Aberdeen Group

The Business Value of IT Outsourcing Benchmark Report

Managing Expectations — and the Providers

July 2006

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Executive Summary

Outsourcing has become a standard business tool for many IT organizations — growing from its beginnings in mainframe data centers, through the emergence of offshoring in the late 1990s, when Y2K application remediation gave birth to companies in other parts of the world — most notably, India — that now develop and maintain applications at a fraction of the cost of U.S. internal IT departments. Outsourcing continues to mature as a business tool; a growing number of companies are using it to solve critical IT skills shortages and become more nimble in responding to the ever-increasing pressures of globalization.

Aberdeen Group's recent survey for this benchmark report found that 67% of respondents' companies outsource at least some of their IT work (16% outsource all of it), and another 9% plan to launch their first outsourcing deals within 12 months.

Key Business Value Findings

Most companies report only adequate satisfaction with their outsourcing initiatives, a survey finding consistent across eight different IT activities: applications development or maintenance (ADM), data center computing and operations, end-user computing (e.g., PCs and help desk), business continuity, disaster recovery, IT security, voice network management, and data network management. However, satisfaction can vary depending on whether your enterprise outsources all or part of IT or whether it uses one vendor for a particular function or several.

It should come as no surprise that most enterprises turn to IT outsourcing to save money. In fact, 63% of survey respondents cite cost reductions as their top reason. While the drivers are clear and widely understood, there are a host of pressures that stand in the way of getting the best value out of an IT outsourcing arrangement. These pressures — or challenges — boil down to two solutions: ***managing outsourcing expectations*** and ***managing the outsourcing provider***.

Best in Class, or leading, companies excel in these two areas and it sets them apart from other organizations. First, Best in Class enterprises work hard on setting the right outsourcing expectations from the outset. By being more willing to use outside advisors, such as independent consultants and lawyers, they understand the outsourcing market better, have a better going-in strategy, and are more likely to get the outsourcing specifics — RFP, pricing, service levels, vendor management processes — right the first time.

Building off this solid foundation, Best in Class companies do a better job of managing the outsourcing provider by applying more management time and talent, creating new internal cross-functional structures to manage outsourcing relationships, and being more willing to escalate problems with an outsourcing provider to its senior executives. However, a significant portion of Best in Class companies (33%) doesn't believe it has the right IT skills or number of staff to manage their outsourced environments.

Implications & Analysis

An outsourcing agreement is much more involved than conducting a cost analysis that can compare how much an enterprise can save by shipping an IT service or function outside the four walls. It's much more involved than that, and respondents to our survey are overwhelmingly adamant about proceeding with caution, holding the provider accountable for performance shortfalls, and managing the relationship effectively.

The most important step companies are taking to maximize the value they get from outsourcing IT functions is appointing a company officer who can be held accountable for improving outsourcing performance. In addition, a company will often need an external "honest broker" ─ a consultant, a lawyer, or both ─ for intelligence about the outsourcing market and guidance in reaching the right outsourcing decision.

Among Best in Class firms, the CIO is more likely than any other C-level executive to make the final decision on an outsourcing contract. This highlights the increasingly strategic role CIOs are playing in companies that have experienced the best results from outsourcing. It also bodes well for the future stature of the role.

Some 25% of the survey sample do not outsource. The top three reasons respondents gave for why their companies don't outsource IT have long been common:

- Loss of control of IT resources;
- IT is a core competency; and
- Company strategy does not include outsourcing.

Recommendations for Action

Outsourcing an IT function or service is a complex and significant initiative that requires more up-front thought, strategy, and executive effort than most companies realize. Success begins by treating outsourcing as a strategic issue rather than as a tactical deal. Therefore, involve a cross-functional group of executives in developing a strategy, engage independent advisors with experience in the outsourcing marketplace, and apply the necessary management time and talent at the start of the effort. This correctly sets the outsourcing expectations at the outset.

The efforts continue by having a detailed but focused RFP in place before sitting down with potential providers. That starts with knowledge of the work being outsourced, identifying the right provider candidates, and addressing upfront the challenges in sending the work outside. It continues with a process that collaboratively engages providers on the important issues, doesn't get bogged down in trivial details, and, at the start, builds a relationship that treats the providers as part of your company.

Foremost, though, driving the most value out of an IT outsourcing arrangement is about managing the provider — providing the right skills, number of resources, executive attention, and focused responsibility needed to make this strategic initiative a success.

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Chapter One: Issue at Hand

Key Takeaways

- Globalization has broadened the outsourcing supply options for companies of all sizes, notably with India-based companies that began their rise with application development work.
- As it did in the not-so-distant past, reducing operating costs remains the primary driver behind IT outsourcing.
- However, about half of the enterprises represented in Aberdeen's survey are outsourcing IT services to access expertise they don't have in-house and to help their internal IT professionals focus on the organization's core competencies.

Outsourcing has become a popular business subject over the last decade as companies look to cut costs and become more nimble in responding to the ever-increasing pressures of globalization. For many IT organizations, outsourcing has become a forced necessity since the late 1990s, when Y2K remediation gave birth to companies in other parts of the world — most notably, India — that could perform legacy code fixes at a fraction of the cost of the typical U.S. IT department.

The Internet, of course, has facilitated communication between hemispheres, and at the same time given the customer more power and leverage in getting the product or service he wants, at the right price point and at the right time. That has forced IT organizations to become increasingly nimble. If the in-house staff can't deliver an application within a tight time frame, it can farm out the job to a company that can — and maybe do a better job if it has the superior technical expertise.

