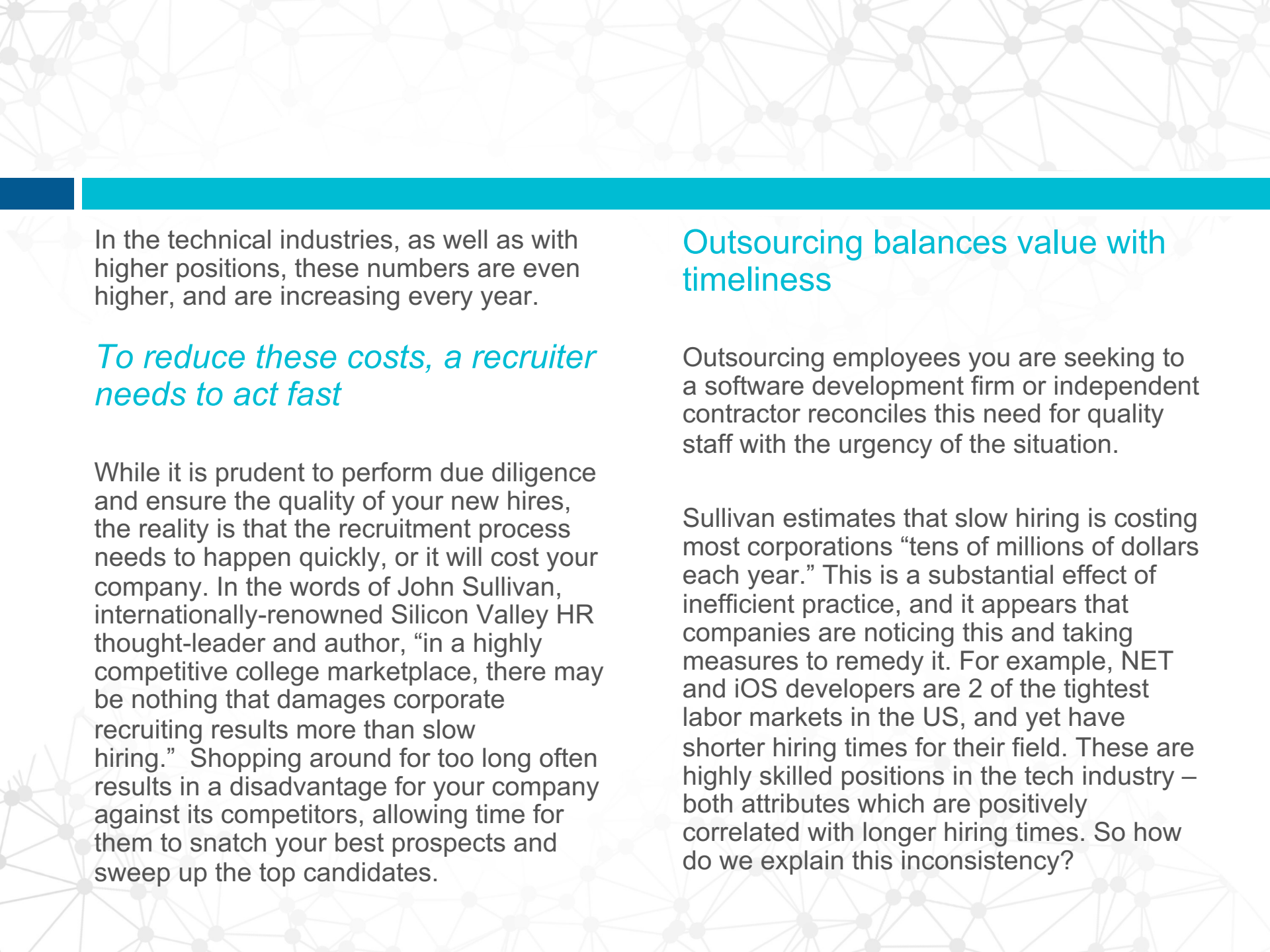
The reality of the IT world is that we live in an employee's market

The general labor market has been tightening since the financial crisis, with hiring duration hitting a 29-day all-time high in January 2016, and it is much worse in tech. With this talent shortage, recruiting and hiring takes more time, which exponentially increases both costs and effort as time goes on.

