

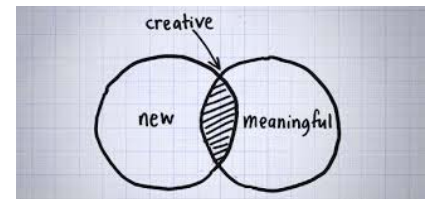


Executive report: The State of Services & Outsourcing in 2014

“Things will never be the same again”

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Services and outsourcing have entered a phase of very significant disruption

Outsourcing is teetering at a crucial juncture between providing genuine value and low-cost staff augmentation. Providers need to prove they can do more than basic operations, otherwise outsourcing runs the risk of becoming a staff augmentation model for flexing operations as opposed to a strategic partnership between provider and buyer that can add more skill, technology, and analytical capability for clients.

The conversation is moving rapidly away from process improvement and cost reduction:

- Anything *rules-based* must be automated/moved into the cloud/outsourced
- Labor costs are the *new dirty word*
- Businesses are increasingly *externalizing* their services supply chain
- Transactional talent needs to become *digital talent*
- We are on the verge of *knowledge creation* instead of mass collection of unstructured data. That is the true value driver in analytics.

Services and outsourcing has entered a phase of unparalleled disruption (continued)

Decisions are *rapidly democratizing*—very different from three years ago

Information is suddenly everywhere—the *pace of new thinking* (and noise) is staggering

We are entering into a period of genuine secular change for the services and outsourcing industry—things will never be the same...and those who are only just realizing this may already be too late

Executive findings

Both shared services and outsourcing are on the increase. One in four enterprise buyers are reinvesting heavily in their global shared services operations, while seven out of ten are continuing to make (largely moderate) investments in their outsourcing delivery.

Integrated global services models that incorporate both shared services and outsourcing are the core focus for most enterprises. Approximately 56 percent are already increasing investments in their centralized hybrid governance function to manage their mix of service delivery models.

Buyers are shifting more of their higher-value work into their offshore shared services. Three out of ten enterprises are *increasing* the offshore component of their finance and accounting, over the next year, with similar trends are occurring across IT, procurement, HR, industry-specific, and customer service functions. This next wave of business processes typically entails a greater deal of context and specificity to the business.

Executive findings (continued)

Clients are rapidly losing patience with services providers that aren't working proactively with them to provide more value than the basic terms of the original contract. Many clients are actively looking to *fire* their provider if they cannot get past operational teething issues and actively begin the process of transforming the way they do things. Outsourcing is no longer about achieving significant cost reduction targets and getting basic tactical operations functional—is about moving clients into a future state that is much more effective than the current one.

Sixty percent see operational analytics as a very important outsourcing outcome, and a similar majority are already expecting their providers to provide savvy talent and better technology within two years. The onus on clients to move the conversation to one of better analytical capability, more savvy and creative support talent, access to better tools and tech, has leapt onto the table: these are the new stakes. It is already very clear that an increasing majority of enterprise clients expect their providers to bring these skills to the table.

Two-thirds of enterprises are falling short in “digital” areas. The internal skills to change processes, automate them, analyze them, or come up with creative thinking on how to improve operations, is widely cited as lacking. A major talent crunch is coming and enterprises need to prepare.

Executive findings (continued)

Forty nine percent of today's enterprise buyers expect to move to a "wide-scale transformation of business processes enabled by new technology tools/platforms" in just two years. This may be a pipe-dream for some enterprises, but what is clear is that many of those operations leaders failing to steer their enterprises away from legacy delivery models will get cast aside quickly in today's tolerance-diminishing business environment.

Ambitious and sophisticated clients are now seeing the huge benefits of shifting from on-premise to "as-a-Service" delivery and many now view BPaaS as an alternative to outsourcing. This isn't something that is occurring in a few years, it's already happening where our latest research shows close to one-in-three enterprises already using (or about to use) BPaaS/cloud as an alternative to legacy outsourcing in areas such as HR, industry-specific operations, finance and accounting, and procurement.

Analytics and process automation technologies have emerged as critical technologies to drive better outcomes for clients. Close to half of buyers now see these two technologies as adding significant value in their outsourcing engagements.

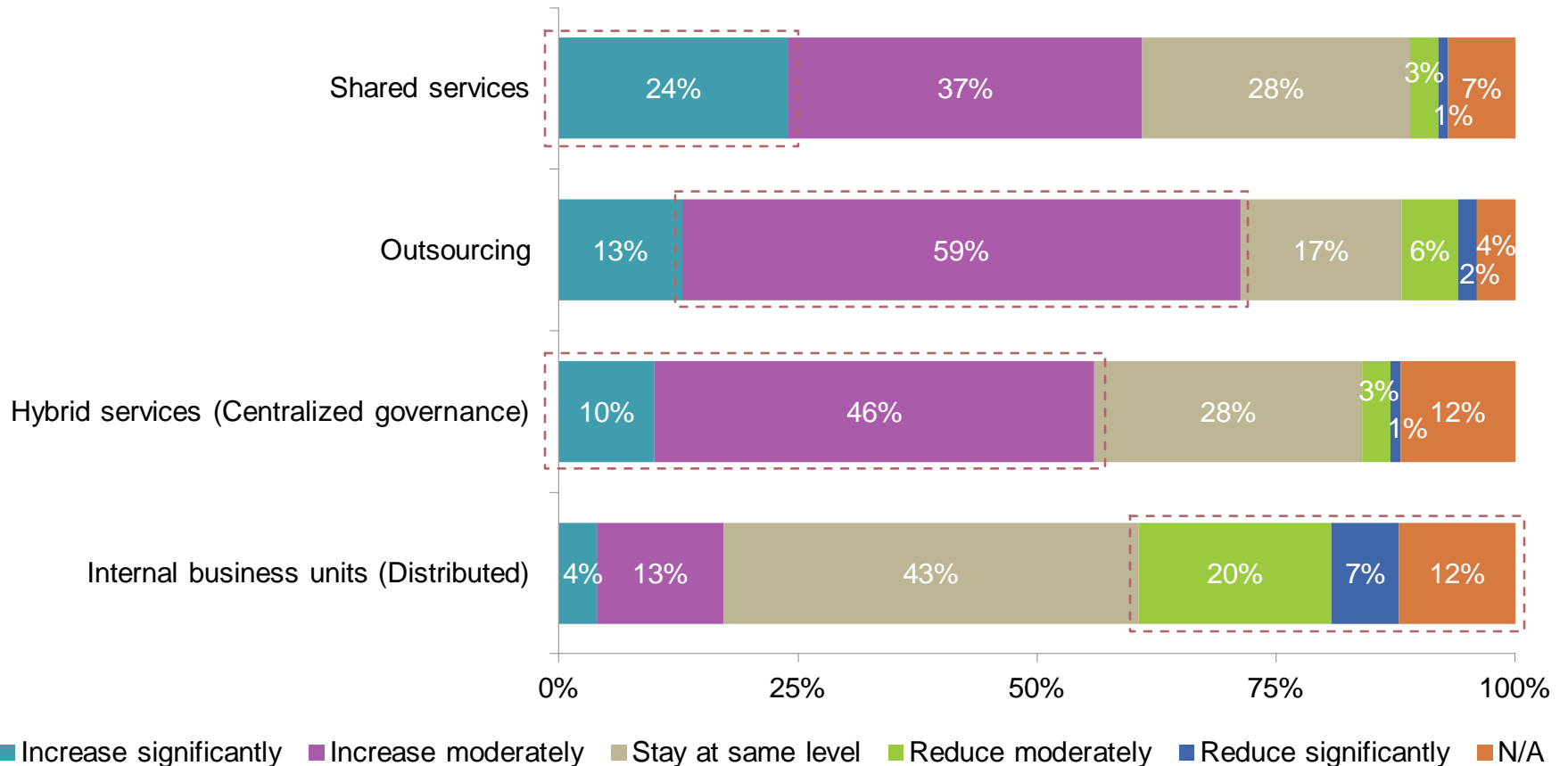
Executive findings (continued)

Buyers want advisory services that can help them govern their outsourcing engagements better—and also need data and research to help them approach outsourcing more effectively. Fifty two percent of advisors report that their clients have increased their thirst for research and benchmarks. Simply put, buyers want to be more empowered to understand the market, analyze their operations, and compare their performance with other firms. Hence, advisors need to have the ability to arm their clients with data and insight to help them. If they do not have any research, their clients will likely look elsewhere for help. In addition, 50 percent of advisors see their buyer clients wanting More help with governance and their provider relationships. This means providers need some advisors on staff who have lived the practitioner experience (with the battle scars to prove it).

There is an major communication problem in the outsourcing industry. “SMAC” does not mean anything to 70 percent of buyers, finance executives have been talking about “big data” for four decades and nothing is really new except the fact there is better technology to help them analyze it. In addition, nearly a one-third of buyers do not understand what “transformation” means to their business.

Future operating models: Outsourcing forms a critical lever for an integrated services model

Q. Over the next two years will your company increase/reduce its reliance on the following operating models for your general and administrative functions?

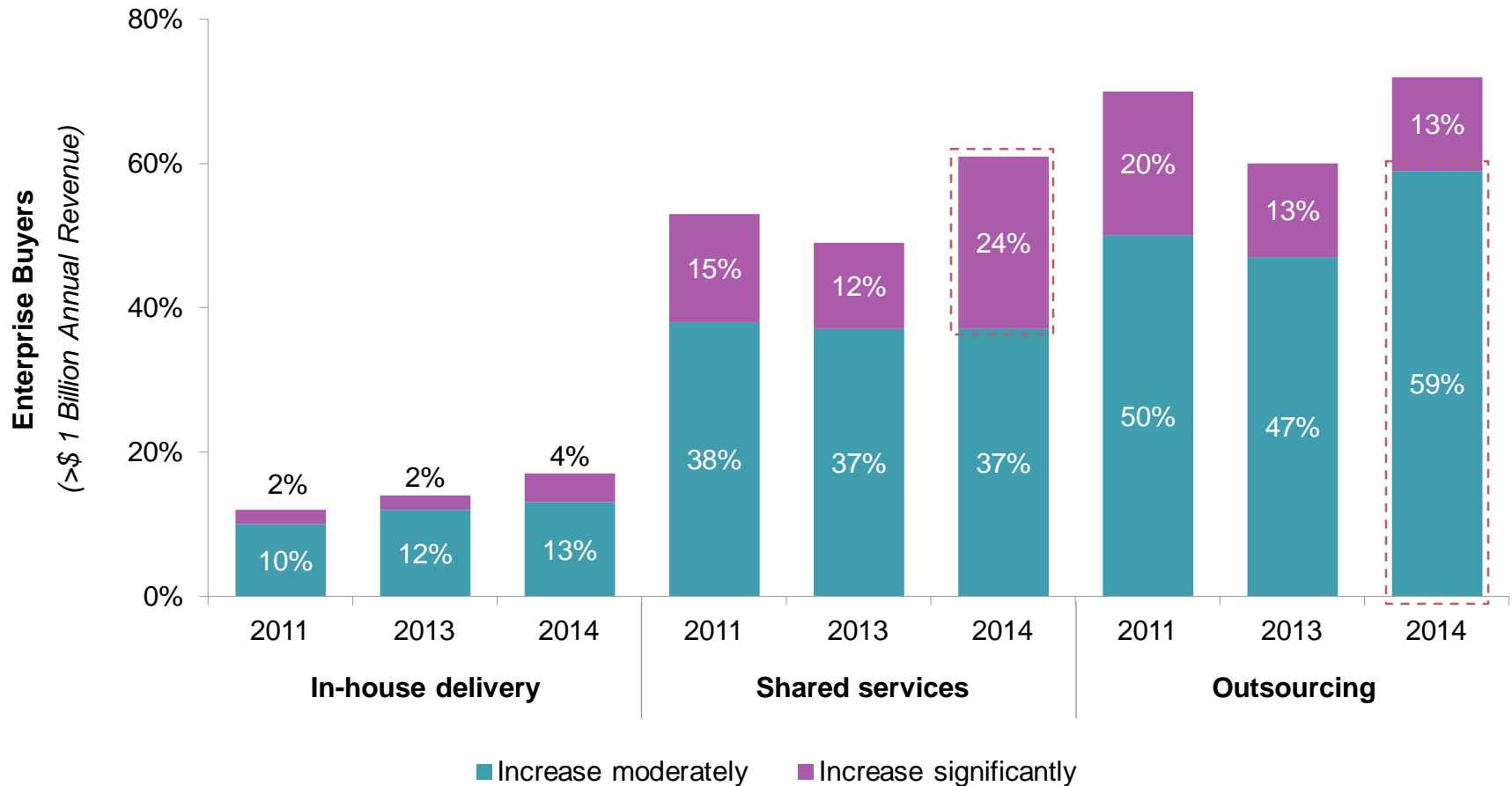


Source: 2014 State of Industry Study, May 2014, HfS Research in Conjunction with KPMG.
(Sample 312 Enterprises)

Key findings: Outsourcing is not dying—it's simply become a key part of a broader enterprise operations strategy

- **Both shared services and outsourcing are on the increase.** One in four enterprise buyers are reinvesting heavily in their global shared services operations, while seven out of ten are continuing to make (largely moderate) investments in their outsourcing delivery. This is driven by technology advancements and automation and the rampant globalization of enterprise supply chains and business ecosystems.
- **There is a clear move towards integrated global services models that incorporate both shared services and outsourcing.** The long and short of this is that 93 percent of enterprises today have shared services and 96 percent are outsourcing some element of their back office IT and business operations, while 27 percent are actually reducing their investments in their own internal business units. What's more, 56 percent are already increasing investments in their centralized hybrid governance function to manage their mix of service delivery models. To this end, the increasing majority of enterprise buyers today are investing in an *integrated global services model* that orchestrates their process delivery across all available vehicles of sourcing.