Aberdeen Group's recent survey for this benchmark report found that 67% of respondents' companies outsource at least some of their IT work (16% outsource all of it), and another 9% plan to launch their first outsourcing deals within 12 months.

Satisfaction, however, yields a mixed picture. Most companies report only adequate results from outsourcing across eight different IT activities: **applications development or maintenance** (ADM), **data center computing and operations, end-user computing** (e.g., PCs and help desk), **business continuity, disaster recovery, IT security, voice network management**, and **data network management.**

> Nine of every 10 companies represented in the survey have saved money on outsourcing IT, with the average savings about 15%.

But when it comes to saving money, the chief driver for outsourcing IT, the results are much better. Nine of every 10 companies represented in the survey have saved money on outsourcing IT, with the average savings about 15%. Aberdeen based the Best in Class performers for this survey on how much they saved:

- **Best in Class** companies saved at least 21% through IT outsourcing.

- **Industry Average** companies saved between 6% and 20%.
- **Laggards** either lost money or saved no more than 5%.

What's Driving IT Outsourcing?

Nearly two-thirds of respondents cited reductions in operation costs as the chief driver behind IT outsourcing (Figure 1). The second and third most important reasons address the issues of IT skills and how enterprises can get the best skills for the right cost at the right time. About half of the companies represented in the survey recognize that there are talent limits within their IT staffs and look outside for help in filling those talent "gaps."

And, a sizeable minority cite the need for outsourcing IT functions as a way of helping the IT organization become more nimble in fulfilling business-unit requests, especially those that are in danger of running behind schedule.

Competitive Framework Key

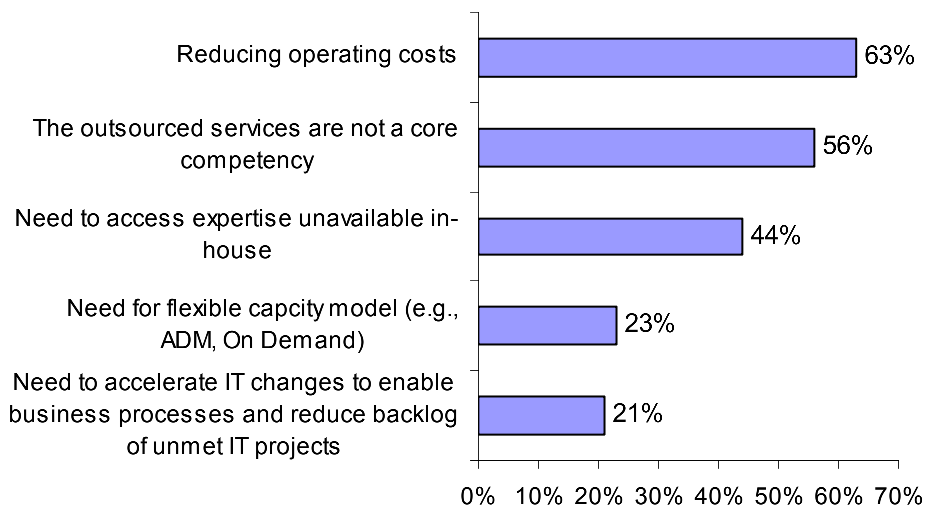
The Aberdeen Competitive Framework defines enterprises as falling into one of the three following levels of practices and performance:

Laggards (30%) —practices that are significantly behind the Industry Average

Industry Average (50%) —practices that represent the average or norm

Best in Class (20%) —practices that are the best currently being employed and significantly superior to the Industry Average

Figure 1: Key Drivers of IT Outsourcing



Source: AberdeenGroup, July 2006

Behind these drivers lie other pressures the IT organization faces in getting the most value out of outsourcing initiatives. It is these pressures — and the actions, capabilities, and enablers enterprises have at their disposal to ease those pressures — on which much of this report is focused. In Chapters Two and Three, we will examine how the Best in Class, Industry Average, and Laggard enterprises respond to these pressures by the processes they use, their organizational structures, the knowledge they use, and the technology and outside services they use to enhance the payback they get from outsourcing.

PACE Key — For more detailed description, see Appendix A

Aberdeen applies a methodology to benchmark research that evaluates the business pressures, actions, capabilities, and enablers (PACE) that indicate corporate behavior in specific business processes. These terms are defined as follows:

Pressures — external forces that impact an organization's market position, competitiveness, or business operations

Actions — the strategic approaches that an organization takes in response to industry pressures

Capabilities — the business process competencies required to execute corporate strategy

Enablers — the key functionality of technology solutions and services required to support the organization's enabling business practices

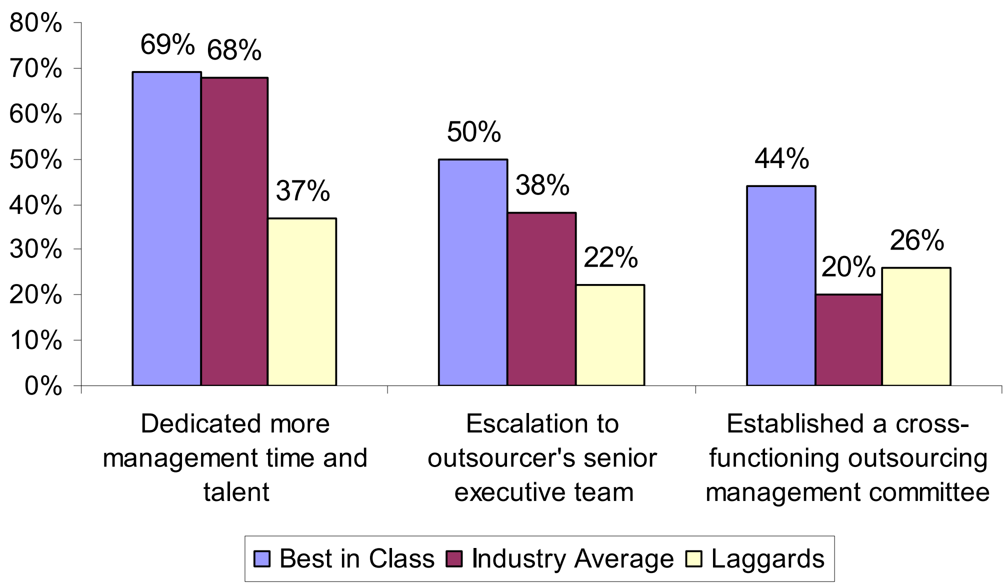
Chapter Two: Key Business Value Findings

