



Steering Clear of the IT Danger Zones

In this *Executive Insights* Analysis on Technology, L.E.K. Consulting examines the key drivers behind the global growth in IT services, changing behaviors of IT services buyers – and how vendors and investors can steer clear of danger zones.









Steering Clear of the IT Danger Zones was conducted by **Aaron Smith, Darren Perry** and **Harsha Madannavar**, Managing Directors in L.E.K. Consulting's Technology practice. Aaron and Harsha are based in San Francisco and Darren is based in Boston.

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What's driving global growth in IT services?

Companies increasingly seek to maximize operating flexibility by taking advantage of IT services that help migrate their industry-specific business processes to the cloud.

Key market demand drivers over the next 3-5 years	Regions impacted	Segments impacted	W.W. market
<p>Migration toward the cloud</p> <p>Customers need help developing customized cloud strategies; however, cloud reduces demand for on-premises ITO services, cannibalizing traditional offerings</p>	Largest impact in U.S.; China earlier in adoption curve, and EU lagging	Applications Infrastructure Technology Outsourcing	 
<p>Moderated macroeconomic growth</p> <p>Spending on IT services contracted during the most recent global slowdown, but has since improved with macro conditions</p>	U.S. strong, with EU beginning to strengthen and APAC softness expected to continue	All segments	
<p>Increasing IT complexity / resource constraints</p> <p>Increased IT heterogeneity heightens demand for specialized expertise; an industry talent shortage has made finding required IT skill sets more difficult</p>	Worldwide trend	Infrastructure Technology Outsourcing	
<p>Industry-specific demand for technology offerings</p> <p>Customers are demanding new ways to view and interact with data, driving industries (e.g., banking) to bolster offerings</p>	Worldwide trend	Applications	
<p>Growing pricing pressures</p> <p>IT services prices have increased in line with inflation; commoditization of ITO is putting some pressure on prices overall</p>	Worldwide trend; strong APAC pricing pressures	All segments	