Globalization of operations in full swing as investment intentions in both shared services and outsourcing reach record high



Sources:
 2014 State of Outsourcing Study, n = 312 Buy-side Enterprises.
 2013 State of Outsourcing Study, n = 399 Buy-side Enterprises.
 2011 State of Outsourcing Study, n = 226 Buy-side Enterprises.

Key findings: The emphasis is on significant reinvestments in shared services for higher-value processes

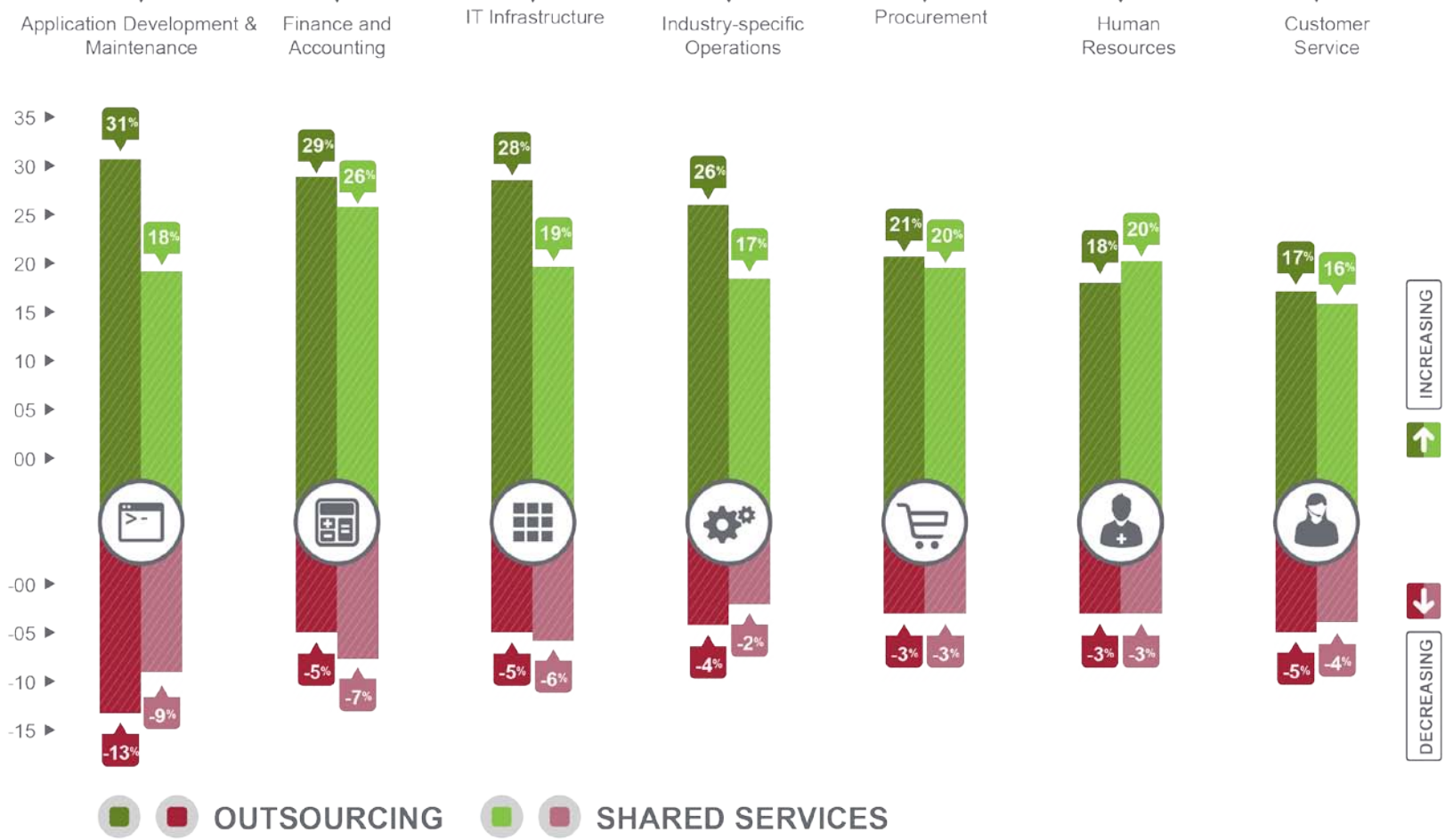
Shared services makes its strongest reemergence as a delivery model for a decade. While the broad number of firms increasing their focus on both the outsourcing and shared services models is relatively consistent over the past three years, the difference today is the *intensity* of investment. Outsourcing has slowed to a more moderate pace, while a number of large-scale enterprises are focusing on moving more work into their internal shared services centers—the first time in a decade we are really seeing shared services making a reemergence of this magnitude.

Buyers have historically been shifting more of their higher-value work into their offshore shared services operations, and continue to do so at an increasing pace. Buyers are aggressively globalizing their operational strategies and leveraging their offshore shared services centers, almost as much as their outsourcing providers' resources, as they seek to move more work from their internal business units into a centralized integrated services delivery model. As the following slide outlines, close to three out of ten enterprises are increasing the offshore component of their finance and accounting, over the next year, into both their shared services and outsourcing operations, while similar trends are occurring across IT, procurement, HR, industry-specific, and customer service functions. From our discussions with multiple buyers, the next wave of business processes they are moving into their offshore shared services often require a greater deal of context and specificity to their own businesses and, in most cases, compliance requirements.

Outsourcing is teetering at a crucial juncture between providing genuine value and low-cost staff augmentation. Providers need to prove they can do more than basic operations, otherwise outsourcing runs the risk of becoming a staff augmentation model for flexing operations as opposed to a strategic partnership between provider and buyer that can add more skill, technology, and analytical capability for clients.

Prolific use of offshoring continues

Q. How will your level of offshoring change in the next year?



Source: 2014 State of Industry Study, May 2014. HFS Research in Conjunction with KPMG (Sample 312 Enterprises)

Key findings: Offshoring is rampant across most enterprises today and showing no signs of an immediate slowdown

Offshore capability has moved in tandem with the globalization of the revenue for an enterprise. Part of the offshoring movement over the last twenty-plus years has been in support of the increasing globalization of enterprises in their pursuit of the next dollar, euro, peso, yen, or yuan. Shared services delivery capability has often been co-located with manufacturing, distribution, or sales facilities whether in Latin America, Asia, Central Europe, or Africa. As global revenue have risen and more complex operating models for tax management have emerged in the last several years, there is little incentive to pull back from offshored business process or IT delivery when the rest of the business is staying put.

Offshore resources have become an increasingly large component of business operations. Clearly, the offshore option offers immediate savings and firms are getting much more adept, confident, and experienced at managing their processes remotely—whether by an outsourcing provider or their own offshore shared service center. Most of the perceived “risk” of moving offshore has gone.

Key findings: Offshoring is rampant across most enterprises today and showing no signs of an immediate slowdown (continued)

Many enterprises are increasingly establishing a strong brand with offshore talent and investing in their own internal capabilities to run processes offshore. While, in the recent past, most enterprises relied more on service providers to provide the talent for their offshore capabilities, an increasing number of enterprises are now offering attractive career progression to offshore staff themselves and the investment is paying off. Moreover, most enterprises can hire offshore staff at wages rates cheaper than their own providers charge (i.e., not paying their margins), which is nothing new, but clearly many are more determined and confident to govern their own offshore internal resources themselves. What's more, many organizations are unsatisfied with the quality of their providers' resources and have made the decision to move to an integrated services model to deliver services to their organization. This is why we are seeing a heavy push from some major consultancies to enforce their own managed governance and GBS expertise with enterprises. We are even seeing providers with deep offshore specialization, eager to push their service models and capabilities to clients, often as separate engagements from their existing bread-and-butter outsourcing relationships.

Key findings: While enterprises with extensive offshoring are likely to stay the course, those with limited offshoring are likely to look at new value levers for efficiency gains, such as SaaS and automation

Over-investment in offshore delivery could impede future capability to innovate operations. The more that gets extended offshore, the more challenging it may become for enterprises to shift the model away from *linear* labor-based services that are so dominant today. Quite simply, offshore outsourcers with predictable FTE-based annuity contracts are in no hurry to disrupt their own sources of recurring revenue, while enterprise operations leaders may not have genuine incentives from their leaderships to substitute their own offshore labor for technology-driven alternatives.

Offshoring provides a very durable Band-Aid for many organizations and we're still yet to witness a slowdown in the amount of offshoring taking place—in fact, the data shows quite the opposite is happening. However, we do predict it will be more those organizations that have yet to do a lot of offshoring, which will likely look to move straight to automation and SaaS models to reduce high onshore costs. Eventually, competitive pressures will force all (surviving) leading providers to shift a much larger proportion of their labor-driven models onto technology-based platforms (where IBM has already placed its bets); however, the attractiveness of the high cost-savings benefits that locations such as India and the Philippines can provide is still on an upward trajectory and likely to remain this way for several years to come.

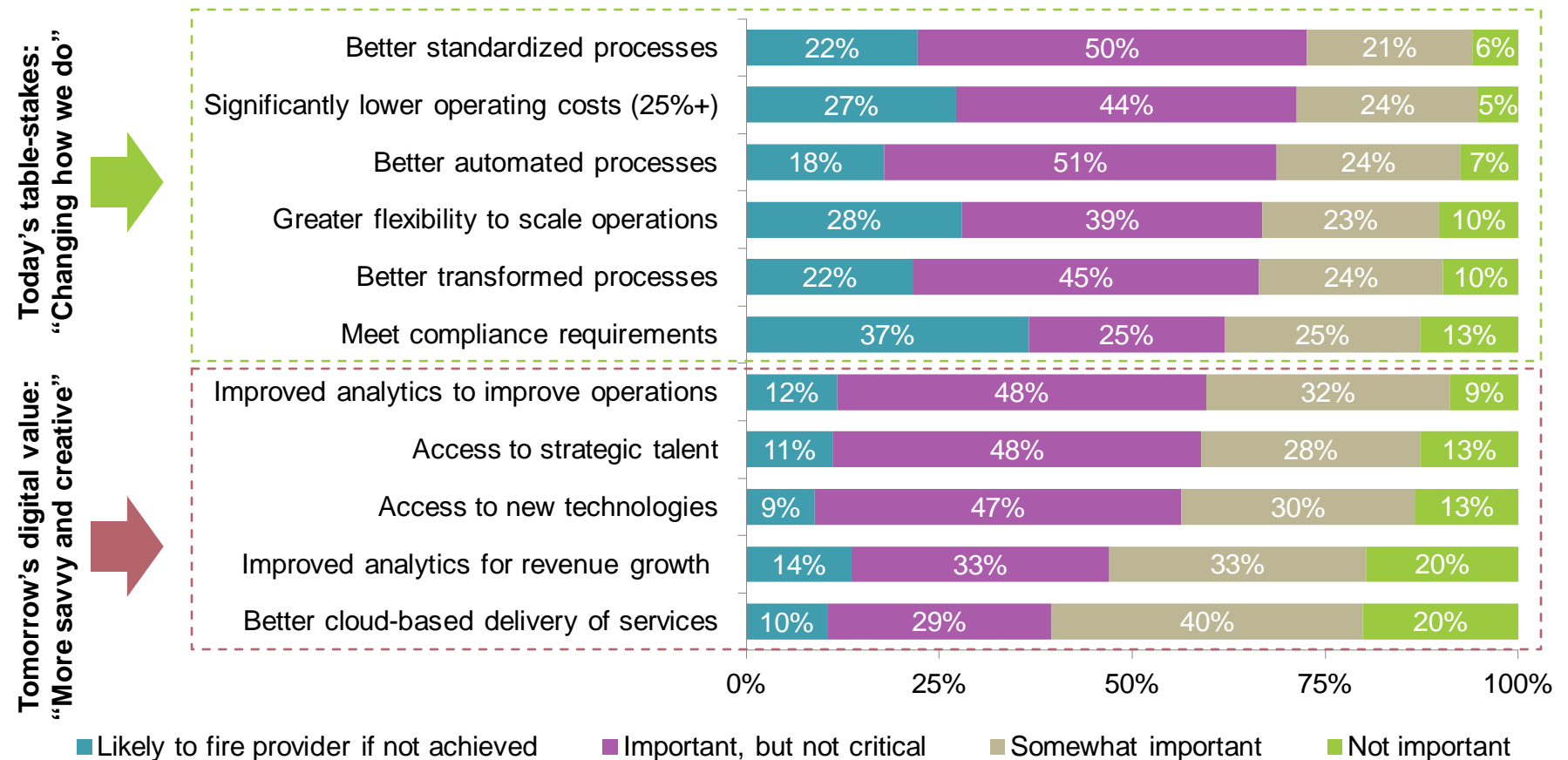
Key findings: Service providers need to evolve beyond labor arbitrage and basic operational delivery to survive long-term

The integrated services model is going to force ambitious providers to evolve their capabilities if they want to survive in the long-term. The traditional global services model has evolved largely by transactional work being moved initially into shared services centers and buyers eventually outsourcing that work to providers as it becomes easier to “shift,” once it has become centralized into a smaller number of locations. Now a similar cycle could well be happening with middle and front office processes. However, as global management of integrated processes matures, and buyers become increasingly adept at developing their own offshore management competencies, it is not guaranteed that the majority of buyers will continue to look at the traditional outsourcing model down the road (and several are already evaluating their future sourcing strategies).