Time equals money

According to a 2016 Devskiller study, it takes an average of 43 days to fill an entry-level position. This number is substantial, but the fact that this time frame can reach upwards of 95 days is alarming. The average total cost of the hiring process (productivity loss during this time, plus internal and external costs of recruitment) – can exceed \$60,000 and is most often underestimated by 90-95%. Loss of productivity accounts for a \$33,251, and is caused by the vacant position, as well as the both internal and external costs, such as the time it takes the HR department to review resumes, interview, travel, etc. The cost of recruitment accounts for \$31,970.

Recruiters may be prepared for the advertising, travel, and consultancy fees, but case-by-case expenses such as immigration fees, technological expenditures, background checks, and third-party services often have a surprise effect.



In the technical industries, as well as with higher positions, these numbers are even higher, and are increasing every year.

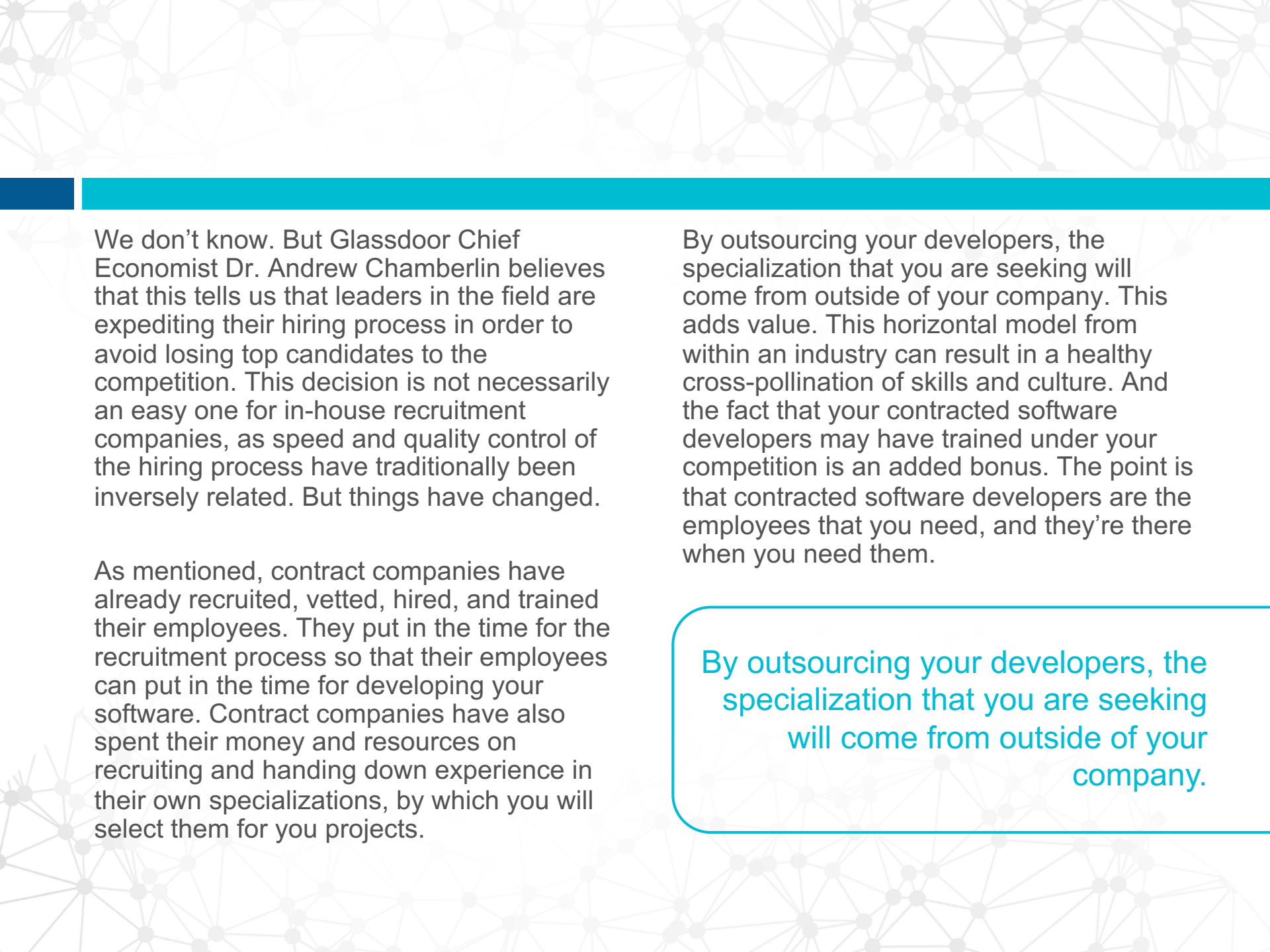
To reduce these costs, a recruiter needs to act fast