Source: L.E.K. survey, interviews and analysis

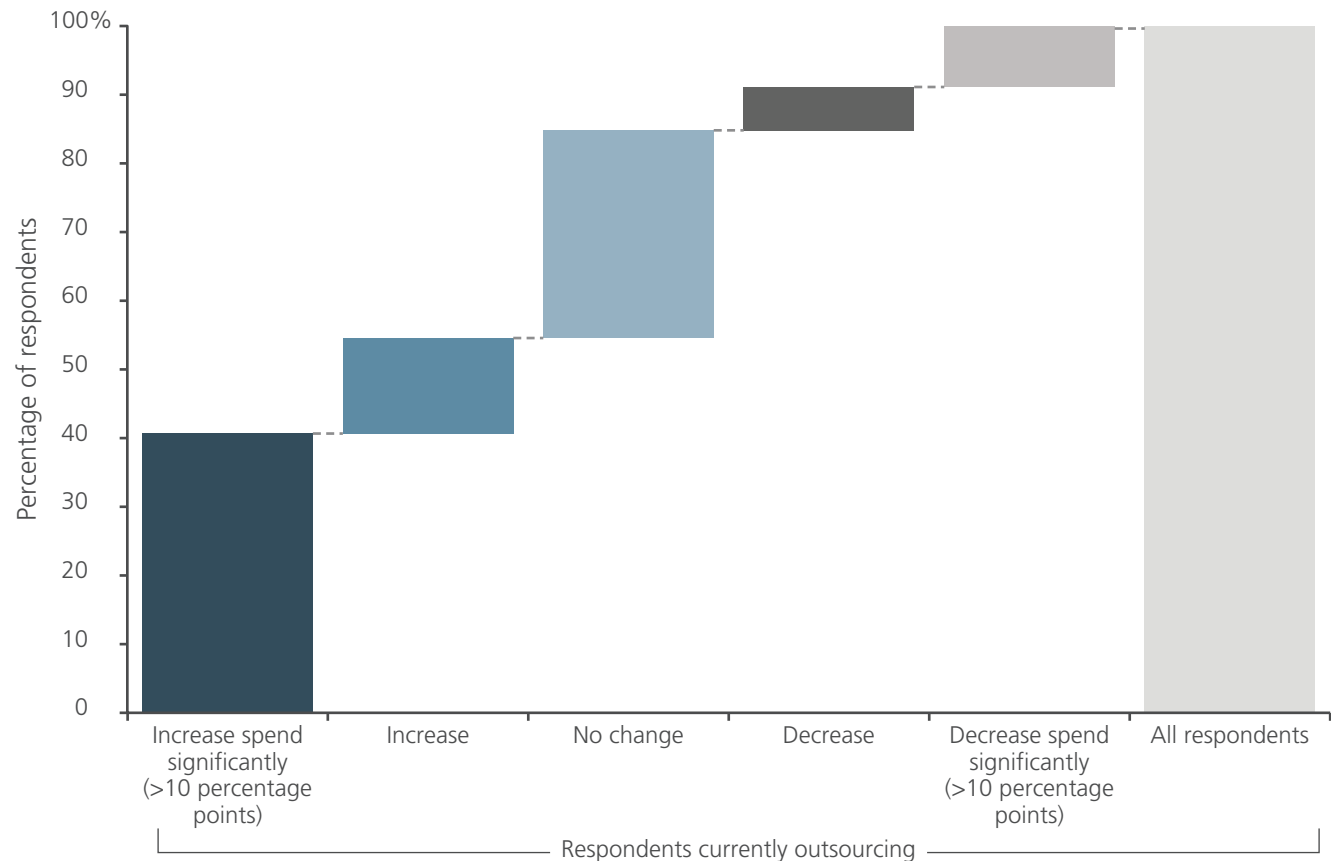
What market trends underpin demand? ►

Most companies expect to increase their spend on outsourced IT

To realize better returns on their IT dollars, companies are increasing their outsourcing relationships with vendors.

Over half of all senior executives surveyed expect to increase their level of IT outsourcing over the next three years, with a majority of those expecting to spend 10 percentage points or more on outsourcing compared with last year.