There are multiple levers now available to clients seeking greater productivity and value. These include SaaS-based business platforms, high-value analytics tools and skills, better automation and robotization of their processes, and simply hiring their own offshore teams to do the work, as opposed to paying the (often higher) rates of the providers. Hence, those providers that are getting ahead of the disruption curve and supporting clients with more productivity tools and capabilities beyond simply offshore arbitrage and process standardization, are the likely winners down the road as clients integrate their global services delivery.

As digital services needs emerge, the provision of flex and process transformation are today's table-stakes

Q. How important are the following business benefits that you EXPECT to be achieved from your company's current IT outsourcing and BPO experiences over the next two years?



Source: HfS Research 2014

2014 State of Outsourcing Study, conducted with support from KPMG. (Sample 312 Enterprises)

Key findings: The new table-stakes require enterprises to fix their “analog present” to get to a “digital future”

The overwhelming mood from enterprises is one of frustration to get beyond this tactical status quo of legacy operations, in which so many find themselves stuck. Meanwhile, most service providers are not going to come to the table with the technology and talent until their customers clearly dictate and *demand* what they need to cross this chasm. And those providers that simply do not have the digital capabilities their clients demand to address these gaps, run the risk of being relegated to the class of legacy staff augmentation provider that performs only the low-value transactional work, or being removed from many client provider rosters altogether. And this is already happening with some ambitious and determined clients. What’s more, our research points to a significant decrease in renewal rates of outsourcing contracts (as many as 40 percent in some areas) where enterprises are moving more work into the cloud, simply pulling back in-house, or switching to alternative providers with more digital capabilities.

Clients are rapidly losing patience with services providers that aren’t working proactively with them to provide more value than the basic terms of the original contract. Many clients are actively looking to fire their provider if they cannot get past operational teething issues and actively begin the process of transforming the way they do things. In so many instances, clients are beginning to doubt their current provider actually has the skills or acumen that they were promised during the early courting days prior to contract signing. In today’s climate, close to a quarter of clients will actively seek to eject their current provider if they have not effectively helped them standardize, automate, and transform their processes within the next two years. This is no longer about achieving significant cost reduction targets and getting basic tactical operations functional—it is about moving clients into a future state that is much more effective than the current one.

Key findings: The new table-stakes require enterprises to fix their “analog present” to get to a “digital future” (continued)

The focus on digital outcomes has dramatically emerged, with many clients increasingly no longer viewing tactical success as their end-game. Whereas, in years gone by, the focus was slowly shifting from cost reduction to better global scale, the onus on clients is to move the conversation to one of better analytical capability, more savvy and creative support talent, and access to better tools and technology - these are the new stakes. While most providers will not get fired today for digital failure in the short-term, it is already very clear that an increasing majority of enterprise clients expect their providers to bring these skills to the table. Sixty percent already see operational analytics as very important as an outsourcing outcome, and a similar majority are already expecting their providers to pony up savvy talent and better tech within two years.

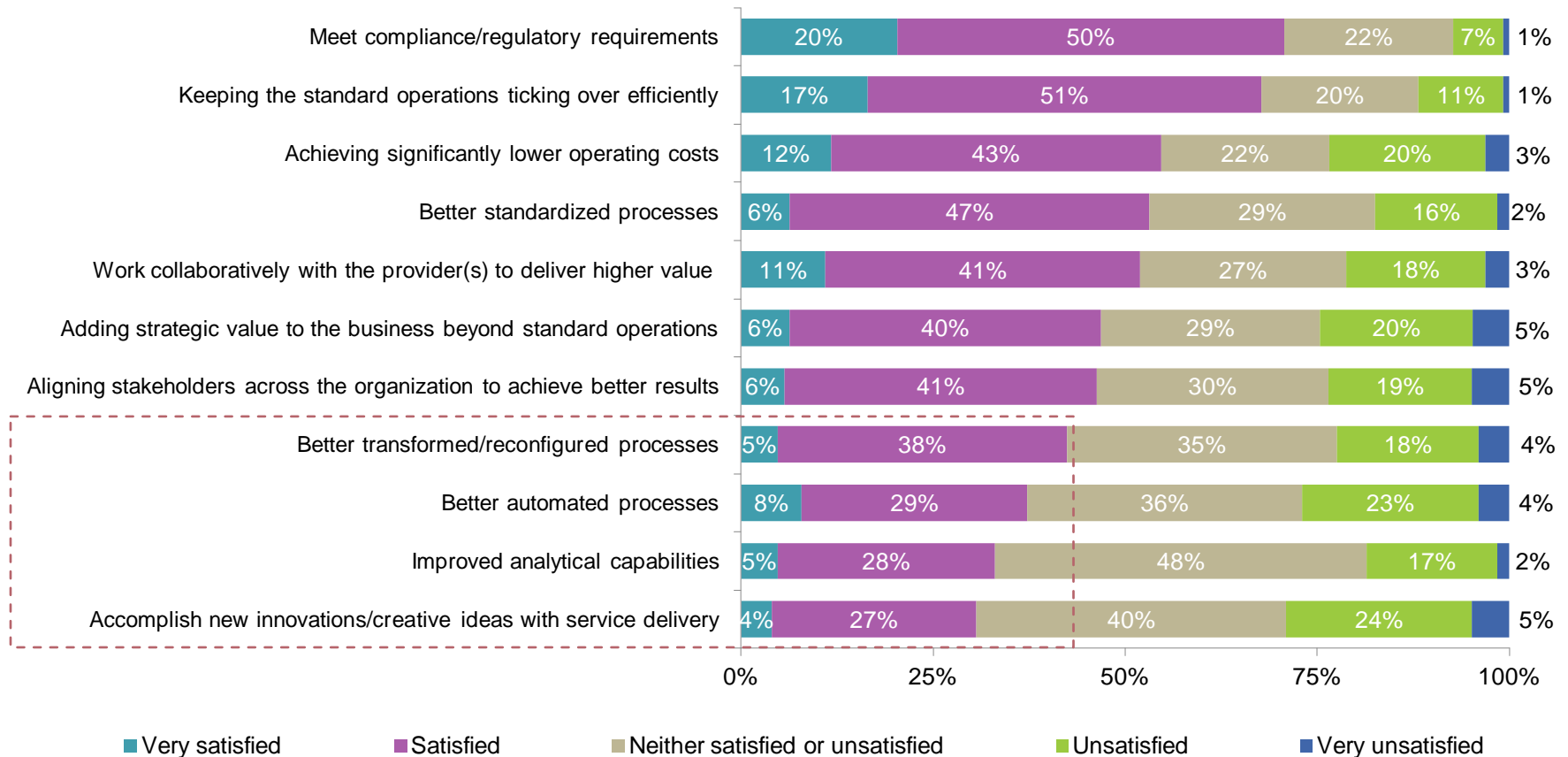
The table-stakes of 2014 are now a must-have for clients that have their eyes firmly planted on what they need to achieve in the medium and long term. They want providers who know how to engage with them to help them get to the next level. However, too many of today's providers have lost interest in their clients once they have reached an operational steady-state—and are laser-focused on winning that next deal, as opposed to fixing their existing ones.

Key findings: The new table-stakes require enterprises to fix their “analog present” to get to a “digital future” (continued)

Both clients and providers need to invest in the skills and tools they need. They must recognize that failure to do so will likely result in their ultimate failure to drag themselves out of this operational low-value cycle. In addition, intermediaries and advisors need to stop forcing these deals to get done in three-week RFPs so they can walk away with their fees paid with little care for what that client and its provider really achieve down the road.

Operations talent struggling with automation, analytics, and creative thinking

How satisfied are you with your internal talent's ability to achieve the following business outcomes with your current outsourcing engagement(s)?



Source: HfS Research State of Outsourcing Study 2014 conducted in conjunction with KPMG.
Sample = 312 Enterprise Buyers

Key findings: Two-thirds of enterprise talent is falling short in “digital” areas

There is widespread dissatisfaction from enterprises with their own internal operations talent. The internal skills to change processes, automate them, analyze them, or come up with creative thinking on how to improve operations is widely cited. The talent dearth is so bad that barely a one-third of buyers have seen any positive impact on their own talent with their current outsourcing relationships.

Organizations clearly cannot reach their desired outcomes without professional help. “Digital” capabilities, in this context, relate to the acumen of operational services talent to understand the interplay between their applications and processes to achieve better automation and more productive workflows that can ultimately lead to better analytics to base future business decisions. In addition, these capabilities also relate to the creative flair of staff to align their services with the core business and come up with new ways of doing things to drive value, new ideas for business improvement and, in short, to behave more like a “front office” employee than transactional operator.

Key findings: Two-thirds of enterprise talent is falling short in “digital” areas (continued)

A major talent crunch is coming. This will impact the vast majority of ambitious organizations struggling to find or retrain operations staff to be more “front office” and “digitally savvy” with their approach to services. Two-thirds of outsourcing clients are happy with how their internal teams manage costs, keep the basics ticking over, and respond to compliance needs. But, as these “light on” capabilities become increasingly commoditized through more sophisticated global delivery and standardized technology platforms, the need for the current number of operational staff is steadily decreasing.

The ability to harness digital technologies is becoming a core attribute staff need to develop. What is clear is that technology has become a major component for future value of the enterprise, and one avenue for operations staff to increase their future value is to train in areas such analytics and process automation where they can add whole new echelons of value to their organizations.

Key findings: Two-thirds of enterprise talent is falling short in “digital” areas (continued)

Sadly, many of the two-thirds we identify above are not going to make it, and others are simply not going to be needed. The relentless pursuit of increased value and decreased labor costs will see to that. *Less is more* is the brutal rule for the future of the enterprise operations function.

The need for progressive skills and capabilities is creating opportunities for smart consultants and providers. Ambitious clients are becoming rich hunting grounds for valuable partnerships in the future, as the need for the digital skills and new talent steadily proliferates. Many clients will find their need to develop or acquire better talent a fruitless exercise and will look to their external partners to plug these operational gaps that will drive future value. This shift of skills is the new sourcing services, with transactional processors being replaced by data scientists, in addition to a similar shift in application developers as well as mainframe staff.

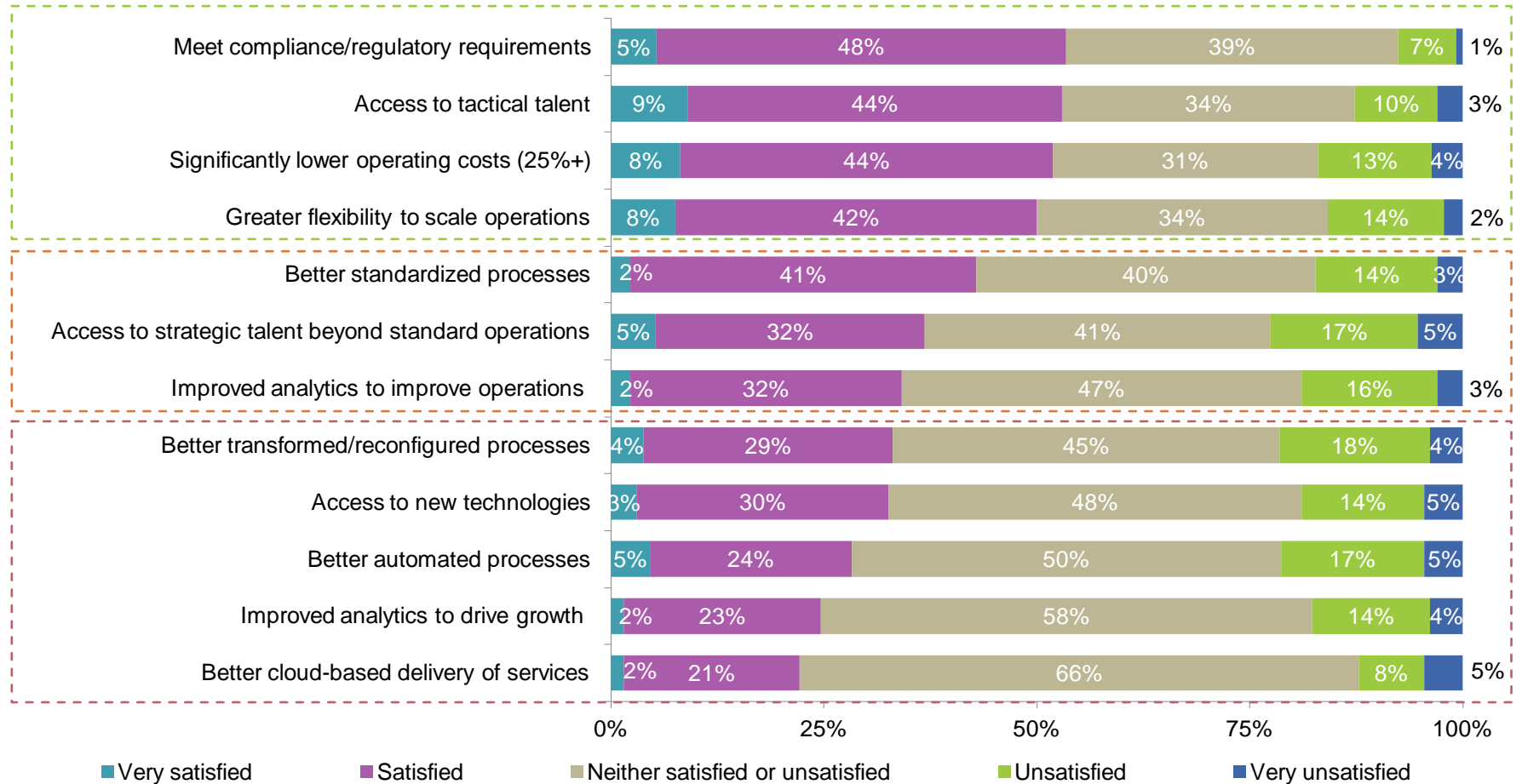
Key findings: Two-thirds of enterprise talent is falling short in “digital” areas (continued)