Key Takeaways

- Driving the best results from IT outsourcing begins with managing the outsourcing provider and managing expectations.
- Best in Class enterprises are more likely to rely on outside help in reaching a decision on outsourcing and to get the RFP requirements and pricing right.
- Companies that outsource report the highest satisfaction levels with application development and maintenance (ADM) and data center computing and operations work.

While the drivers of IT outsourcing are clear and widely understood, there are a host of pressures that stand in the way of getting the best value out of an IT outsourcing arrangement. These pressures — or challenges — boil down to two simple issues: ***managing the outsourcing provider*** and ***managing outsourcing expectations***. Best in Class companies excel in these two areas and it sets them apart from Industry Average and Laggard organizations (Figure 2). Note the higher willingness to escalate problems to a provider's senior executives and to create an internal, cross-functional executive group to manage the provider.

Figure 2: How Companies Responded to Initial Outsourcing Challenges



Source: AberdeenGroup, July 2006

One chief information officer from a Best in Class firm cited this issue in response to an open-ended question Aberdeen asked in the survey about advice respondents would give on IT outsourcing. "Make sure you have the internal skills to effectively manage any outsourcing partner." An IT manager for another Best in Class enterprise adds: "If you have decided (to outsource), you need to commit 110% to succeed in it."

The Best in Class exhibit many other clear differentiators of success in this report (Table 1), among them:

- The effort in managing vendors is not much different for most firms in this group compared with Industry Average and Laggard firms;
- They are more likely than Industry Average or Laggard firms to use independent, help, such as consultants and lawyers, for input into an outsourcing decision;
- They are more likely to get the RFP and pricing right; and

Table 1: The Business Value of IT Outsourcing Competitive Framework

	Laggards	Industry Average	Best in Class
Process	Integration with out-sourcer at the operational and executive levels is not close.	More likely to implement new or revised vendor management processes or escalate problems with an outsourcer to its executives.	More likely to have the right vendor management and governance processes in place to manage out-sourcing providers.
Organization	CEOs and CIOs hold equal influence levels into outsourcing decisions, with CEOs more likely to make the final decision.	The CIO holds more sway than other C-level officers in an outsourcing decision, followed by the CEO.	The executive owner or board of directors is more likely to make final decision on strategic outsourcing More likely than Laggard and Industry Average firms to establish a cross-functional group to manage outsourcing.
Knowledge	Less likely than Industry Average or Best in Class to benchmark costs, contract terms, and SLAs against current market practices.	Less likely than Best in Class to reach outside the company for up-to-date outsourcing market information	More likely than Laggard and Industry Average firms to engage an independent outsourcing advisory firm to provide market intelligence and assist in building the business case and RFP.
Performance Management	Most have not achieved or have yet to achieve planned savings levels. Improved IT services delivery 10%	Most achieve planned savings levels within two years. Improved IT services delivery 13%	Most achieve planned savings levels within one year. Improved IT services delivery 14%.

Source: AberdeenGroup, July 2006

- The enterprise owner or board of directors is much more likely to make the final decisions on an outsourcing contract, indicating that pulling the trigger on an outsourcing deal is more a strategic than a tactical issue.

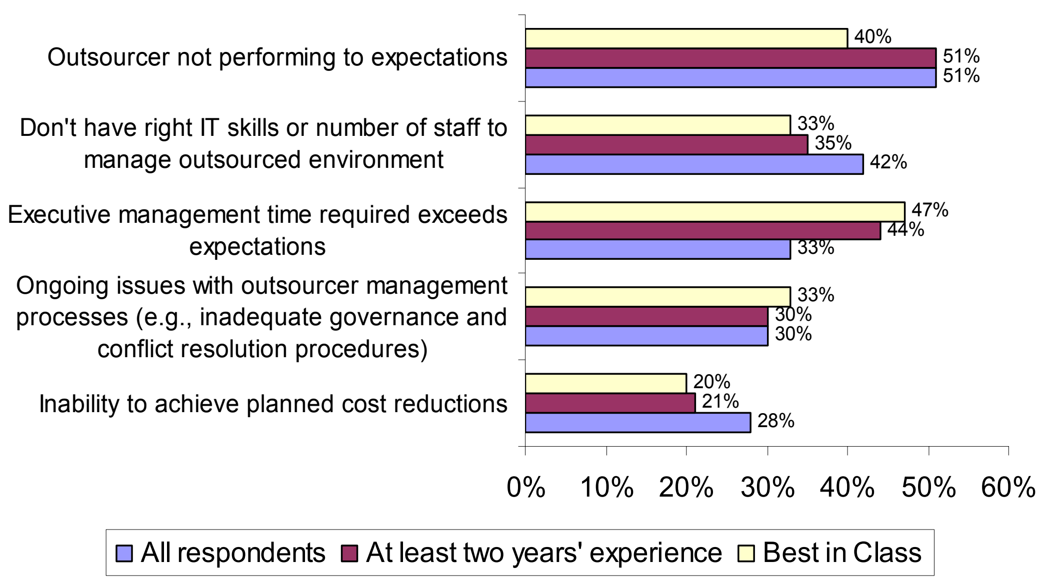
Challenges and Responses

If one were to examine the top challenges companies say they face with IT outsourcing contracts, he or she would conclude that problems lie in managing the outsourcing provider and having enough experience with outsourcing to set realistic expectations (Figure 3). In fact, many respondents cited these issues when we posed an open-ended question that asked for the advice they would provide a peer on how to maximize the business value in an outsourcing deal. The answers included the following comments:

- Get the requirements right but make sure to build in flexibility;
- Check the references of IT skills offered by the vendor;
- Plan well ahead and ensure the culture of your company accepts outsourcing; and
- Get the SLAs (service level agreements) right!

Even Best in Class companies and those who have at least two years of experience with IT outsourcing face the same challenges. However, with two key internally focused issues — insufficient skills and staff strength to manage the outsourcing providers and inability to achieve planned cost reductions — it appears that experience can help an enterprise achieve these objectives (Of the Best in Class, 58% have at least two years' experience with IT outsourcing; 11% have less than six months).

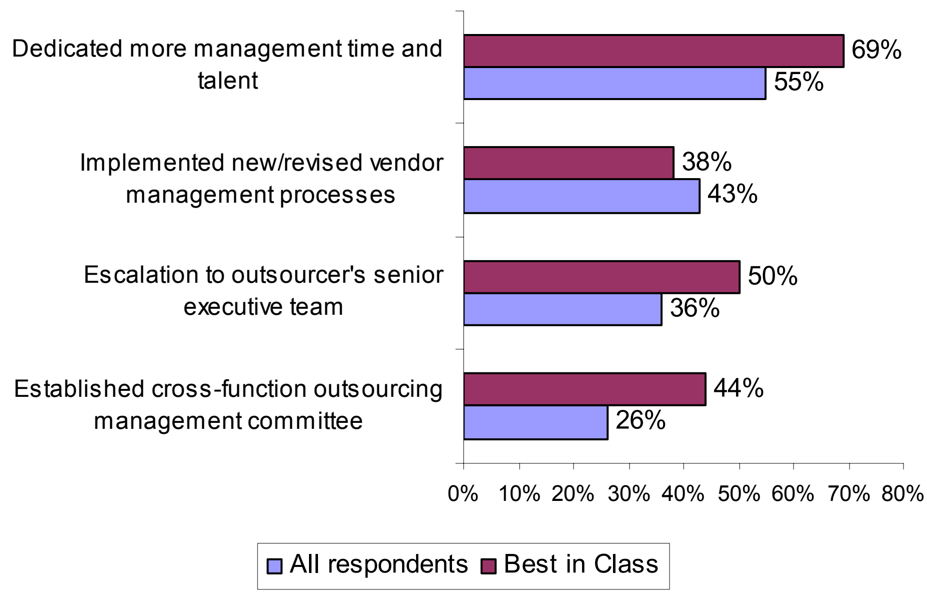
Figure 3: Top Challenges with Current IT Outsourcing Contracts



Source: AberdeenGroup, July 2006

To answer those challenges, most companies will add more management muscle or take up any issues with the outsourcing providers themselves (Figure 4). For Best in Class companies, these practices are more common. This highlights the importance of management and relationship management skills in driving the best possible value out of IT outsourcing relationships.

Figure 4: Responses to IT Outsourcing Challenges



Source: AberdeenGroup, July 2006

What's Being Outsourced?

Respondents were asked to rate their satisfaction with the IT functions they outsource. The highest reported satisfaction levels were in data center computing and operations and application development or maintenance (ADM) (Table 2). This is indicative of the high level of competition among vendors in these two areas. The rise of offshore providers in the ADM space has forced U.S.-based outsourcing vendors to compete for customers not just on the basis of price, but on quality as well. In particular, many offshore providers based in India have increased their levels of software process maturity to a point at which some providers have achieved the highest rating — Level 5 — of the Software Engineering Institute's Capability Maturity Model (CMM).

However, enterprises that outsource all of their IT functions are more likely than those that outsource only some IT work to express satisfaction or dissatisfaction with the quality of services they're receiving. For instance, enterprises that outsource all of IT reported broader satisfaction with business continuity and disaster recovery, as well as a broader dissatisfaction with the same service areas, rather than label the quality of their service delivery as "adequate." There are two notable exceptions for ADM and data center outsourcing, which received the highest mean ratings:

- **ADM**: The satisfaction gap between full and partial outsourcers was 10%, with companies that outsource all of ADM more satisfied. Enterprises that partially outsource were slightly more dissatisfied.
- **Data Center Computing**: Satisfaction was about even between the two groups, though full outsourcers expressed more dissatisfaction, by 9%, over partial outsourcers.