While it is prudent to perform due diligence and ensure the quality of your new hires, the reality is that the recruitment process needs to happen quickly, or it will cost your company. In the words of John Sullivan, internationally-renowned Silicon Valley HR thought-leader and author, “in a highly competitive college marketplace, there may be nothing that damages corporate recruiting results more than slow hiring.” Shopping around for too long often results in a disadvantage for your company against its competitors, allowing time for them to snatch your best prospects and sweep up the top candidates.

Outsourcing balances value with timeliness

Outsourcing employees you are seeking to a software development firm or independent contractor reconciles this need for quality staff with the urgency of the situation.

Sullivan estimates that slow hiring is costing most corporations “tens of millions of dollars each year.” This is a substantial effect of inefficient practice, and it appears that companies are noticing this and taking measures to remedy it. For example, NET and iOS developers are 2 of the tightest labor markets in the US, and yet have shorter hiring times for their field. These are highly skilled positions in the tech industry – both attributes which are positively correlated with longer hiring times. So how do we explain this inconsistency?



We don't know. But Glassdoor Chief Economist Dr. Andrew Chamberlin believes that this tells us that leaders in the field are expediting their hiring process in order to avoid losing top candidates to the competition. This decision is not necessarily an easy one for in-house recruitment companies, as speed and quality control of the hiring process have traditionally been inversely related. But things have changed.

As mentioned, contract companies have already recruited, vetted, hired, and trained their employees. They put in the time for the recruitment process so that their employees can put in the time for developing your software. Contract companies have also spent their money and resources on recruiting and handing down experience in their own specializations, by which you will select them for your projects.

By outsourcing your developers, the specialization that you are seeking will come from outside of your company. This adds value. This horizontal model from within an industry can result in a healthy cross-pollination of skills and culture. And the fact that your contracted software developers may have trained under your competition is an added bonus. The point is that contracted software developers are the employees that you need, and they're there when you need them.

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Recruiting In-House is Unproductive

In-house turnover rates have skyrocketed

One change in the employee-employer marketplace that has had a huge impact on the cost-benefit analysis of outsourcing versus in-house hiring is the increasingly high turnover rate of in-house employees. Employers are willing to spend a substantial amount of time, money, and resources in order to train their developers in their specialized field. In 2015 American employers spent an average of 53.8 hours of training per employee, per year. This number has been increasing at a substantial rate, up 31.8% from 2014, for example, when it was only 40.8 hours. And these averages are more striking when inspecting various segments of the market.

So why are companies willing to spend this amount of time training employees, rather than outsourcing the work?

Because the instinct remains that with an in-house, dedicated software development team, the fixed costs of hiring, training, and employing will work themselves out to be minimal over time. Unfortunately, this long-term relationship has become the exception rather than the rule.

According to a 2015 Recruiter survey, the average employee stays with a given company for less than 6 years. 30% of the working population changes jobs every 1-3 years, and 29% every 4-6 years. But the most disconcerting statistic might be that **“20% of new hires leave in 12 months.”** If these numbers apply to your company, then your fixed costs of hiring will remain fixed.