Why the new wave of digital capabilities is challenging the workforce like never before. Organizations have been trying to reduce their labor costs for decades, but something feels very different about the new digital reality in which we operate. Many people thought the onset of Web technologies would be the big game changer with how we utilized labor, but it actually increased our reliance of humans—many business processes became Web-enabled, which necessitated training on new applications and helped us work more effectively, but they didn’t fundamentally change how we operated. The Web really just enabled us to run things the same way as previously, just with more global capabilities and much more efficient communication. It was this previous wave of digital that really enabled the great outsourcing boom of the last 15 years, as communication costs plummeted and Web applications made it possible to work with people anywhere/anytime. The initial Web evolution helped globalize the workforce, but didn’t have as much impact on how we could automate processes, mine vast pools of data, and leverage mobile applications to interact with our employees, partners, and customers.

We have entered an era today where there is real capability to change how we run our businesses. From the back office processing to the front office customer interaction: we have tools and apps to target and interpret meaningful data, we have developing software solutions to automate and even robotize processes like we never could in the past, and we have all submerged ourselves in a mobile culture where all forms of business are conducted on all types of devices and interfaces. Perhaps even more importantly, cloud-based platforms are being developed that allow us to share these capabilities, reinvent the way we run services, and process transactions that require a lesser amount of human intervention and oversight.

Higher expectations driving poorer client satisfaction

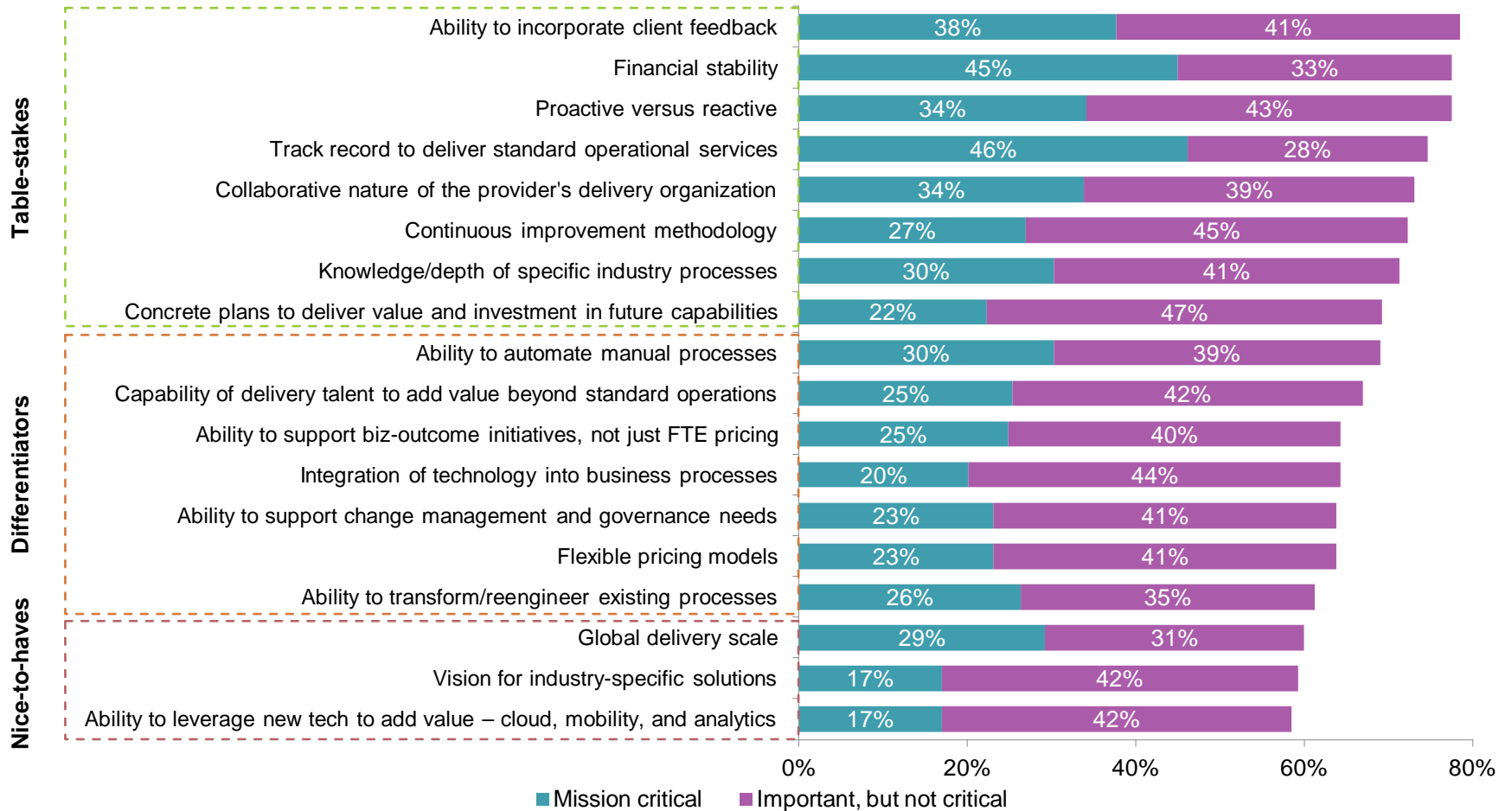
Q. How satisfied are you with your primary service providers' performance to meet each outcome?



Source: 2014 State of Industry Study, May 2014. HfS Research in Conjunction with KPMG. (Sample 312 Enterprises)

Providers being held to a much higher standard

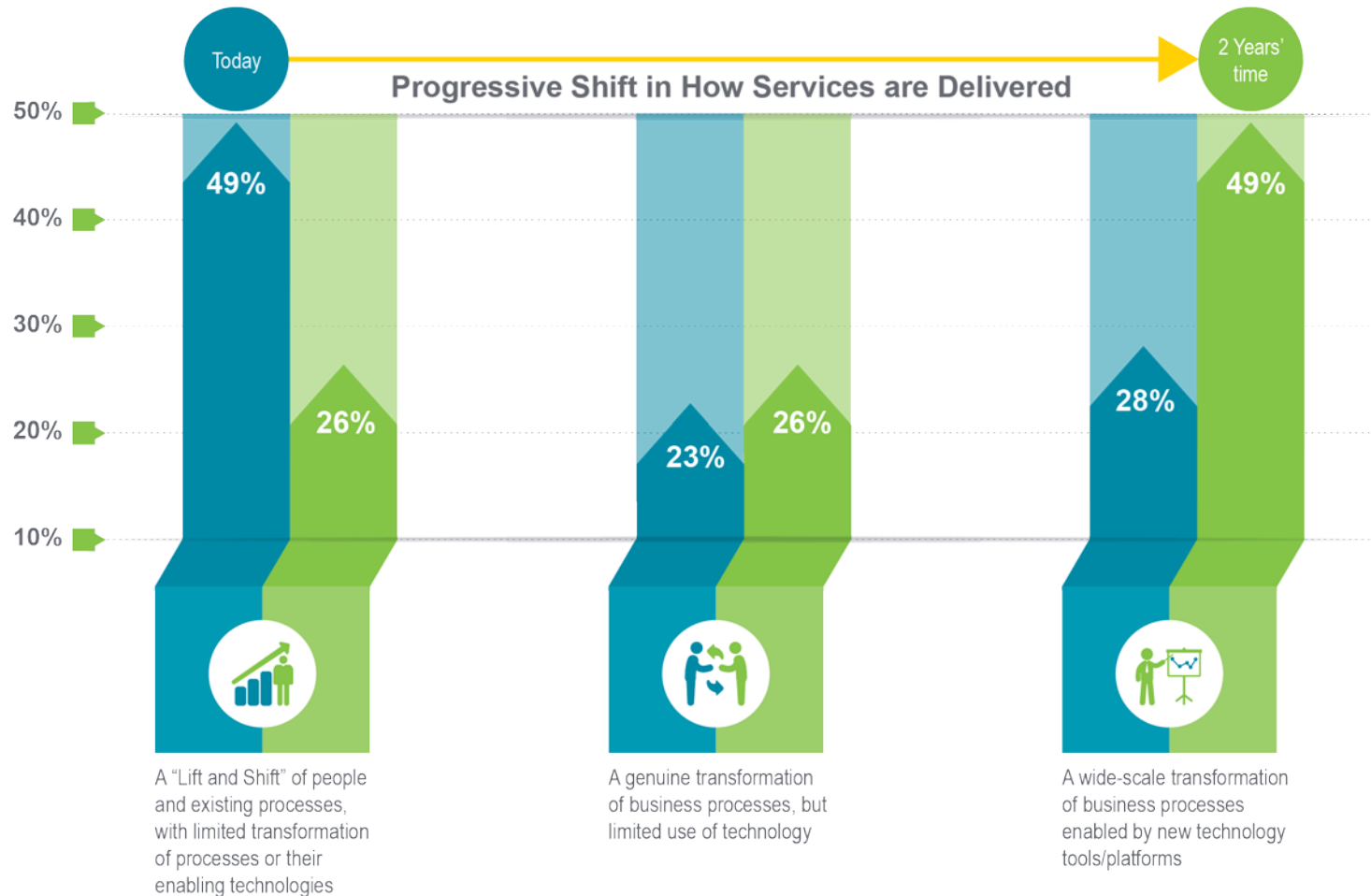
How important are the following service provider attributes to your organization today?



Source: 2014 State of Industry Study, May 2014. HfS Research in Conjunction with KPMG. (Sample 312 Enterprises)

Operations leaders expect to make the leap to technology-enabled operations – and fast!

State of BPO Engagements today and expectations for 2 years time



Source: HFS Research, 2014. Sample = 189 Major Enterprises

Key findings: Half the industry expects to break out of the old world of “lift and shift” ...and fast!

Forty nine percent of today’s enterprise buyers expect to move to a “wide-scale transformation of business processes enabled by new technology tools/platforms” in just two years. This may be a pipe-dream for some enterprises, but what is clear is that many of those operations leaders failing to steer their enterprises away from legacy delivery models will get cast aside quickly in today’s tolerance-diminishing business environment. The speed of technology changes (and lower investments required) is allowing for this change to happen much quicker than it has in the past, where multi-year ERP implementations held many enterprises back from achieving its original business goals.

Operations leaders don’t have the luxury of ten year improvement programs anymore—corporate leadership expects to see tangible results in much shorter time frames. Most are under a renewed pressure to continue driving out costs, while delivering ongoing improvements to data quality and having greater alignment with front-office activities. The old “we need to fix our ERP first” excuse just isn’t cutting it these days.