Table 2: Grades for Outsourced IT Activities (% represents proportion of companies offering a particular rating)

	Poor	Sub-Optimal	Adequate	Above Expectations	Excellent	MEAN RATING
Application Development and Maintenance (ADM)	8%	16%	48%	25%	4%	**3.01**
Data Center Computing and Operations	3%	24%	48%	16%	9%	**3.04**
End-User Computing (PCs, Help Desk)	7%	20%	55%	12%	5%	**2.89**
Business Continuity	6%	32%	47%	14%	2%	**2.73**
Disaster Recovery	10%	24%	51%	12%	3%	**2.74**
IT Security	5%	28%	51%	12%	5%	**2.85**
Voice Network Management	8%	23%	44%	23%	2%	**2.87**
Data Network Management	7%	12%	52%	20%	3%	**2.94**

(NOTE: Mean Rating represents a weighted average in which Poor = 1, Sub-Optimal = 2, Adequate = 3, Above Expectations = 4 and Excellent = 5)

Source: Aberdeen*Group*, July 2006

Now that many companies have discovered the savings potential of sending ADM work offshore, many of those same vendors are also offering infrastructure management services, such as data center operations and help desk/end user support. One survey respondent, an IT manager for a health care organization in the U.S., says her employer has sent batch processing functions to an India-based provider, which can do the work overnight because of the multi-hour time difference between the vendor and the home office. The client has one person to manage the provider and the two sides meet monthly to discuss the relationship. The vendor is "very responsive" to criticism and the two sides enjoy a positive working relationship, according to the IT manager.

Single Vendor vs. Multiple Vendors

The survey also indicated that it may be better to have "one throat to choke" when it comes to outsourcing some IT functions. Enterprises that use only one vendor in each IT function tend to be more satisfied with the value they're receiving. Yet, companies that use more than one vendor said they were more satisfied with data center computing and operations and data network management. The enterprises that use more than one vendor for the data center may be taking advantage of a competitive space in IT outsourcing to see which vendor can deliver the best service and value.

Meanwhile, in ADM, where single-vendor companies expressed more satisfaction, it may be easier for companies to manage application portfolio prioritization and cross-application integration and data models when the company works with a single third party that can perform high-quality work within the entire portfolio.

What if Your Company is NOT Outsourcing IT?

A full 25% of the respondents who answered the Aberdeen survey say their companies do not outsource IT (2% said they did but don't anymore). However, of that 25%, an overwhelming 80% are small or mid-size enterprises (less than $1 billion in annual revenue), compared with 65% for the entire survey pool. Because of their size, it's more common for small and mid-size companies to keep all of IT in-house. Meanwhile, large companies — which are more likely to pursue cost reduction as an ongoing corporate strategy — represent an overwhelming proportion of the 75% who say they outsource at least some IT functions now or plan to within the next year.

The top three reasons survey respondents gave for why their companies don't outsource IT have long been common:

- Loss of control of IT resources;
- IT is a core competency; and
- Company strategy does not include outsourcing.

Indeed, having a well run IT organization that serves the business well can effectively blunt calls for complete outsourcing or serve as a good reason to not pursue it. With today's pressures for companies to hold the line on costs and become more nimble to fulfill customer demand, gain market share, and grow profits, the IT function must be well managed and highly responsive. With growing global competition among outsourcing providers and new technologies helping to improve communication between an outsourcing provider and its customer, there are many options that allow companies to lower their operating costs and gain access to scarce technical resources while maintaining control of their IT operations.

But for the would-be customer, it all comes down to how effectively it can manage the supplier, being thorough in its requirements and RFP process, and holding the provider accountable for service delivery. After all, if the customer's IT organization is still in charge, it can be more difficult to fix a problem that had been in-house but later sent to a provider halfway around the world. As one respondent noted: "Go with someone who is the best at what they do; it isn't just about money."

Chapter Three: Implications & Analysis

Key Takeaways

- The most important step companies are taking to maximize the value they get from outsourcing IT functions is appointing a company officer who can be held accountable for improving outsourcing performance.
- You may need external help — a consultant, a lawyer, or both — in guiding you toward an outsourcing decision. Most Best in Class companies call on these experts.
- Among Best in Class firms, the CIO is more likely than any other C-level executive to make the final decision on an outsourcing contract. This highlights the increasingly strategic role CIOs are playing in companies that have experienced the best results from outsourcing. It also bodes well for the future stature of the role.

It's easy to just pull the trigger on an IT outsourcing arrangement if all you do is conduct a cost analysis. However, it's much more involved than that, and respondents to our survey are overwhelmingly adamant about proceeding with caution, holding the provider accountable for performance shortfalls, and managing the relationship effectively.

Aberdeen's PACE Framework for gaining value out of IT outsourcing (Table 4) highlights these issues, especially the actions enterprises take in responding to the pressures behind outsourcing, along with the capabilities and enablers they can employ to ease those pressures. While most of the steps companies take toward maximizing outsourcing value focus on management and processes, some use IT governance application software or call on an independent third party to perform periodic reviews of contracts and relationships (Note boldface items in Table 3).

Table 3: Top 5 Steps Organizations Take to Maximizing Business Value of IT Outsourcing Contracts

	AVG. RATING
Make a Company Officer Accountable for Outsourcing Performance	1.49
Retain Independent Third Party to Perform Periodic Contract/Relationship Reviews	**1.70**
Conduct Regular Internal Management Oversight and Review Discussions	1.75
Implement IT Governance Application Software	**1.85**
Design/Implement New or Revised Vendor Management Processes	1.86

(NOTE: Numbers represent weighted averages; respondents were asked to list their TOP THREE steps from among a list of 11 and rate them 1, 2, and 3 in order of priority)

Source: Aberdeen*Group*, July 2006

Table 4: PACE (Pressures, Actions, Capabilities, Enablers)