Expectations for outsourcing over the next 3 years



Source: L.E.K. survey, interviews and analysis

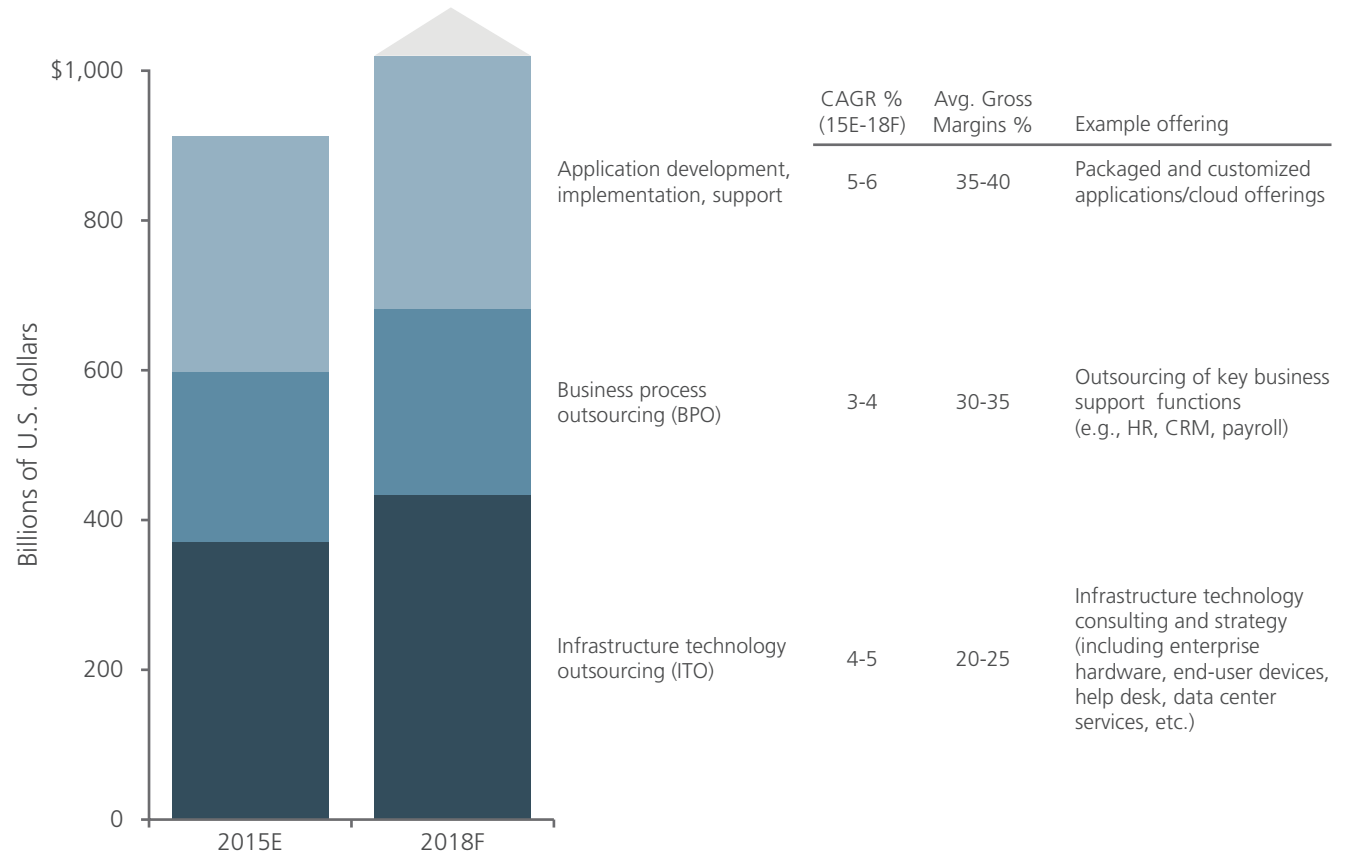
What market trends underpin demand? ►

Outsourced IT has huge upside — \$1 trillion in annual spend by 2018

At face value, almost all service lines are expected to experience some growth and appear attractive.

Upon closer examination, however, those services that more directly drive workflow productivity gains are expected to generate higher revenue and/or margin opportunity for vendors.

Enterprise IT services – W.W.
(2015E-18F)