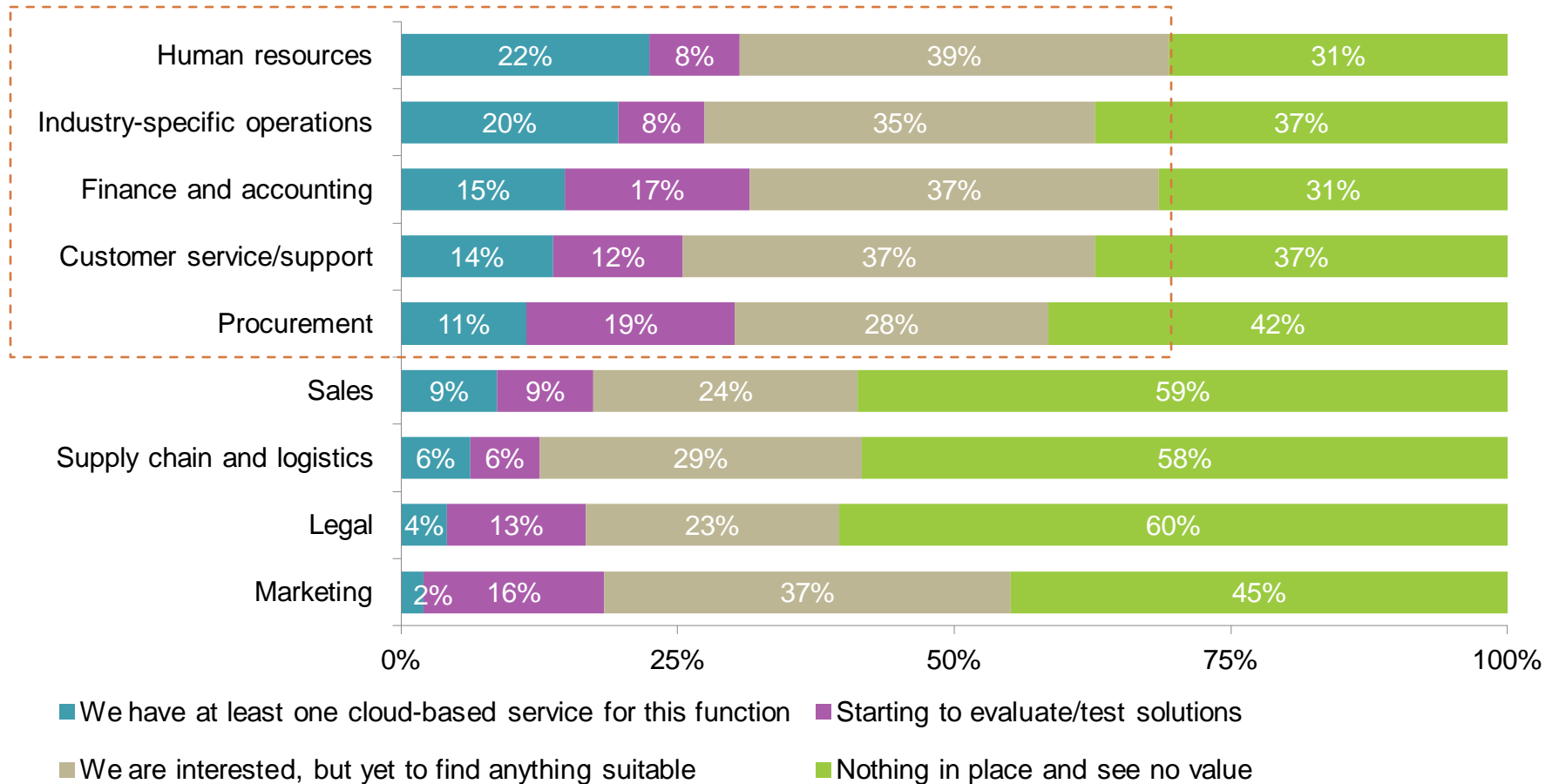
Key findings: Half the industry expects to break out of the old world of “lift and shift” ... and fast! (continued)

Providers can only deliver what their clients demand of them—and pay for. Simply put, 49 percent of enterprise buyers have only ventured as far as doing basic labor arbitrage, and are clearly failing to find much (if any) value beyond those wage savings. Most providers are not delivering that value, but in most circumstances, this is because their customers have failed to put forward a value-based agenda and work with their provider to have them help achieve it. Providers will not seek to deliver value until their clients demand it, and are prepared to invest in it, and will disengage with them if they then fail to deliver it.

BPO is the start of a new phase of change for many enterprises...it's persisting with the change agenda that dictates the pace of new value creation. These 49 percent of “lift and shift” engagements have been set up for short-term cost gains, not long-term improvements and innovations. However, all is not lost, because moving into a “lift and shift” BPO environment isn't necessarily leaving the buyer and provider in a bad situation. They have achieved goal number one with most outsourcing: they got the bloated costs off the books and are in a better place to effect change.

BPaaS is already replacing legacy outsourcing

Q. In what areas are you considering cloud/as-a-service options to augment/replace traditional outsourcing?



Source: HfS Research State of Industry Study June 2014, conducted in conjunction with KPMG.
 (Sample 312 Enterprises)

Key findings: Half the industry expects to break out of the old world of “lift and shift” ...and fast!

Ambitious and sophisticated clients are now seeing the huge benefits of shifting from on-premise to “as-a-Service” delivery. This isn't something that is occurring in a few years, it's already happening where our latest research shows close to one in three enterprises already using (or about to use) BPaaS/cloud as an alternative to legacy outsourcing in areas such as HR, industry-specific operations, finance and accounting, and procurement.

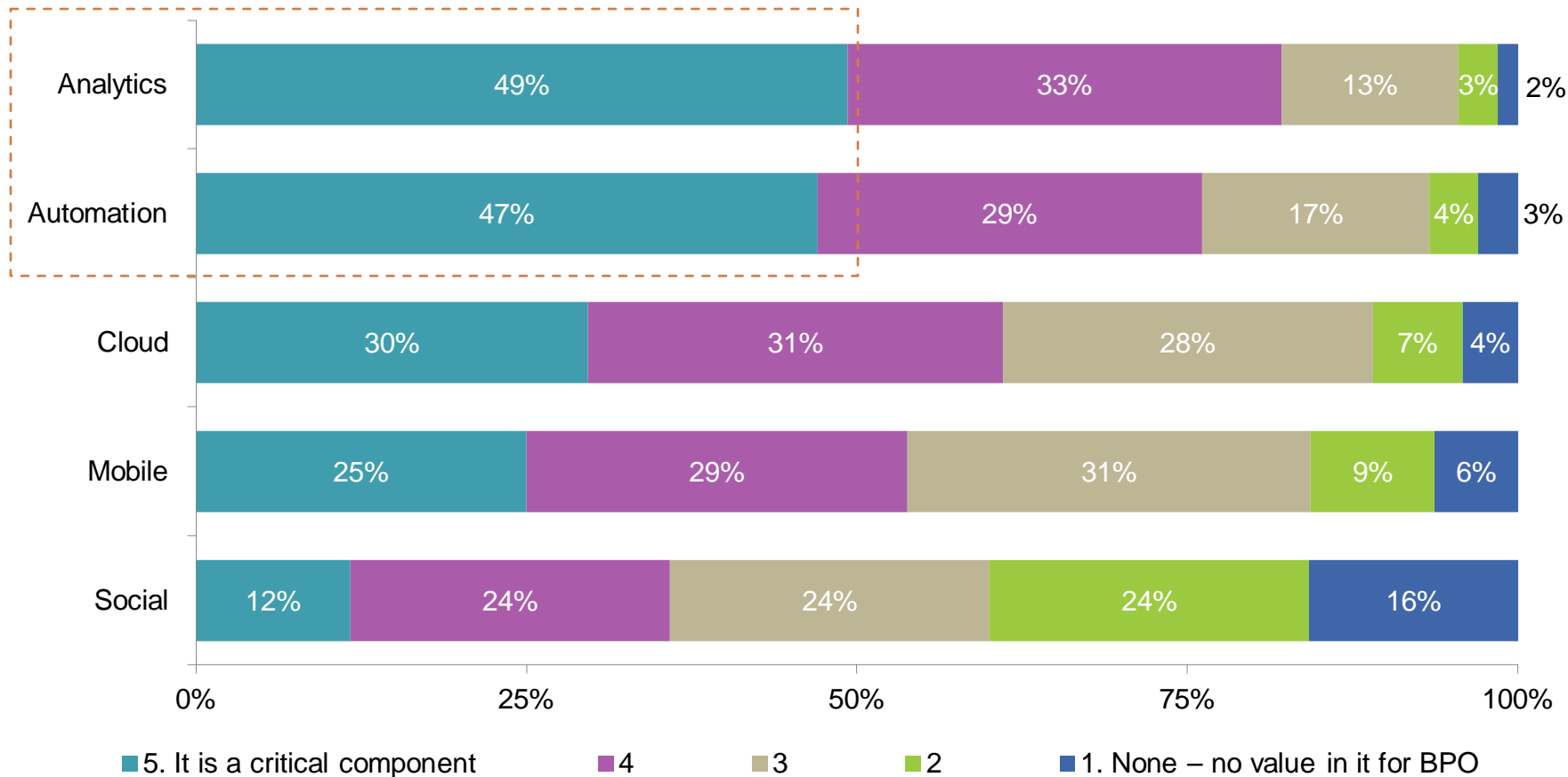
Having a provider that understands and can implement a cloud platform, support the transformation, and provide the necessary services that add real value to the front-office is the Holy Grail for many buyers. Many enterprises have already taken the leap to Workday, but some failed to invest in the right services expertise, not only to implement the product, but to go through the requisite change management and organizational redesign needed to get the maximum benefit from the cloud solution. It's already clear from the Workday example alone that outsourcing and cloud need to be delivered as one potentially seamlessly-accessible service, where outsourcing “is” technology. Most enterprises adopting cloud products and expecting simply to “figure out” how to enable the operations around them are going to go through a lot more pain and long-term frustration that they ever anticipated.

Key findings: Half the industry expects to break out of the old world of “lift and shift” ... and fast! (continued)

The successful providers will be those that can bridge the divide between cloud/infrastructure and process delivery. When you talk to buyers today, most will tell you that having to deal with the technology and operations/BPO divisions of providers is akin to dealing with two separate companies. There is often very little synergy—and very different working cultures—between those people that deliver business processes and those who design, develop, and maintain technology solutions. When providers section off process delivery and operations from technology, it nearly always makes it challenging to get the right access to funds, align all the stakeholders that matter, and make meaningful, credible business cases. Having operations and infrastructure in the same unit creates more opportunity for transformational thinking at the solution-architect level in operations, by increasing awareness of—and exposure to—emerging technologies.

Analytics and automation have become crucial technologies for improving outsourcing outcomes

Q. What role can each of the following emerging technologies play in improving the outcomes of your current and future outsourcing engagement(s)?



Source: HfS Research 2014. Note: n=189 Enterprise BPO Clients.

Key findings: There exists a broad mandate for buyers to unleash the potential of several different flavors of technology to add value to their current outsourcing experiences

Half of the buyers stated that analytics is a critical component to making the move to value beyond cost.

This is not a surprise, given the focus on analytics technologies and capabilities from service providers over the last few years. However, it is also clear that buyers need to give their providers access to their intimate data, if they really want value from their expertise. Traditional cost-based, labor arbitrage deals generally would not—and should not—be expected to deliver on anything more than the occasional descriptive insight, as service providers would not have the necessary capabilities in place to provide broader insights; and buyers likely have not given their providers access to the necessary data to create a deeper level of collaboration to bring these insights forward.

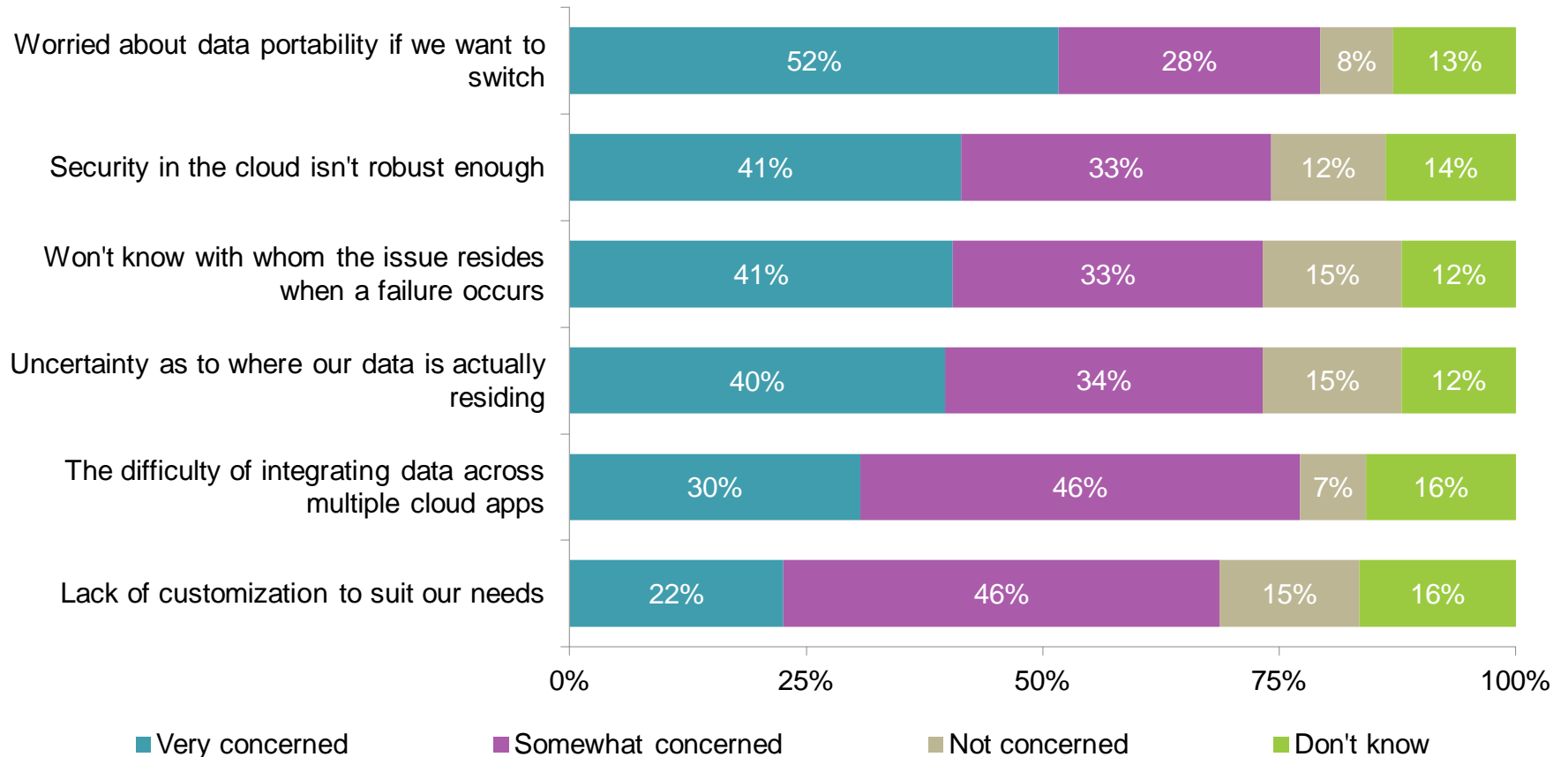
Process automation has rapidly emerged as a key technology to improve processes. What was surprising was the nearly comparable level of support from buyers (47 percent) for automation which, until recently, had barely been in the conversation between buyers, service providers and advisors with the same frequency as analytics. Process automation is first and foremost a cost play, as it seeks to replace certain roles in engagements without transforming and modernizing the underlying legacy applications or systems of record from what they are today. Process automation is also a key technology in bringing value beyond cost for existing “lift and shift” engagements because it can reduce errors and enhance compliance, improve job satisfaction for retained staff, provide process analytical insight, deliver true 24 x 7 potential, and provide an opportunity to reshape engagements around business outcomes.