Priorities	Prioritized Pressures	Prioritized Actions	Prioritized Capabilities	Prioritized Enablers
1	**Outsourcer not performing to expectations.**	Implement new/revised vendor management processes Closely monitor vendor's compliance with contract obligations	Design or implement new or revised vendor management processes	Implement IT governance application software
2	**Company doesn't have right IT skills or number of staff to manage outsourced environment.**	Dedicate more management time and talent. Implement new/revised vendor management processes	Establish outsource management incentives that are tied to outsourcing quality and operational success.	Engage outside help (e.g., independent consulting firm) with outsourcing expertise
3	**Company can't achieve planned cost reductions.**	Use independent third party to identify and implement improvements. Change internal processes to reduce variable outsourcer charges	Benchmark costs, contract terms, and SLAs against current market practices	Engage outside help (e.g., independent consulting firm) with outsourcing expertise
4	**Executive management time required exceeds expectations.**	Dedicate more management time and talent. Establish cross-function outsourcing management committee. Redesign and reinforce retained organization and vendor management staff	Make a company officer accountable for outsourcing performance.	Deploy a collaborative program management system.
5	**Ongoing issues with outsourcer management processes (e.g., inadequate governance and conflict resolution procedures).**	Dedicate more management time and talent. Escalate issues to outsourcer's senior executive team. Renegotiate contract or statement of work	Conduct regular internal management oversight and review discussions. Establish quality management and key performance metrics	Deploy a collaborative program management system. Implement IT governance application software Deploy Business Activity Monitoring (BAM) software

Source: AberdeenGroup, July 2006

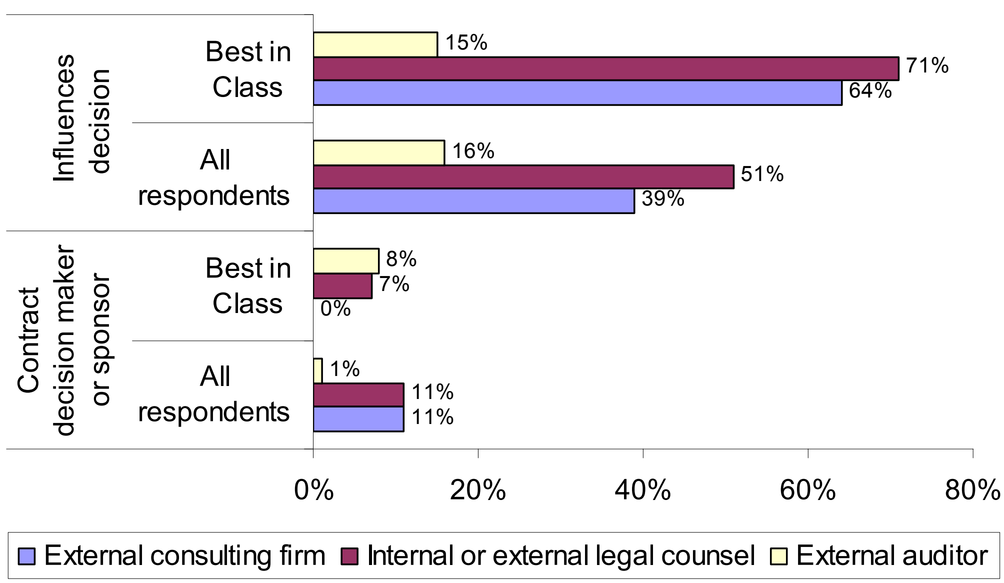
The Value of Outside Advice

The IT outsourcing marketplace is rapidly changing. Best in Class firms are more likely to get the specifics right — requirements, business case, RFP, service levels, pricing, vendor management processes — because they are more likely to retain independent consulting and legal firms with current marketplace intelligence. This allows Best in Class firms to set the right outsourcing expectations from the start.

There are other issues that come into play that enterprises must consider, notably risk management, the strength of both domestic and foreign communications infrastructures, as well as potential legal landmines, such as intellectual property laws. For example, an enterprise must take steps to ensure its application code doesn't fall into the wrong hands, especially a competitor's. Also, a country with political instability that is home to an outsourcing provider may cause a company to look elsewhere or line up potential backup providers that can take over the work with little or no downtime in transition.

That's where senior management may need some advice, and most Best in Class firms do call on outside advisory firms or inside legal counsel. Our survey found that it usually takes more than one senior executive — and sometimes even the owner or board of directors — to weigh in on whether to proceed with an IT outsourcing deal. But Best in Class enterprises are more apt to call on outside experts than the full survey field (Figure 5).

Figure 5: Role of Outside and Legal Assistance in IT Outsourcing Decisions



Source: AberdeenGroup, July 2006

The Role of the CIO

The survey also turned up intriguing findings regarding the strategic role of the chief information officer (CIO), especially in outsourcing deals. Among Best in Class companies, 44% of CIOs make the decision on outsourcing deals, the highest among senior-level executives at Best in Class companies. By contrast, only 37% of CIOs among the entire respondent pool enjoy that responsibility, second to the CEO (41%).

When it's time to review an IT outsourcing contract, it's usually the CIO who is involved, more so among Best in Class enterprises (Figure 6).

Figure 6: Executive Involvement in Periodic Review of IT Outsourcing Contracts

Source: AberdeenGroup, July 2006

This highlights how successful a CIO can be today in playing a strategic role in the business. The fact that CIOs exert more influence among Best in Class enterprises demonstrates that he or she can be an equal with other C-level executives. This is a marked change from the late 1990s, when business thought leaders questioned the role and long-term viability of the chief executive in charge of the IT organization.

Chapter Four: Recommendations for Action

Key Takeaways

- Laggards must increase their market knowledge and know what they want from outsourcing before coming to agreement on a contract.
- Industry Average firms must have strong business cases for maintaining and renewing outsourcing agreements and ensure the right internal processes are in place for managing providers.
- Best in Class firms must ensure they have detailed RFPs in place before sitting down with potential providers. And, don't be surprised if more executive involvement is needed after the provider begins its work.

