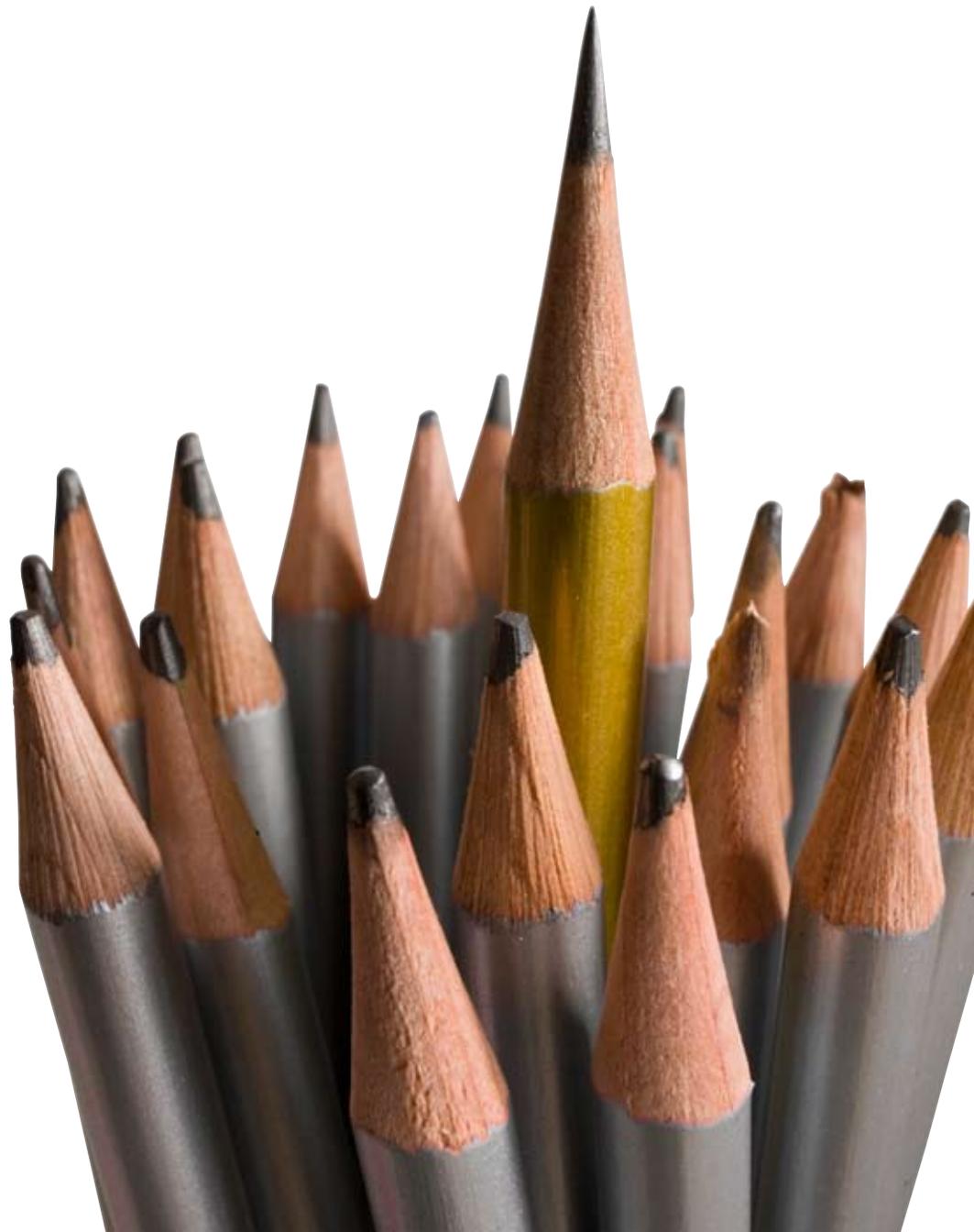


Value-driven AMS
The difference is in the results.