Key findings: There exists a broad mandate for buyers to unleash the potential of several different flavors of technology to add value to their current outsourcing experiences (continued)

Mobility, social, and cloud are increasing in importance to buyers. Buyers suggested for cloud, mobile, and social, they saw their importance rapidly increasing, despite the relatively limited value currently being obtained from them.

And cloud concerns largely sophomoric

Reasons for avoiding BPaaS

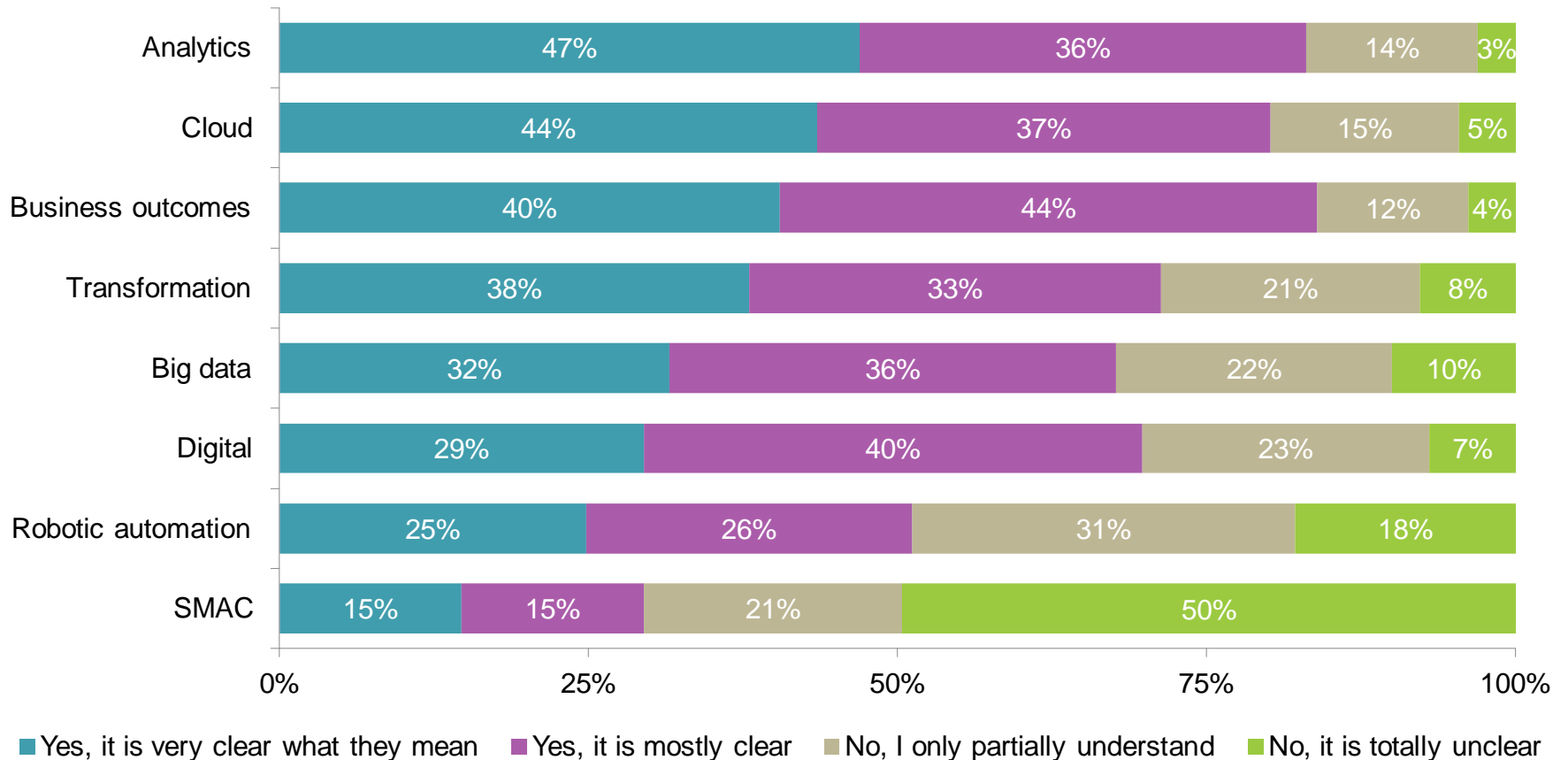


n =740 IT Managers in Enterprises

Source: HfS Research 2014.

Too much ambiguity surrounds many buzz terms

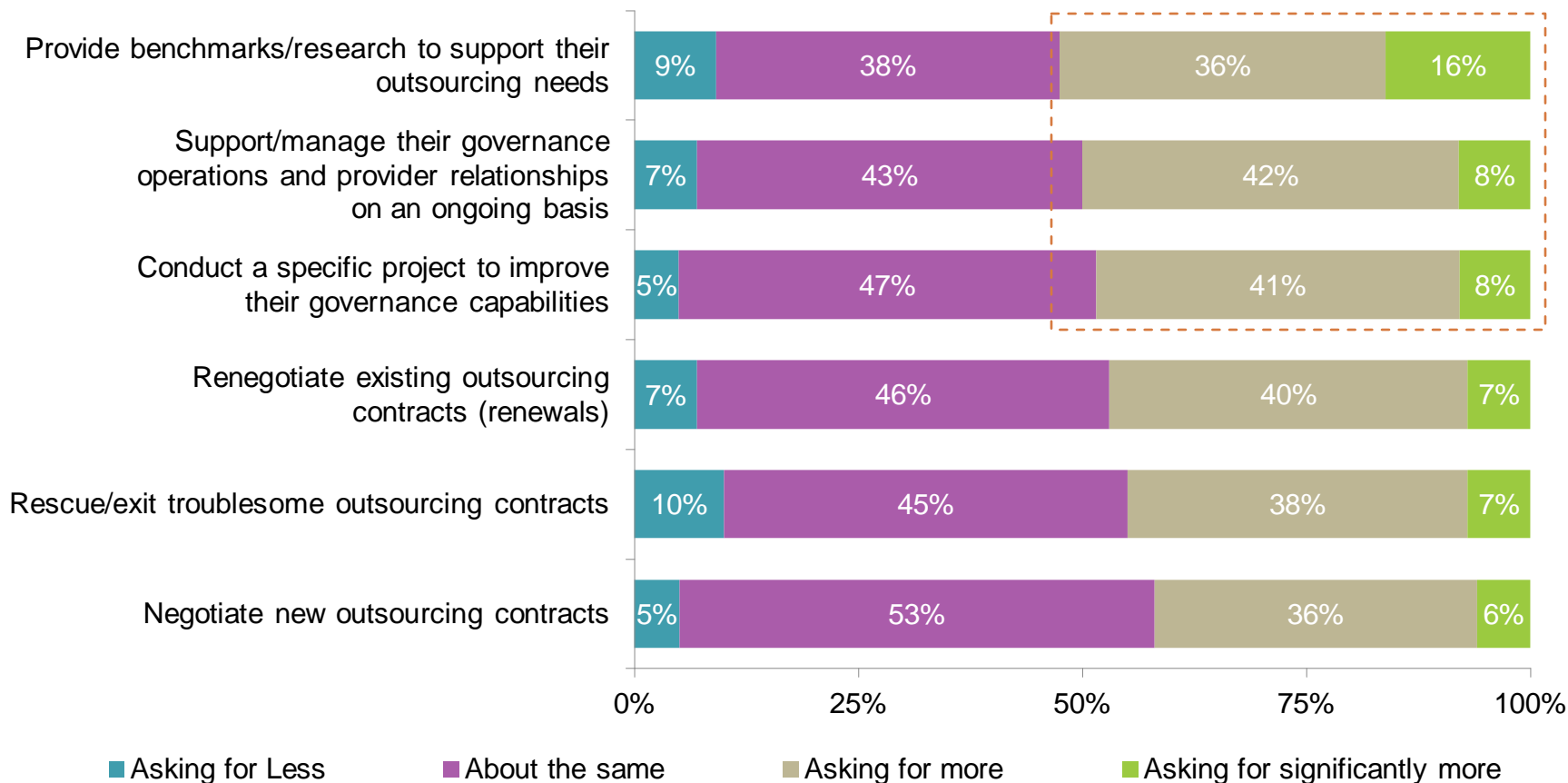
Q. When service providers/consultants use the phrases below, is it clear to you what they mean and what value they represent?



Source: HfS Research in Conjunction with KPMG. Note n=312.

Outsourcing advisors must be governance specialists armed with research if they want to survive

Q. Over the last 12 months, have your clients been asking for more or less of the following outsourcing advisory services from your firm?



Source: 2014 State of Outsourcing Study conducted by HfS Research in Conjunction with KPMG.
Sample: 161 Advisors

Key findings: Buyers want advisory services that can help them govern their outsourcing engagements better—and also need data and research to help them approach outsourcing more effectively

Advisors need to do research. Fifty two percent of advisors report that their clients have increased (many significantly) their thirst for research and benchmarks. Simply put, buyers want to be more empowered to understand the market, analyze their operations, and compare their performance with other firms. Hence, advisors need to have the ability to arm their clients with data and insight to help them. If they do not have any research, their clients will likely look elsewhere for help.

Advisors need to understand how to support governance processes. Fifty percent of advisors see their buyer clients wanting more help with governance and their provider relationships. This means providers need some advisors on staff who have lived the practitioner experience (with the battle scars to prove it)—they can't just reel out deal guys who used to broker contracts for service providers to craft governance strategies. There is no written rule book for governance—it's something that clients need to learn through good advice and real-world experience.