In the worst case scenario, training your employees may actually be a negative investment, given the 20% chance that they will be working for your competitors in the next 12 months.

Let's take a look at how this translates to the profit and loss statements:

- ✓ The average time to hire a software engineer is 35 days; and remember – these averages increase drastically given certain factors, many of which directly relate to tech.
- ✓ US companies' expenditures on learning tools and technologies rose by 137% between 2014 and 2015.
- ✓ In 2015 this expenditure represented an average of 5% of their total budget or \$602,306 (vs. \$254,256 in 2014).
- ✓ In 2015, total training expenditures (including payroll and spending on external products and services) increased by 14.2%. Spending on outside products and services rose by 29%, while other training expenditures (travel, facilities, equipment) increased by over 100%.
- ✓ After all is said and done, we can value the average replacement of an employee at between 6 and 9 months of that employee's salary.
- ✓ A new Glassdoor analysis has found that the time to hire a new employee in the US has increased 80% over the last 5 years, citing the interview process screening methods as a main cause of this setback.
- ✓ Moreover, independent contractors are better for your cash flow. Rather than abiding by the strict state and federal laws, such as minimum hourly wage you will set the pay schedule yourselves. You can pay your contractors as your clients pay you.



Let your contractors absorb these time costs so that your company can get to work

Let specialized companies with acquired skills and experience come to you trained, knowledgeable, and ready to hit the ground running. You can't prevent other companies from acquiring and training skilled developers, but you can leverage their hard work and success by utilizing their talent for your own company's benefit, making yourself more competitive in your field. Speed up the process of filling those urgently-needed positions with outsourced employment.

Remember that you aren't limited to a single contract company

The beauty with this model is that you can use as many different contracted developers or development companies as you want, making it that much easier to match the particular needs and specializations of each project. While you outsource app development, software development, and more, the companies that chose to stay in-house are forced to maintain a myriad of full-time, trained employees on staff, increasing their costs and liabilities, decreasing their acquired outside expertise, and ultimately weakening their competitive edge against you and the rest of the field.

So you're convinced that you need to consider outsourcing your software developers.

What are some ways for software developer recruiters to optimize outsourced software development?

The first thing to consider is:
where are all the quality developers?

Where can you look to optimize your pursuit? In other words – how can you maximize the quality of your developers while minimizing the time it takes for you to find them?

Here is a general breakdown of the different ways to outsource, along with some pros and cons of each.



Onshoring is outsourcing your labor from your in-house employees to an outside company, within your country.

Pros: If you have never hired an independent contractor before, and are wary, this may be your best option. You can cut your costs in half just by going outside of your metropolitan area (annual pay for a position that ranges from \$64,980 in North Dakota starts at \$119,180 in California), and you can rest assured that you share a culture, a language, and time zones. If you hire close by, you will have the comfort of being able to do face-to-face meetings, and to see product in person.

