

EquaSiis Market Assessment

Data, Research and Analysis on the Global Business and IT Services Markets

The Findings

Market Pulse Update: Outsourcing Demand Holds Steady – What Can and Should Service Providers Do to Accelerate?

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The recently completed 2Q09 EquaTerra Pulse survey found that growth in buyer demand for outsourcing remained stable in the second quarter after a sharp increase at the beginning of this year. Global sourcing usage remains steady despite market noise to the contrary, though there is an uptick in demand for nearshore and onshore services and offshore services in locations other than India. The economy remains the dominant factor impacting demand and deal flow, mostly in a positive way.

The following list summarizes the key findings of the 2Q09 EquaTerra Pulse survey:

- Forty-six percent of EquaTerra advisors indicated that third-party business and information technology (IT) services demand levels were up overall in the quarter. This is a decrease of 3 percent over last quarter but an 8 percent increase from the second quarter of 2008. It is below the average response of 53 percent for all EquaTerra Pulse surveys to date.
- Just 7 percent of advisors felt that demand declined during the quarter, in line with the survey average but down 3 percent from last quarter.
- Demand levels were generally similar across geographic and functional areas. However, advisors supporting work in Europe were somewhat less positive about overall customer demand growth than those in the Americas. Please see the survey's appendix for a complete breakdown of response levels by location and type of work supported.
- Sixty-five percent of service providers polled noticed pipeline growth during the quarter. This level is up 8 percent quarter over quarter and 13 percent year over year and 11 percent over the survey average. It is the highest level recorded since the second quarter of 2006.

The acute need to reduce costs and overhaul operating models will continue to drive more outsourcing deal flow into the market, resulting in an increase in signed deals in the second half of 2009. Protectionist trade policies, anti-outsourcing rhetoric and anti-globalization efforts will continue expanding in most Western markets with limited impact on overall outsourcing levels, though specific measures will complicate some individual buyers' agendas. However, demand for other types of third-party services – such as unbundled consulting and more discretionary application development work – will remain weak throughout 2009.

The 2Q09 EquaTerra Pulse survey found that buyers are becoming more aggressive in their use of global or offshore resources in their outsourcing efforts. This is despite the noted growth in

protectionism, calls to create and keep more jobs in local markets, and the increased supply of lower-cost labor in Western markets. The reality is that the combination of the critical need to reduce costs and the quantity of quality services available offshore outweighs the factors pushing back against global sourcing.

The nature of global sourcing is changing, and customers today are more likely to source from multiple locations – often beyond India – and structure their sourcing efforts as a portfolio rather than a series of point-to-point or country-to-country initiatives. Buyers are frequently deploying a mix of service delivery models that include onshore and nearshore outsourcing coupled with work carried out further offshore. Offshore work is performed either by a third party or through captive operations, though the appeal of captives continues to slip or minimally evolve toward delivering a more specialized set of services. Figure 1 illustrates the usage trends for different global service delivery models.

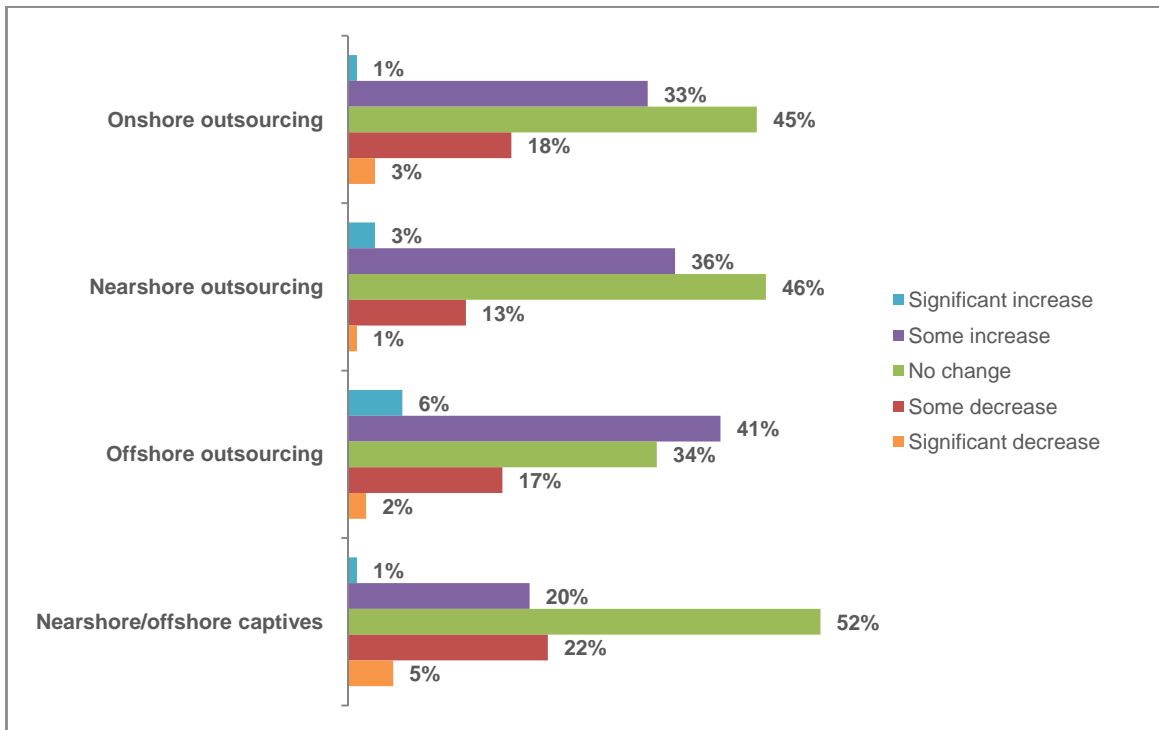


Figure 1 – Change in Sourcing Model Preference and Demand

Other key findings from the 2Q09 EquaTerra Pulse survey include the following:

- Pricing pressure:** Fifty-three percent of outsourcers polled felt that pricing pressure rose in the quarter. India-based providers in particular indicated that they are seeing increased pricing aggressiveness. While this is a high percentage, it represents a decline of over 20 percent from last quarter.