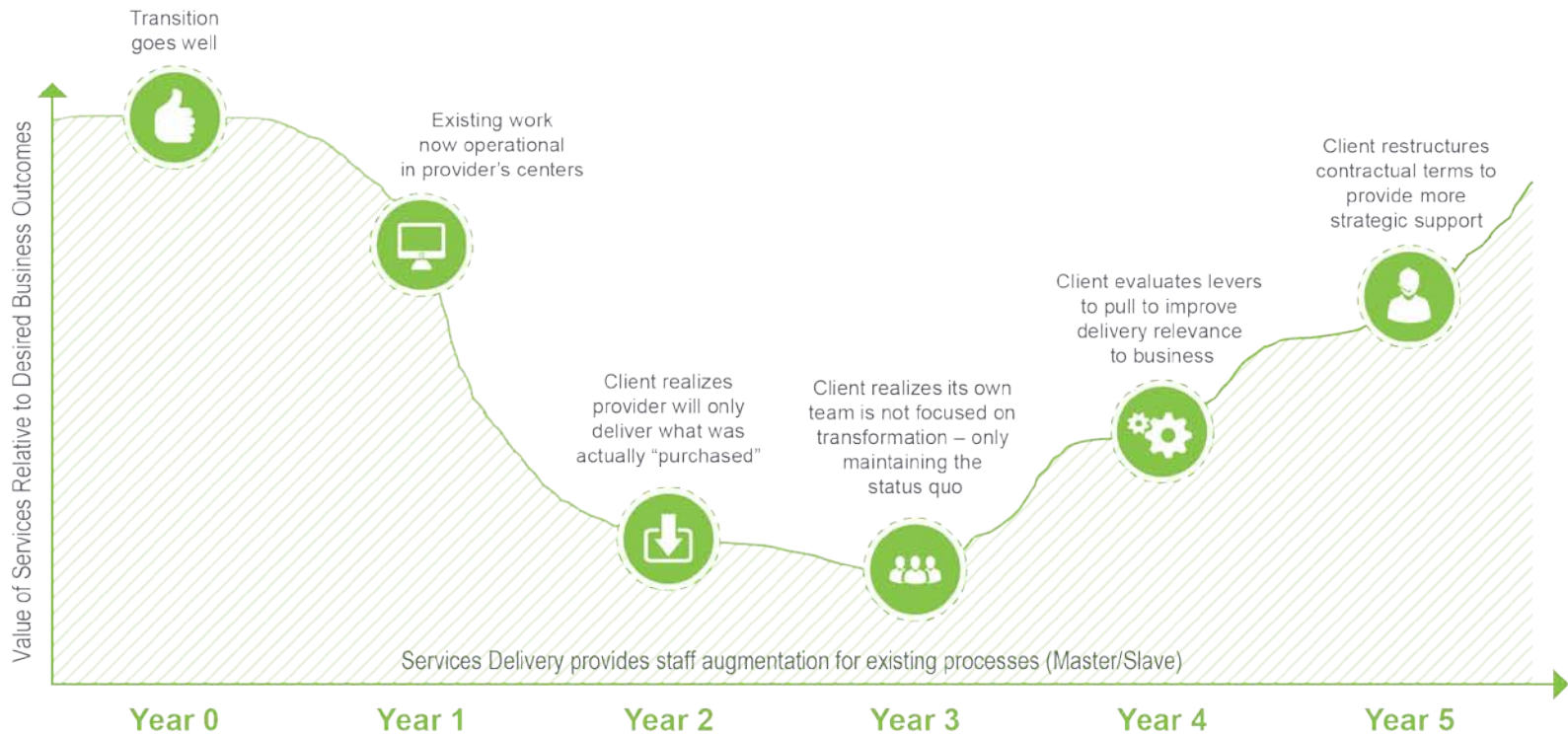
Key findings: Buyers want advisory services that can help them govern their outsourcing engagements better—and also need data and research to help them approach outsourcing more effectively (continued)

Advisors still need to be good at negotiating deals. Buyer needs for deal help are definitely not decreasing—and close to half are wanting even more help. This means the deal guys can still get paid, but clearly need to up their game if they want to keep winning business with clients. Clients want to hire advisors that can be great at deals, but also great beyond the deal.

Additional third parties in a client's ecosystem will drive additional complexities, which will amplify the need for the expertise. Managed outcomes (end-to-end) vs. traditional performance management will become more and more important as we blur the lines between further between third parties, internal operations, and end users.

The “all too typical” outsourcing scenario

Strong Alignment between Business Objectives and Services Outcomes (Collaborative)



Source: Hfs Sourcing Executive Council Members, 2014

Key findings: If outsourcing is to survive long term as an industry, then buyers, advisors, and providers should consider the following measures

Less focus on the deal, more on the relationship. Providers are all-too-frequently being forced in the position of saying what they need to win the deal, as opposed to having a structure to propose a realistic partnership that works for both sides, with specific milestones and balanced delivery expectations.

Advisors need to create a more collaborative RFP process that allows for more interaction between the buyer and interested providers. Advisors also need to set better expectations for their clients and potentially get their governance consultants involved earlier in the down-selection process.

Key findings: If outsourcing is to survive long term as an industry, buyers, then advisors, and providers should consider the following measures (continued)

Ambitious buyers must push aggressively towards a managed outcomes governance model. The challenge is that business outcomes truly cross multiple functions and groups (internal and external). Similar to 10–15 years ago, when clients really didn't invest in outsourcing governance, we will see a need to invest in the ability to govern performance across functions, providers, and internal operations on business *outcomes* —not the traditional metrics.

Providers need to develop a plan on how to develop their existing clients. Providers need to view their clients as future growth opportunities, as opposed to chasing that next deal simply because there is more immediate money on the table, which means more consultative account managers and less out-and-out salespeople. Simply running client engagements as cheaply as possible with limited investment is a sure route to failure in today's industry.

Key findings: If outsourcing is to survive long term as an industry, buyers, then advisors, and providers should consider the following measures (continued)

Buyers need real proof-points on provider culture, performance, and capability. Buyers need access to pragmatic experts that talk to a multitude of peers in other organizations in order to get a stronger view of the post-transaction performance of providers. Simply relying on rose-tinted references will rarely give an accurate expectation of what they are likely to experience further down the road with a provider. Buyers need to do their own research and use the expertise of advisors and analysts to validate their strategies. They must talk to other buyers, go to conferences, and seek them out on social media groups.

Early exit provisions should be implemented as an insurance from “value disappointment.” There needs to be smarter forethought in the whole process where the buyer and provider prepare in advance for failure to meet expectations. If providers are being shoe-horned into responding to a price-squeezing, innovation-sapping relationship, there should be an early exit provision for both sides (for example after 36 months). If the relationship isn't working, it probably makes sense for both sides to exit quickly, cost-effectively, and painlessly.

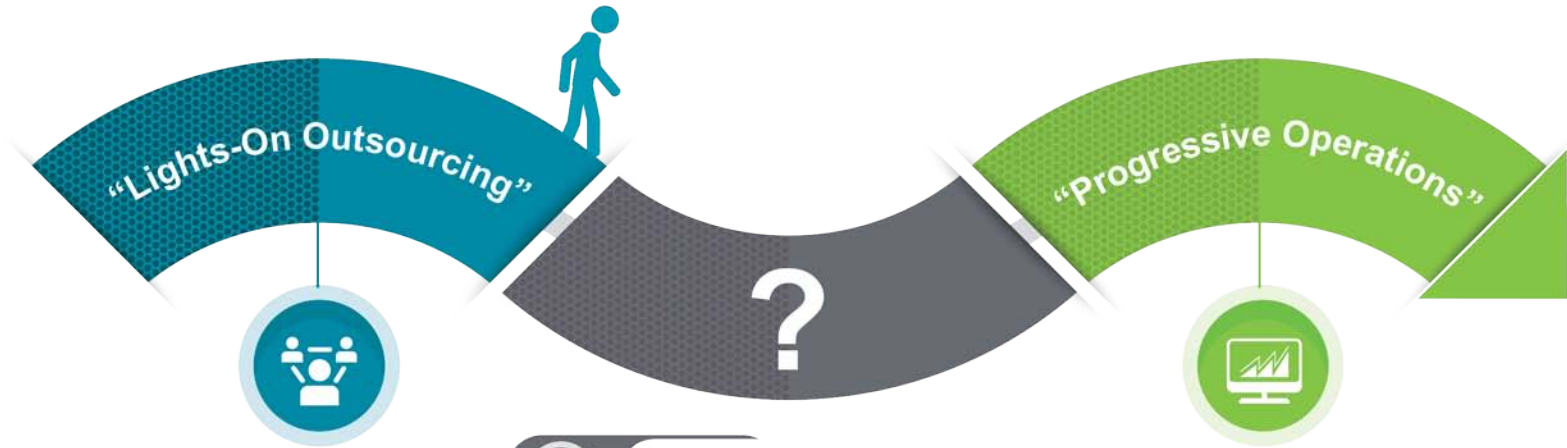
Key findings: If outsourcing is to survive long term as an industry, buyers, then advisors, and providers should consider the following measures (continued)

Enterprise buyers need to recognize the profession of services governance. Most corporate staff have little knowledge or understanding of what services and sourcing governance people do and why they matter (or even exist). In fact, we estimate that 90 percent of employees are ignorant of the role and value a services governance function provides—or should provide. Until services and sourcing governance is recognized as a crucial professional discipline, it will continue to struggle to improve flawed relationships and educate corporate citizen of its value to the organization.

Appoint a chief services officer (CSO). Many CPOs are proving ill-equipped to manage services governance, so surely it is time for smart organizations to create the CSO function, with a direct reporting line to the top of the company. It is to convince top talent to work for buyer-governance teams when they are submerged many layers down the organization from any decision-making authority. With the concerted move to increase investments in offshoring, shared services, and outsourcing, not having an empowered senior corporate officer responsible for transforming operations is an impediment for so many of today's organizations.

Wrap-up: So how do we cross this chasm?

Wrap-up: So how do we cross this chasm?



- Command of the Hybrid Model
- Managed Outcomes Governance Model
- New Models for Governance
- Next Generation Solution Architects
- Process Automation Tools
- Configurable Process Methodologies
- Analytics Talent and Tools
- Presentation Layers for Insights
- Flexible Delivery Center Layouts

Appendix: Survey demographics

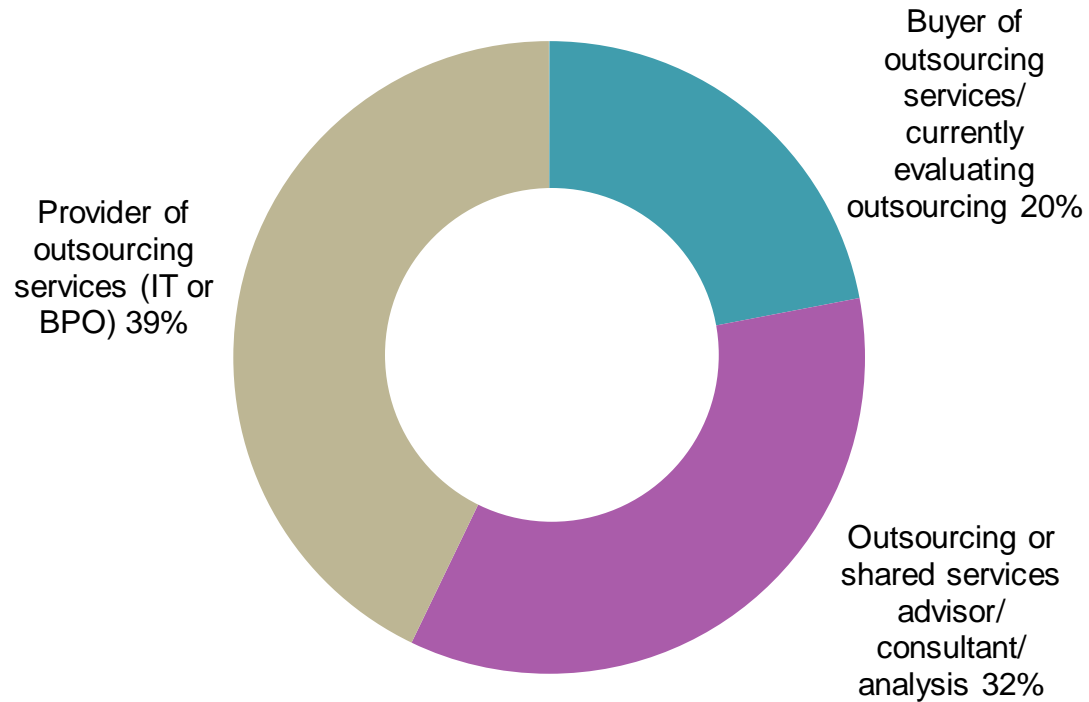


About the survey – Results

- This survey was fielded between May and June 2014
- Total number of respondents to the survey were 1,079, which breaks down to 312 people from buy-side organizations, 347 representing outsourcing/shared services advisors and consultants, and 420 representing providers of business and technology outsourcing

Survey details

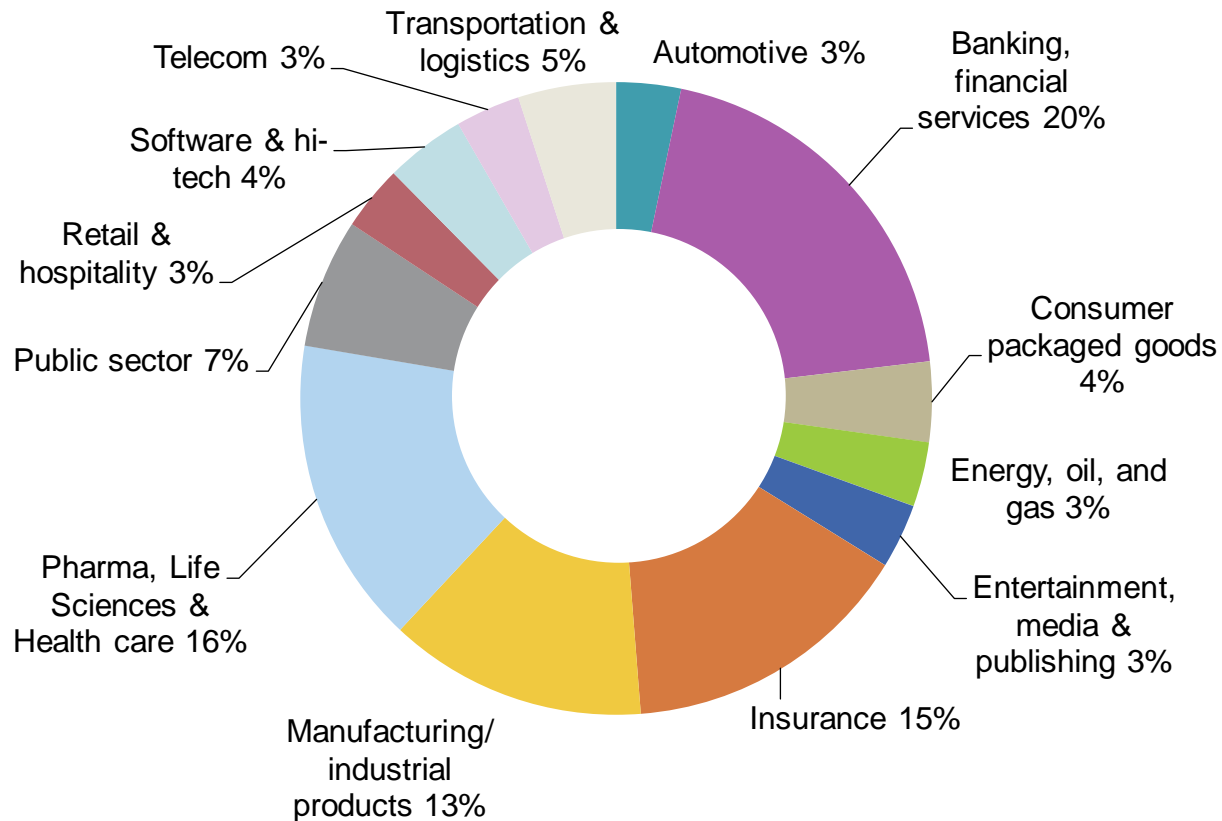
Which of the following roles best describes you?