Source: L.E.K. survey, interviews and analysis

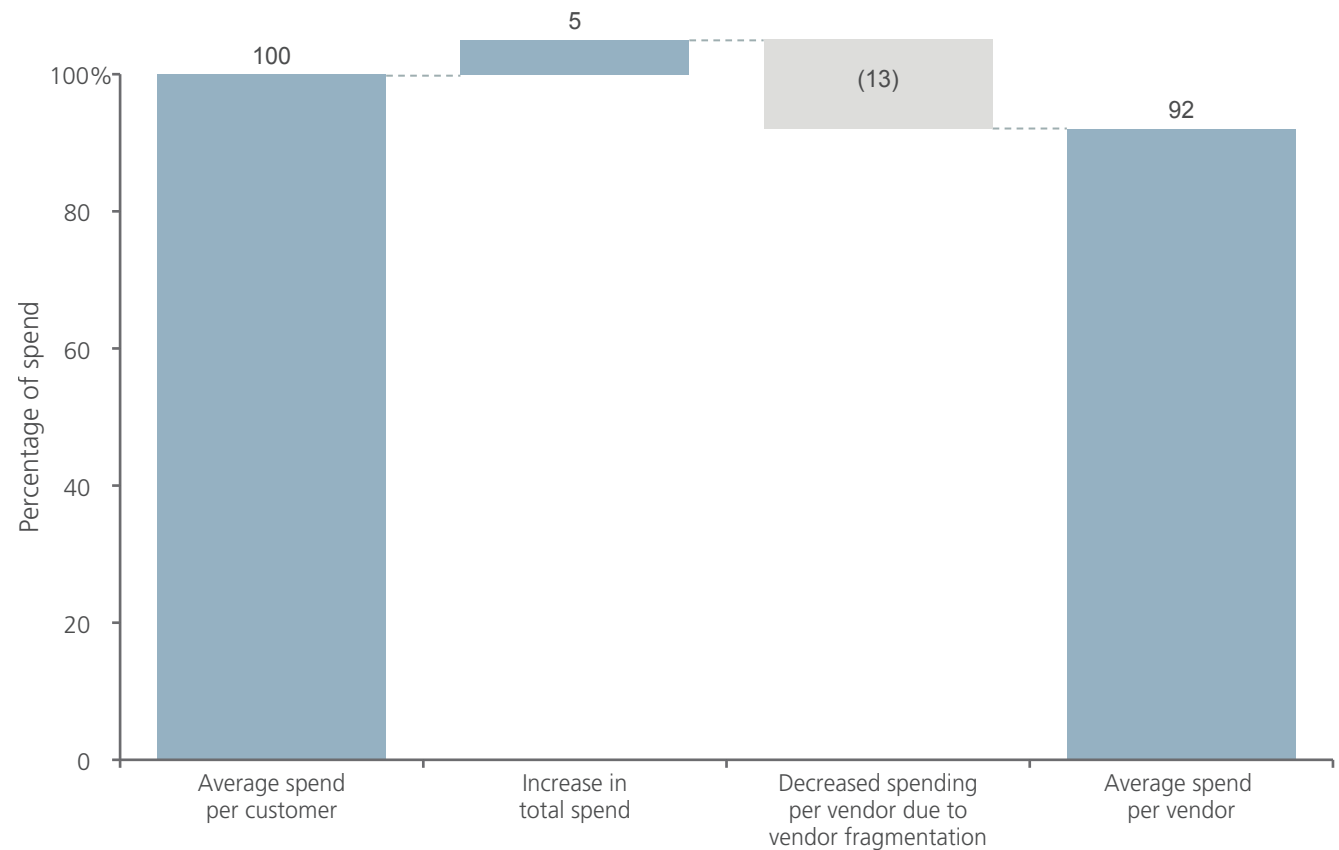
How are customers utilizing vendors? ►

Fragmented IT spend: more on specialized service providers, less on legacy providers

Although companies are increasing IT services spending overall, they are also utilizing more vendors to meet the growing complexity of their business and operational needs.

As a consequence, vendors must accelerate new-customer wins or successfully increase their share-of-wallet to keep pace with overall industry growth.