- **Sales cycles:** Twenty-five percent of service providers indicated that sales cycles lengthened. This level is higher than the survey average but marks the first quarter-over-quarter decline since the end of 2007.
- **Deal scope levels:** Twenty-six percent of providers indicated that deal scope levels decreased. This is the highest percentage ever recorded in an EquaTerra Pulse survey. Twenty-six percent felt that scope levels increased, down 3 percent from last quarter and representing the third straight quarterly decline.
- **Outsourcing transitions:** Both advisors and outsourcers agreed that most buyers struggle with outsourcing transition efforts. This is not necessarily news or a surprise, but difficult transitions can quickly lead to problematic outsourcing efforts from which some buyers never recover.

The Advice

Service providers are currently in a good position to accelerate the increased flow of outsourcing deals into the market. Demand is strong and continues to grow among buyers that recognize global economic and market conditions have fundamentally changed and so too must their models for delivering a broad range of supporting operational services. The question is less about why and more around how to do it well when it comes to outsourcing. Forward-thinking customers are proactively preparing for an economic upturn and assessing how they can apply more focus and resources to gaining market share. This often involves shifting resources away from and reducing the complexity and costs of less value-added back office activities. Either way, the demand for outsourcing grows.

Nevertheless, not every outsourcer will come out a winner in today's market. Just as negative market conditions serve to thin the herd and eliminate weaker, slower-moving and slower-to-adapt buyer organizations, so too will they affect business and IT services providers. Credentials, capabilities, ability to execute and strategic insights will characterize the providers that emerge as or remain market leaders coming out of this economic slump.

There are several tactical points that all service providers must keep in mind in the current market.

- **Maintain focus on quick hits, clear business cases and return on investment (ROI).** Buyers still have short time frames for achieving the benefits of any change efforts. While they may enter into a five-year outsourcing deal, they need to realize tangible benefits as soon as possible. It is important that any business case is realistic, clearly defined and easy to validate.
- **Give some, and take some.** Providers that are adept at haggling well – but fairly – are in an especially good position. Buyers have long lists of wants (for example, lower prices, better service levels, quicker ROI, less mistakes and better terms), but outsourcers must defend, promote and satisfy their own needs (that is, maintain or improve margins, expand scope, move more work offshore, or gain extended terms). The ability to compromise as amicably as

possible on a fair set of concessions and gains is the key to winning new business and maintaining existing relationships.

- **Leverage global sourcing capabilities.** As the 2Q09 EquaTerra Pulse survey illustrates, global sourcing continues to grow and become more pervasive despite the market rhetoric. This is both a challenge and an opportunity for many providers. The challenge comes from more sophisticated buyers that prefer different services delivered via multiple locations and delivery models. This requires a level of coordination, integration and management well beyond that which is required to deliver a relatively straightforward service – such as call center support or applications development and maintenance (ADM) – from one offshore location back to the West.
- **Emphasize rapid and clean (as much as possible) transitions.** Over one half of the EquaTerra advisors polled in the survey indicated that transitions almost always or frequently have a negative impact on the start of buyer/service provider relationships. This has serious implications for the long-term health of any outsourcing effort. While there is no such thing as a painless transition, providers must work aggressively to limit the amount and duration of the pain. There are many ways to do this, including limiting upfront transformation work; pushing for standardized, over-customized solutions; taking an incremental approach to larger deals or change efforts; simplifying the transition requirements and addressing them in an iterative fashion; and, above all, ensuring that customers understand transition realities and their role in the process.

Conclusion

The market for third-party business and IT services remained stable in the second quarter of this year, according to the EquaTerra advisors and third-party business and IT service providers polled in the 2Q09 EquaTerra Pulse survey. Demand levels were positive and in line with those from last quarter and last year. The economy remains the dominant factor impacting buyer demand and deal flow, mostly in a positive way.

Global sourcing usage is growing – despite market noise to the contrary – and the demand for offshore services in locations other than India is expanding. The need and desire to cut costs outweighs other factors that detract from global sourcing, such as trade protectionism and the increased availability of labor at the lowest cost in several years in Western markets. There is also more interest in nearshore services, which is an indicator of the overall growth of all outsourcing models and buyer desires to take advantage of good deals wherever they can find them.

Additional Resources

[Full 2Q09 EquaTerra Pulse Survey Results](#)

About EquaSiis

EquaSiis, an EquaTerra company, provides software and services that improve the business support services lifestyle for shared services, outsourcing practitioners and service providers. The software, EquaSiis Workbench and EquaSiis Enterprise, is a framework for collaboration used during the service delivery assessment and sourcing process to assist in analysis and decision making for shared services or outsourcing. EquaSiis provides intelligence and optimization for the delivery of business support services across the entire organization. The company also offers service providers market intelligence, research, customer satisfaction and trending data through its Insights group. For more details about EquaSiis' research offerings, please contact Stan Lepeak, stan.lepeak@equasiis.com.

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