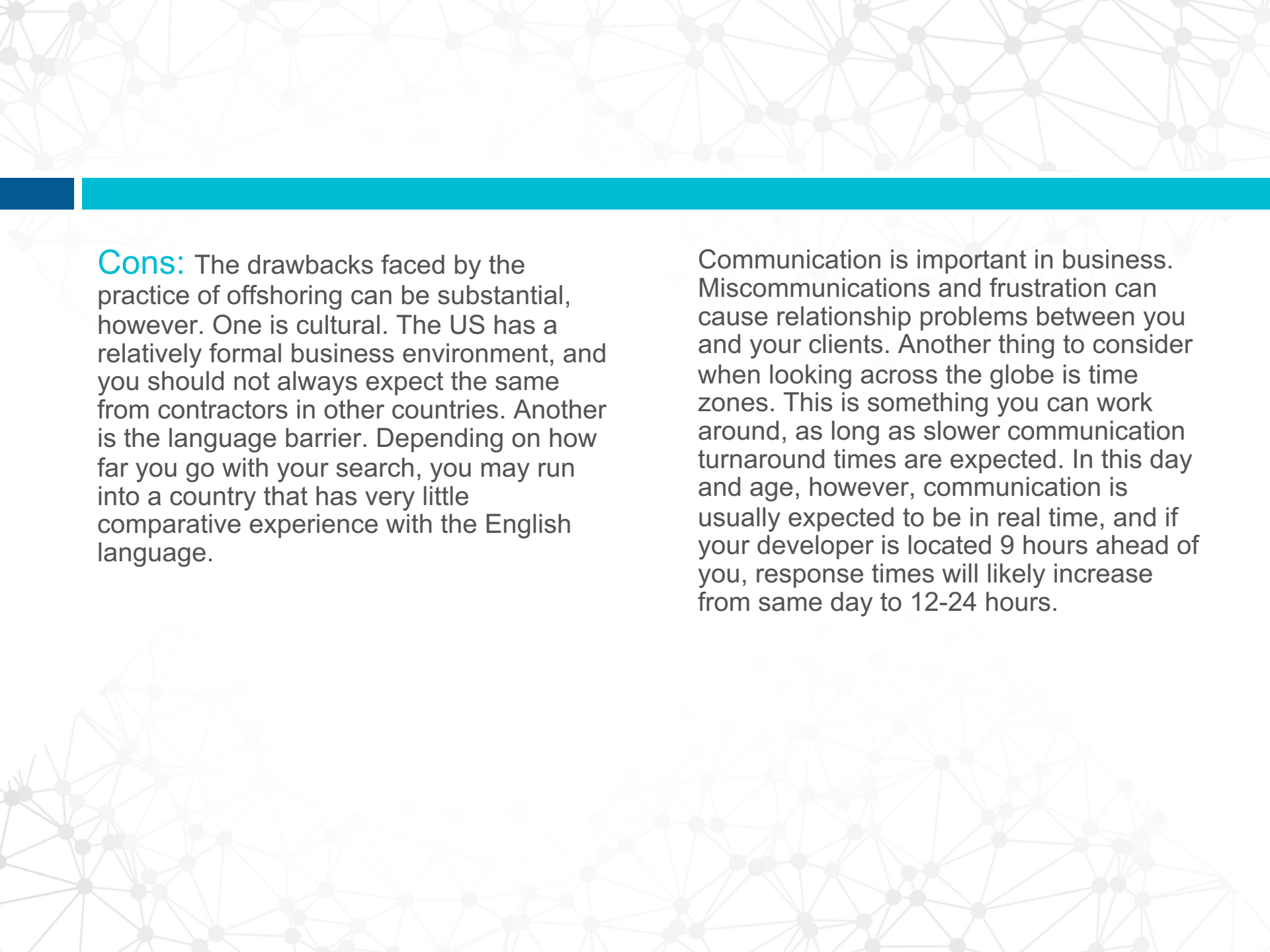
Cons: In a value-to-price comparison, however, we may have better options. In a country where the median annual salary for developers is more than 200% that of the world, your company would be well-served to look elsewhere.

Offshoring: Offshoring is outsourcing to another country.

Pros: Competition to find quality software developers in the US can be prohibitively difficult. There are simply too many positions and not enough developers to create a competitive employer's market, and the truth is that the rest of the world is catching up with the US on this front. Silicon Valley's own Hacker Rank competitive programming challenge of August 2016 put the US in 28th place for quality of programmers.

If you're in the tech field you probably realized a long time ago that there are quality software developers outside of the US – many of them. But you may only have exposure to them over the phone from China, in which case you probably experienced some cultural or language barriers to optimal productivity.

Don't let this turn you off. Remember that there are cities outside of the US that are becoming technology hubs, some of which operate more cheaply than the hubs of the US. Indian developers, for example, make \$24,000, while American developers are paid \$83,000 for the same job. And you can find and hire them faster than their American counterparts. While the average time to fill a position across all industries is lower in the US than the rest of the world, in the industries of engineers and information technology it is higher in the US.