Expected change in customer spending per vendor



Source: L.E.K. survey, interviews and analysis

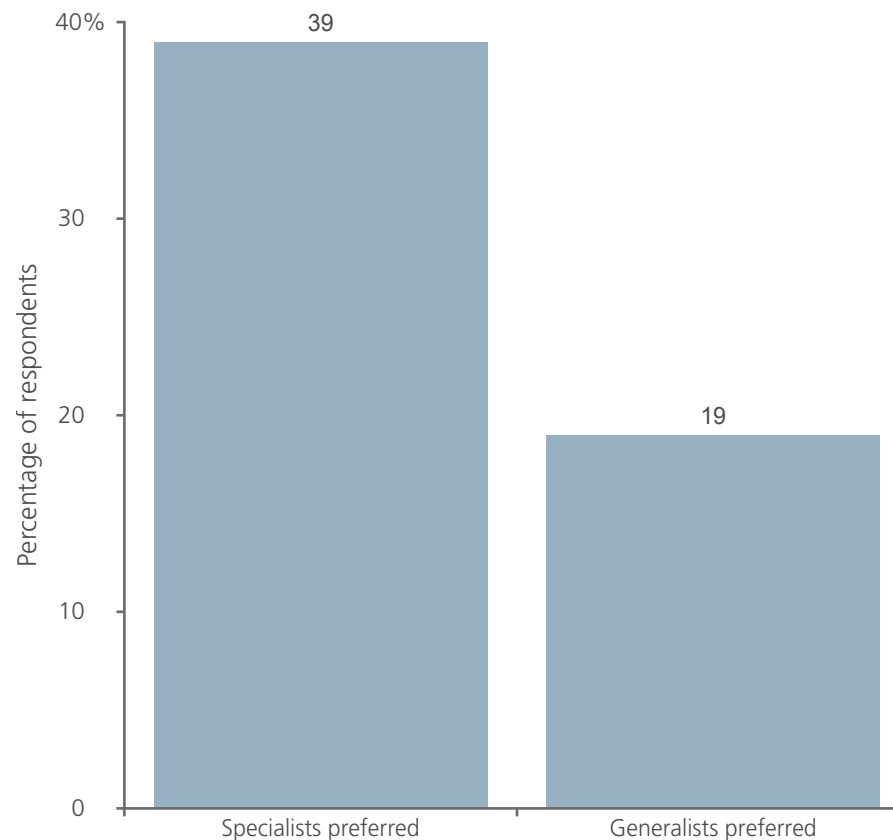
What vendors are winning or losing? ►

Specialists preferred by 2-to-1 margin over generalist vendors

Companies are shifting spending away from undifferentiated generalist service providers and toward specialist providers, demonstrating increasing confidence that specialists will deliver meaningful business impact.

Service providers that don't tailor their offering to the customers' nuanced business needs are expected to struggle, particularly as companies increasingly realize more value from specialists than from generalist IT services vendors.

Customer preference for using specialist vs. generalist IT service providers



Source: L.E.K. survey, interviews and analysis

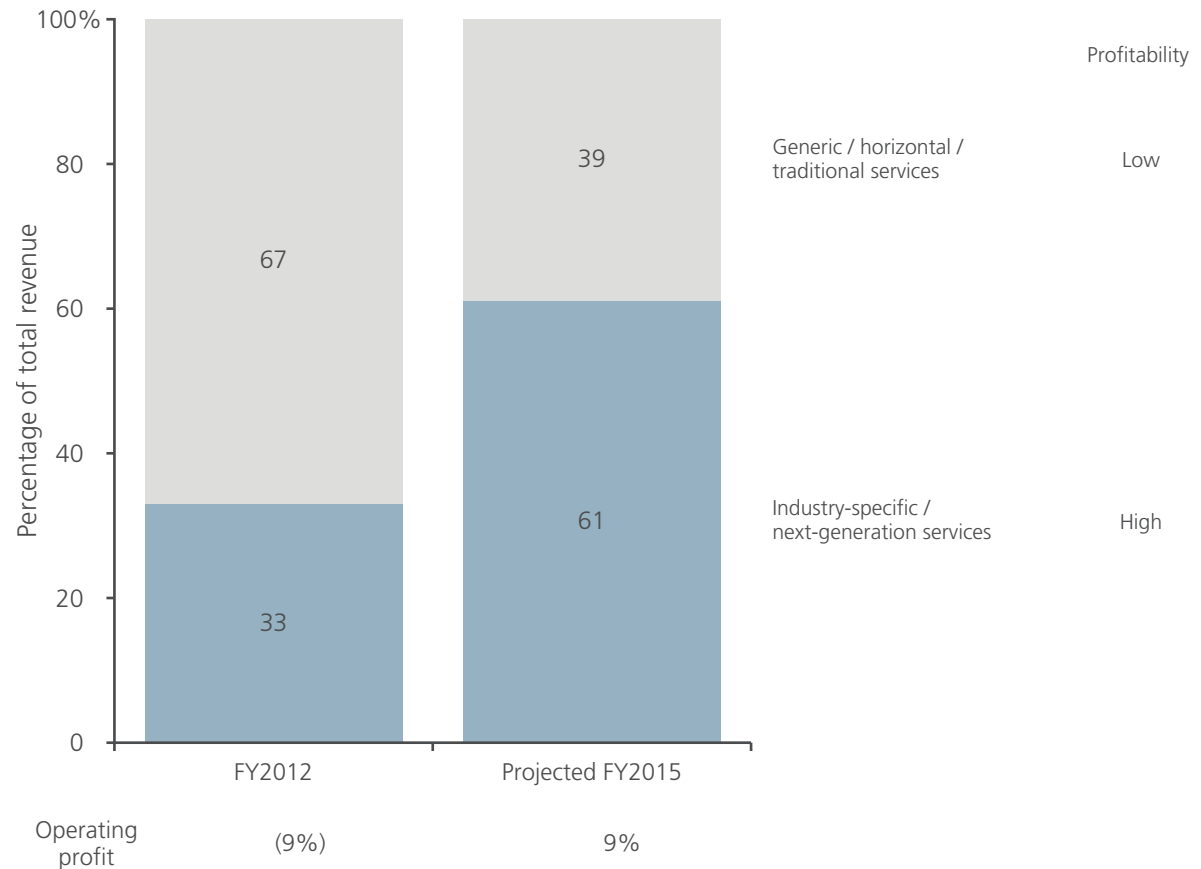
How are vendors capitalizing on these trends? ►