Source: HfS Research in Conjunction with KPMG. Note: n=1079.

Survey details (continued)

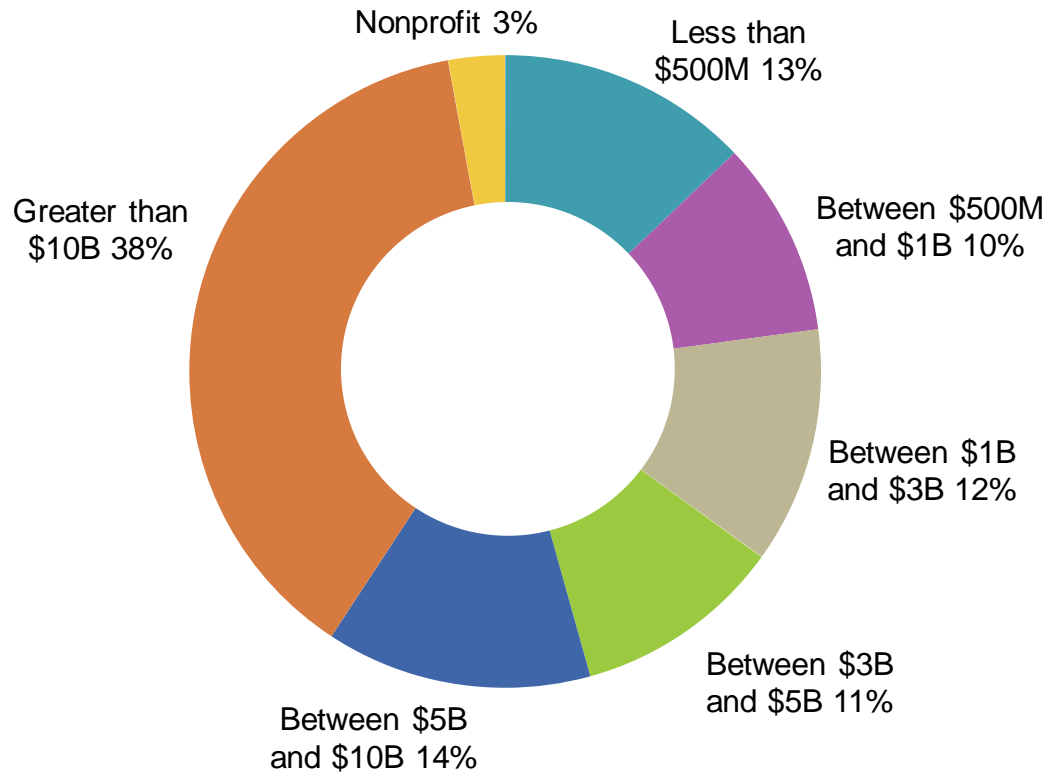
Please specify your company's industry:



Source: HfS Research in Conjunction with KPMG. Note : n=312.

Survey details (continued)

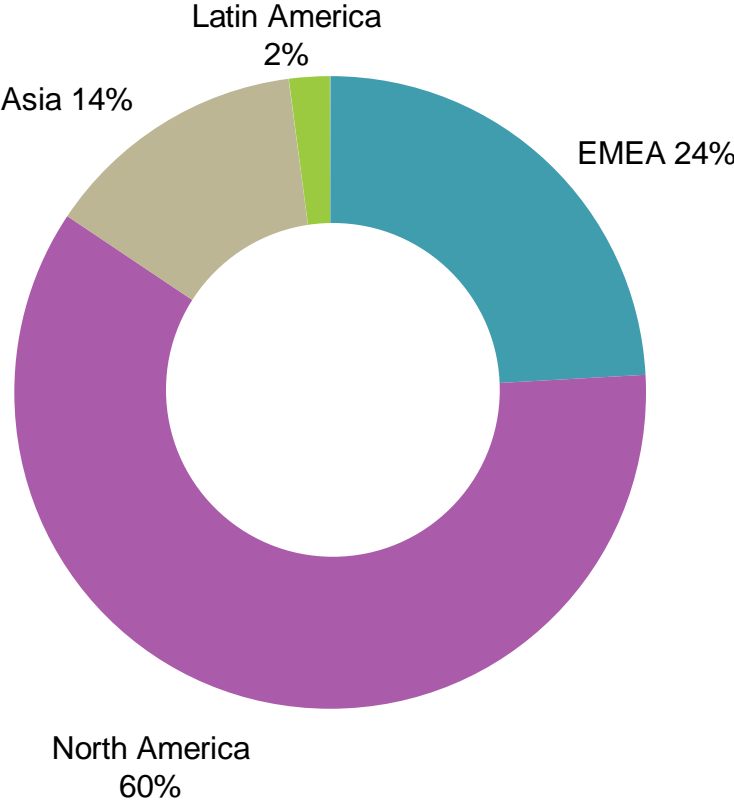
What are your company's annual revenues?



Source: HfS Research in Conjunction with KPMG. Note : n=312.

Survey details (continued)

Where are you located?



Source: HfS Research in Conjunction with KPMG. Note : n=312.

Buy-side groupings used for analysis

- Company size
 - Three groups under \$1 billion in revenue, between \$1 billion and \$10 billion and over \$10 billion
- Region
 - Three groupings Americas (United States, Canada, and Latin), EMEA, and Asia (including major Asian countries and ANZ)
- Industry
 - Three groups BFSI (banking, financial services, and insurance), manufacturing (discrete and process manufacturing product categories including pharma, consumer, hi-tech & industrial), and other

Appendix: About the authors



Phil Fersht, Founder and CEO, HfS Research



Overview:

- Over 18 years of business experience in the global outsourcing and shared services industry across the United States, Europe, and Asia
- An acknowledged industry advisor, strategist, author, speaker, practitioner, and blogger
- Advised on hundreds of global IT & BPO engagements

phil.fersht@hfsresearch.com

Previous experience:

- Practice head for IT Services & BPO Practice, AMR Research (Gartner Inc.)
- BPO Marketplace Leader at Deloitte Consulting
- Vice president for Everest Group, leading research and consulting teams based in the United States and India
- Prior career:
 - *Regional Director, IDC Asia/Pacific*
 - *Program Manager, European IT Markets Services, IDC Europe*

Education:

- BS degree with honors in European Business & Technology, Coventry University, United Kingdom
- Diplôme Universitaire de Technologie in Business & Technology from the University of Grenoble, France

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Education, licenses & certifications

- MBA degree, finance/accounting, Queen's University in Kingston, Canada
- Bachelor of finance degree/accounting, University of Windsor, Canada
- BA degree, sociology and psychology, University of Windsor, Canada

Background

Dave is the global lead for KPMG LLP's (KPMG) Shared Services and Outsourcing Advisory practice. In this role, Dave provides shared services and outsourcing advice to many of our larger, complex deal structures. Dave has more than two decades of experience in IT and business process outsourcing; shared services design/build/implement, sourcing management; contract renegotiations; and finance budgeting, planning, and analysis. Dave also delivers hands-on services as a client executive and has led many multinational deals and provided leadership support on several large and complex deals for both IT and business processes.

Professional and industry experience

In addition to advising clients, Dave engages senior members of outsourcing service providers' financial and IT delivery teams to establish and implement industry-accepted processes and structures related to outsourcing transactions.

Before joining KPMG through the acquisition EquaTerra, where he held various senior leadership positions including the establishment of the Financial Architect & Benchmarking practices and was a client executive leading large multinational, multifunctional shared services and outsourcing engagements, Dave was a senior advisor at TPI. In that role, he assisted clients with the evaluation, negotiation, implementation, and management of IT and business process sourcing initiatives.

Earlier in his career, Dave held various financial and IT positions in the telecom industry including Southwestern Bell Information Services, Southwestern Bell Directory Operations, Ameritech Advertising Services, and Bell Canada.

Sample client experience

- Led a large pharmaceutical company through a global IT outsourcing transition involving transitions with total contract value in excess of \$1 billion.
- Led Eli Lilly's global finance and accounting outsourcing transaction and global shared service design/build and implementation.
- Provided financial and negotiation support for Unilever's finance and accounting outsourcing deal (Europe and North America).
- Led an assessment of Oil's (Brazilian Telecom) IT operations, outsourcing and joint venture options. Led negotiations with third-party provider.
- Led a large U.S. oil & gas company through a finance and accounting outsourcing transaction providing overall leadership and financial support.
- Led a large transportation company through procure-to-pay sourcing opportunity providing leadership and financial support.
- Assisted several clients with leadership and financial support that were pursuing IT and finance and accounting sourcing opportunities through market assessments of their current finance and accounting environment, or financial support during the transaction or negotiation.

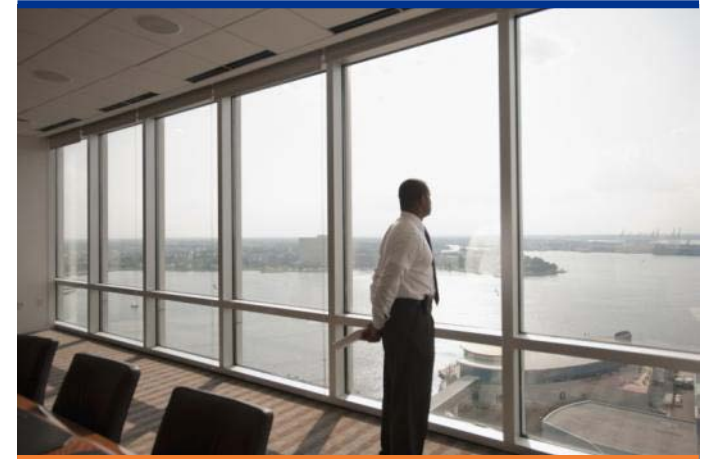
About HfS Research

- HfS Research is the leading analyst authority and knowledge community for business services strategies
- Dedicated analyst team across the United States, Europe, and Asia/Pacific, headquartered in Boston
- Distinct focus on business services and global operations with technology as an enabler
- Facilitates the HfS Sourcing Executive Council, the highest quality network of enterprise buy-side executives leading sourcing initiatives
- Industry-leading Governance Proficiency Certification Program (GPCP) is designed to help today's sourcing executives approach service provider relationships and governance strategy with a sophisticated and pragmatic approach
- Acclaimed research focus on demand-side trends, market landscapes, supplier evaluations (“blueprints”), pricing dynamics, market sizing, and forecasting
- Leverages the vast HfS community of sourcing professionals to deliver rapid insights on global sourcing industry trends and developments, surveying the opinions and dynamics of 20,000 organizations in 2011–13
- The largest Web and social media presence in the sourcing industry with 145,000 research subscribers and the leading blog in the industry (horsesforsources.com)
- A well-regarded new generation media outlet qualified as a Google news source and regularly quoted on services trends in the *Wall Street Journal*, *The Economist*, *CIO Magazine*, and *BusinessWeek*



About KPMG's Shared Services and Outsourcing Advisory practice

- The world's *largest independent third-party sourcing advisor with hundreds of dedicated sourcing professionals in Europe, Asia Pacific, and North America*
- Capabilities stretching across the *full life cycle of strategy to optimization*
- Extensive *global business services strategy, design, and implementation experience*
- Our advisors have *deep functional knowledge in all the major business support functions including technology sourcing, finance & accounting, human resources, procurement, customer contact, and facilities management*
- The *global reach of KPMG's Advisory member firm network – with 30,000 professionals across the Americas, Europe, the Middle East, and Asia Pacific*
- Our advisors are supported by a broad set of intellectual property, tools, and industry-leading research, including our quarterly *Sourcing Advisory Global Pulse Survey—providing insights into trends in end-user organizations' usage of Global Business Services (GBS) costs*
- *Active relationships with all Tier 1 and 2 vendors meaning we understand their business, capabilities (and limitations), strengths and weaknesses, and who the decision makers really are*
- Our *independence from vendor or technology means we can be trusted to provide unbiased advice to clients, serving their interests rather than our own*
- Access to KPMG International's broader set of global member firm capabilities in risk, transactions, tax, and compliance





cutting through complexity

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