Cons: The drawbacks faced by the practice of offshoring can be substantial, however. One is cultural. The US has a relatively formal business environment, and you should not always expect the same from contractors in other countries. Another is the language barrier. Depending on how far you go with your search, you may run into a country that has very little comparative experience with the English language.

Communication is important in business. Miscommunications and frustration can cause relationship problems between you and your clients. Another thing to consider when looking across the globe is time zones. This is something you can work around, as long as slower communication turnaround times are expected. In this day and age, however, communication is usually expected to be in real time, and if your developer is located 9 hours ahead of you, response times will likely increase from same day to 12-24 hours.

Nearshoring: A Healthy Alternative

Both of the previous methods have their pros and cons. To make it simple, onshoring is expensive, and offshoring is complicated. Fortunately, there is another option – Nearshoring is the form of outsourcing that leaves your home country, hiring internationally, but in a country that is close to your own, in both geographical proximity and in culture. There are a few very important benefits in this practice that differentiate it from the other two.

- ✓ **Minimized cultural differences**
Cultural differences tend to increase with geographical distance, as countries' proximity increases exposure to one another. Choosing a country that is closer and more similar to your own decreases incidents of cultural clash, ensuing as a result of surprises.

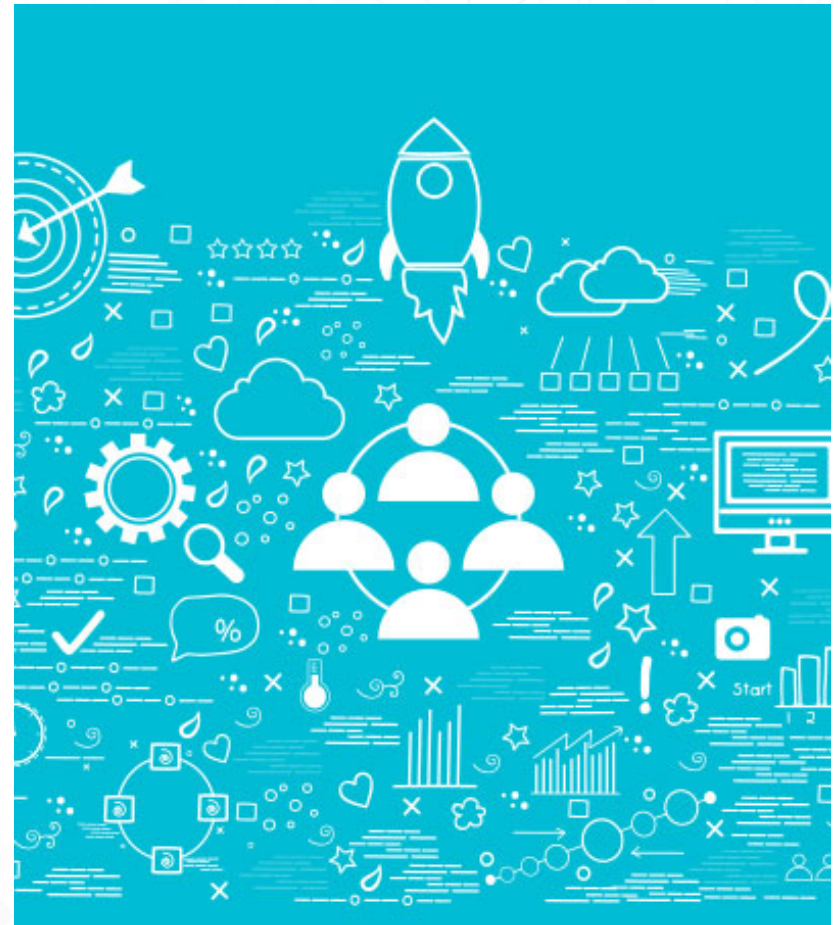
- ✓ **Maintained language capacity**
Ease of communication is important to avoid misunderstandings and frustration. There's nothing that will alienate clients like poor communication, and nearshoring to a country with close ties to the English language improves communication immensely.
- ✓ **Maintained time zones**
If you've ever had to conduct business with an Australian or European company, you know that the inconvenience of a 12-hour time difference is not exaggerated. Outsourcing to countries on your same time zone, or within an hour or two makes communication and scheduling easier.