Generalist vendor response: aggressive moves to meet new market realities

To address IT services needs, CSC has pivoted from its focus on traditional lower-margin/low-growth infrastructure and horizontal applications toward more attractive spaces such as industry-specific solutions, cloud infrastructure, big data, security, etc.

This shift in perspective has resulted in higher profitability, as customers are willing to pay more for these services.

CSC revenue by service type (FY2012, projected FY2015)



Source: CSC; L.E.K. survey, interviews and analysis

What are the key issues for operators or investors? ►

Implications for vendors and investors: big opportunities for those who know where to look

Our *Executive Insights* Spotlight on IT Services series provides a perspective on IT services spending trends and evolving customer purchase behaviors – particularly their growing appetite for specialized vendors.

Tomorrow's winners will be those players that know the danger zones to avoid and can pinpoint where to exploit the greatest opportunities in a fast-changing market that rewards responsiveness and specialized capabilities.

Key considerations for evaluating IT services investments

Build specific capabilities to deliberately accelerate differentiators in a well-defined set of functional or industry-specific solution areas
Ensure ongoing investments in organization, systems and processes continuously improve the delivery effectiveness of cloud/next generation-oriented services
Measure the effectiveness of SLAs primarily against contribution to customers' most relevant business metrics
Understand the triggers behind timely changes in customer satisfaction scores to quickly uncover areas requiring attention/additional investment
Segment customers based on spending behaviors and appetite to pace change, accordingly engage customers with a tailored services adoption roadmap
Focus on driving scale and extracting as much operating inefficiency out of undifferentiated service lines such as infrastructure technology outsourcing

About the Authors



Aaron Smith is a Managing Director and Partner, as well as the head of L.E.K. Consulting's San Francisco office. He specializes in analytics-focused engagements. Recent engagements have included developing a pricing strategy, optimizing a supply network, conducting extensive market

forecasting, and establishing business process optimization initiatives. Aaron is also an active member in our Building Materials & Industrial Products, Private Equity, Surface Transport & Logistics and Technology practices.



Darren Perry is a Managing Director and Partner in L.E.K. Consulting's Boston office. He has more than 10 years of growth-oriented strategy consulting experience and works with clients to assess strategic options in new markets and new products, construct business plans in conjunction with developing

new growth strategies, and evaluate merger and acquisition opportunities. Darren advises clients across a variety of sectors, including aviation, aerospace & defense and technology.



Harsha Madannavar is a Principal in L.E.K. Consulting's San Francisco office. He has more than 17 years of experience in the technology sector and strategy consulting space. Harsha has an MBA from Columbia Business School, a Masters in International Management from Thunderbird, and a Bachelors in Instrumentation Engineering from University of Mysore.

About L.E.K. Consulting

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