Getting the best from any IT outsourcing arrangement is not only a matter of how much money the enterprise will save — unless that's the *only* goal. But for whatever price it pays, a company should receive the level of service it had built its business case on when deciding to ship out the work in question. Look for service improvements, better technical expertise, quick work turnaround, essentially whatever advantage you want to gain.

Here are our recommendations for enterprises that fall within each of the three groups within Aberdeen's Competitive Framework. These recommendations also apply to enterprises that are not outsourcing any IT, but may at least want to explore it.

Laggard Steps to Success

1) *Treat the outsourcing provider as part of your own company*. Getting the best out of an outsourcing arrangement means communicating and working with the provider closely enough that its representatives — i.e., those it has assigned to deliver the services for you — are treated as an extension of internal staff. If there is a service delivery problem, deal with the provider's team primarily, but don't hesitate to take it up with its senior executives if you believe it to be necessary.
2) *Increase your knowledge about measuring success.* To ensure the provider will perform to expectations, you need to have the right service-level agreement (SLA) metrics in place in a contract. Ensuring these means knowing what you want from a provider and how — as well as how often — you will gauge its performance. But do not confuse what your end users expect and need with the IT organization's metrics regarding typical service levels. There should be no ambiguity between customer and provider here.
3) *Seek wide-ranging feedback.* While the CEO and the CIO will likely hold the most sway in deciding on a contract, a cross-functional oversight committee can better ensure that the enterprise can escalate as many end-user concerns as possible over a provider's performance to the provider.

Industry Average Steps to Success

1) *Make sure the business case for outsourcing is solid*. If your company is already in the middle of an outsourcing arrangement — especially an initial deal — be sure there are good reasons for sustaining it when it comes time to renew the contract. Secure enterprise-wide feedback on service performance issues and conduct a financial analysis to determine whether — and where — the company is getting its money's worth.

2) *One throat to speak (or choke).* Hold one person accountable for managing the outsourcing relationship. This person must know what the provider needs to deliver, how it's performing its duties, and be aware of any end-user complaints. In addition, this person should have strong relationship management skills. If the provider is located offshore, this person must also have knowledge of the risks or potential risks that could stand in the way of acceptable provider performance.

3) *Don't be afraid to look outside for help.* Most Best in Class companies rely on independent consulting firms, and some bank on outside legal assistance before executing a contract. These professionals may be able to ask questions and find potential landmines the enterprise team may have overlooked. In the worst-case scenario, they won't and you'll have validation you're on the right track. Outside legal help may be beneficial given the complexities of outsourcing contracts. Outside consultants can provide essential benchmarking guidance at the RFP stage, and best practices and coaching through the relationship building and implementation phases.

4) *Look to automation.* The split responsibilities inherent in any outsourcing contract will amplify the project and relationship responsibilities for the organization, especially the IT department. IT governance application software can help; it's designed to measure, document, manage, and enforce policies in an outsourcing agreement.

Best in Class Next Steps

1) *Get the RFP right.* Securing what you want requires knowing all the details behind what you want, having a strong idea of what an outsourced service might cost *before* the bids come in, and knowing what advantages you want to gain from outsourcing. A few Best in Class companies cited no problems in their RFP work, but some indicated they had to rewrite them. Having a solid, detailed RFP can eliminate some vendors from contention and make it easier to decide which ones you may want to sit down and talk with further.

2) *Be ready to exert more executive effort than what you might have initially believed*. In our survey, the Best in Class were more likely than Industry Average and Laggard enterprises to say that executive oversight of an outsourcing deal took more time than originally expected. This also highlights the importance of holding one person responsible for overseeing the relationship. If that person has the right knowledge of the agreement and good relationship management skills, the enterprise may want to entrust him or her with making even some of the most critical decisions to avoid having to draw in other executives.

For Those That Are *Not* Outsourcing

This report should serve as a guide to the business value organizations are obtaining through outsourcing. By following the lead of the Best in Class, companies that are not outsourcing but considering it should avoid many of the hard lessons our survey participants have learned. For many, the first activity to outsource is voice and data networking.

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Rick Saia conducts research and analysis of IT services as part of Aberdeen's Information Technology practice. His current projects include research into the business value of IT outsourcing, as well as the outsourcing of data center operations and application development and management. He also contributed to the practice in 2005 and early 2006, assisting in data gathering and analysis for *The SOA in IT Benchmark Report* and helping in the formation of later surveys on enterprise applications and network application processing. He has extensive experience in writing and editing information technology research in previous senior-level editorial roles with *Computerworld* and *Cutter Consortium*.

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Appendix A:
Research Methodology

In June and July 2006, AberdeenGroup examined the issues, experiences, and intentions of more than 130 enterprises in information technology outsourcing from a variety of industries around the globe.

Responding executives, most of whom came from information technology functions, completed an online survey that included questions designed to determine the following:

- The pressures driving IT outsourcing agreements and the challenges their enterprises are experiencing as part of those agreements;
- The strategic actions enterprises are taking to help ease the pressures and solve the challenges;
- Enterprises' degrees of satisfaction with various aspects of IT outsourcing; and
- The benefits, if any, that they have derived from their IT outsourcing initiatives.

Aberdeen supplemented this online survey effort with telephone interviews with select survey respondents, gathering additional information on IT outsourcing strategies, experiences, and results.

The study aimed to identify emerging best practices for IT outsourcing and provide a framework by which readers could assess their own capabilities for driving the best possible value from IT outsourcing.