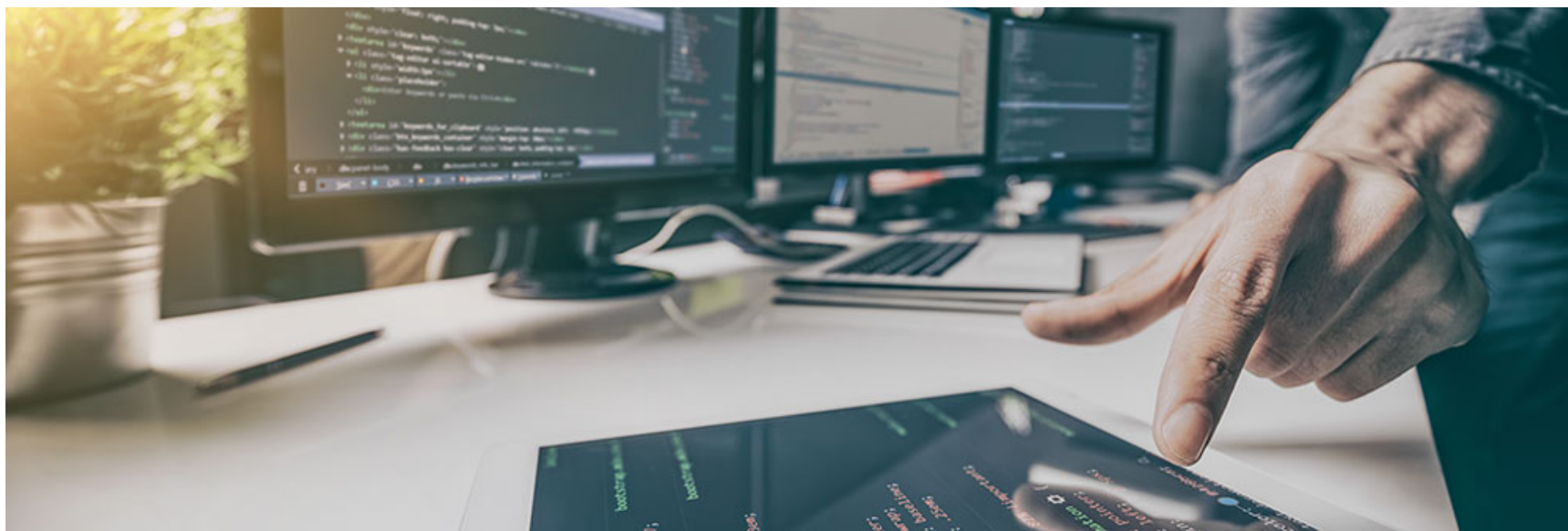
✓ Lower travel costs

We all know that there is some business that you just can't do over Skype. And in this case you just have to travel to your contractors, or pay them to come to you. If your company anticipates that it will want to meet its contractors face-to-face once in a while, consider the cost of those plane tickets in your cost-benefit analysis.

✓ Political and legal similarities

When it comes to business, we always want to avoid misunderstandings. And when it comes to politics and the law, we want to avoid misunderstandings at all costs. Outsourcing to neighbor-countries minimizes this risk because the legal and political systems are more similar.





Looking outward, but not too far

Nearshoring offers the benefits of outsourcing, while reining in the drawbacks. In the age of globalization, lines are being redrawn. We are connected to our neighbors through industry and business practices and, with communications and travel becoming easier every day, companies are finding it easier to utilize the comparative advantages that are outside of their own country. Nearshoring provides a safe place for the cautious recruiter to test the waters of recruiting from outside the US, reaping the benefits of international cooperation so that he or she will not be left behind in the shadows of the in-house entity.



Bydrec, Inc.

4900 Hopyard Road, Suite 100

Pleasanton, California 94588

Phone: [888-864-3124](tel:888-864-3124)

www.Bydrec.com

Email: info@bydrec.com