Responding enterprises included the following:

- ***Job title/function**:* The research sample included respondents with the following job titles: manager (26%); senior management (CEO, CFO, COO) (18%); CIO/IT leader (16%); internal consultant (14%); director (11%); senior vice president (6%); staff (4%); and other (3%). Among functional areas of responsibility, Information Technology was the most widely represented (56%), followed by business process management (11%); marketing (9%); and sales (7%). Other respondents came from procurement (3%), customer service (2%), finance (2%); manufacturing and logistics/supply chain (1% each).
- ***Industry**:* The research sample included respondents predominantly from manufacturing industries, led by high technology/software at 28%, followed by computer equipment and peripherals (6%) and automotive and pharmaceuticals (4% each). Other manufacturing industries represented in the sample were from the following: apparel, chemicals, construction/architecture/engineering, food/beverage, industrial equipment manufacturing, medical devices, mining/oil/gas, paper/lumber/timber, and telecommunication equipment. Among service industries, 13% of the survey pool came from finance/banking/accounting, followed by telecommunications services (9%), and education (4%). Others came from distribution, health/medical/dental services, public sector, publishing/media, retail, transportation/logistics, travel/hospitality/restaurant, and wholesale.

- ***Geography:*** Forty-four percent of the study respondents were from North America (U.S., Canada, Mexico), with 34% from Europe, 14% from Asia/Pacific, 6% from the Middle East and Africa, and 2% from South/Central America and The Caribbean.
- ***Company size:*** About 29% of respondents were from large enterprises (annual revenues above US$1 billion); 27% were from midsize enterprises (annual revenues between $50 million and $1 billion); and 44% of respondents were from small businesses ($50 million or less).

Solution providers recognized as sponsors of this report were solicited after the fact and had no substantive influence on the direction of *The Business Value of IT Outsourcing Benchmark Report*. Their sponsorship has made it possible for **Aberdeen*Group*** to make these findings available to readers at no charge.

Table 5: PACE Framework

PACE Key

Aberdeen applies a methodology to benchmark research that evaluates the business pressures, actions, capabilities, and enablers (PACE) that indicate corporate behavior in specific business processes. These terms are defined as follows:

Pressures — external forces that impact an organization's market position, competitiveness, or business operations (e.g., economic, political and regulatory, technology, changing customer preferences, competitive)

Actions — the strategic approaches that an organization takes in response to industry pressures (e.g., align the corporate business model to leverage industry opportunities, such as product/service strategy, target markets, financial strategy, go-to-market, and sales strategy)

Capabilities — the business process competencies required to execute corporate strategy (e.g., skilled people, brand, market positioning, viable products/services, ecosystem partners, financing)

Enablers — the key functionality of technology solutions required to support the organization's enabling business practices (e.g., development platform, applications, network connectivity, user interface, training and support, partner interfaces, data cleansing, and management)

Source: Aberdeen*Group*, July 2006

Table 6: Relationship between PACE and Competitive Framework

PACE and Competitive Framework How They Interact

Aberdeen research indicates that companies that identify the most impactful pressures and take the most transformational and effective actions are most likely to achieve superior performance. The level of competitive performance that a company achieves is strongly determined by the PACE choices that they make and how well they execute.

Source: Aberdeen*Group*, July 2006

Appendix B:
Related Aberdeen Research & Tools

Related Aberdeen research that forms a companion or reference to this report include:

- *The Business Value in IT Outsourcing* (May 2006)
- *Enterprise Service Bus and SOA Middleware* (June 2006)
- *The Compliance Gap Benchmark Report* (June 2006)
- *The Procurement Outsourcing Benchmark Report* (May 2006)
- *The SOA in IT Benchmark Report* (December 2005)

Information on these and any other Aberdeen publications can be found at www.Aberdeen.com.

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AberdeenGroup

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To be the trusted advisor and business value research destination of choice for the Global Business Executive.

Our Approach

Aberdeen delivers unbiased, primary research that helps enterprises derive tangible business value from technology-enabled solutions. Through continuous benchmarking and analysis of value chain practices, Aberdeen offers a unique mix of research, tools, and services to help Global Business Executives accomplish the following:

- IMPROVE the financial and competitive position of their business now
- PRIORITIZE operational improvement areas to drive immediate, tangible value to their business
- LEVERAGE information technology for tangible business value.

Aberdeen also offers selected solution providers fact-based tools and services to empower and equip them to accomplish the following:

- CREATE DEMAND, by reaching the right level of executives in companies where their solutions can deliver differentiated results
- ACCELERATE SALES, by accessing executive decision-makers who need a solution and arming the sales team with fact-based differentiation around business impact
- EXPAND CUSTOMERS, by fortifying their value proposition with independent fact-based research and demonstrating installed base proof points

Our History of Integrity

Aberdeen was founded in 1988 to conduct fact-based, unbiased research that delivers tangible value to executives trying to advance their businesses with technology-enabled solutions.

Aberdeen's integrity has always been and always will be beyond reproach. We provide independent research and analysis of the dynamics underlying specific technology-enabled business strategies, market trends, and technology solutions. While some reports or portions of reports may be underwritten by corporate sponsors, Aberdeen's research findings are never influenced by any of these sponsors.

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Founded in 1988, Aberdeen*Group* is the technology-driven research destination of choice for the global business executive. Aberdeen*Group* has over 100,000 research members in over 36 countries around the world that both participate in and direct the most comprehensive technology-driven value chain research in the market. Through its continued fact-based research, benchmarking, and actionable analysis, Aberdeen*Group* offers global business and technology executives a unique mix of actionable research, KPIs, tools, and services.

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