Preface

IT landscapes today are large and diverse, trending toward more complexity, not less. That complexity has become costly – with 65 percent of IT dollars now spent maintaining existing technology.¹ To control spending, many companies created new, specialized functions dedicated to managing applications and infrastructure. These have become prime candidates for outsourcing, driving explosive growth in the Application Management Services (AMS) marketplace. Gartner projects enterprise application outsourcing revenues to reach \$86 billion in 2013.² Which is all well and good except for one problem.



¹ US IT Budget Benchmarks – Preparing For 2010, Business Data Services North America and Europe, Forrester Research, January 2010.

² Forecast Analysis: IT Outsourcing Services, Worldwide, 2009–2013, 1Q10 Update, Gartner, March 2010.

The revenge effects of AMS

The history of business is filled with stories of new ideas that come back to bite companies – unintended consequences that can ricochet through the value chain like bullets. They're called revenge effects – and you can find them all over the outsourcing marketplace. To the extent that you're supporting applications through a low-cost labor pool that's isolated from the business, you can expect huge opportunity costs. Performance improvements in efficiency, knowledge transfer, and automation can all suffer. Inertia can swamp agility. And you can sacrifice the value of innovation.

The problem usually starts with low expectations. Traditional AMS can create a divide between applications support and the rest of the world. Even worse, the support function gets moved to denominator of the value equation, where the measure of success is cost reduction through labor. So when you finally do get around to looking for improvements, the people and resources aren't in place to deliver. Organizations then end up shuffling talent, hiring consultants, relearning, and rebuilding. And the practical knowledge needed to respond quickly to changing business demands is hidden in the heads of a floating labor pool, out of reach except at prohibitive cost.

Even worse, when improvements actually do happen, they're usually thrown onto the pile of outsourced applications for someone else to manage. Old assets then get disconnected from new assets and the cycle continues. The minute an existing application enters a stable state, it's put out to pasture with a "keep the lights on" mentality. The message to your organization is unmistakable: Anything that is already implemented is "old." New assets go unleveraged.

When you deliver applications management through a low-cost labor pool that's isolated from business innovation, expect huge opportunity costs.

Another part of the problem is the nature of the traditional applications outsourcing business model itself. For the most part, AMS providers have a strategic interest in pure labor arbitrage. Stable processes and more utilization make contracts more profitable over time. Change is a cost, not an opportunity for improvement. Even when implementation and management are bundled for procurement purposes, there's no inherent motivation to help customers reduce the cost of ongoing maintenance. When your business depends on throwing an army of cheap talent against every problem, innovations that might shrink the army will be generally unwelcome.

In response to this challenging environment, forward-looking IT organizations are starting to view applications management not as an isolated element in the technology lifecycle, but as a capability that must be tightly linked to continuous IT improvement and business innovation. That is the essence of Value Level Management (VLM).

Revenge effects

The world seems to be getting even with mankind, twisting our cleverness against us. Or we may be unconsciously twisting it ourselves. This is not a new phenomenon, but technology has magnified it. Wherever we look we face unintended consequences of mechanical, chemical, medical, social, and financial ingenuity. They are revenge effects, and they are less the malignant ironies of a spiteful world than the results of a lack of human foresight.

The first popular reference of revenge effects by Edward Tanner, in *The New York Times*, July 26, 1991

The evolution of value in Application Management Services

Historical patterns

- Labor arbitrage and scale provided some initial cost relief, but resulted in increased pressure on quality, risk, agility, and internal management.
- Separation between maintenance and continuous value delivery prompted “over the wall” engineering – favoring specifications over perspective, speed over insight. Attempts to supplement resources with skilled talent led to prohibitively high costs – especially for architects, project managers, and senior business analysts.
- Cost, capacity, and contract execution against tactical SLAs drove the agenda, not results and value.
- Deals were structured around business process improvement, but these were rarely achieved. Body count was all that mattered.

What’s different now?

- Cost and scale will always matter, but improvements based on labor arbitrage have hit the wall, with decreasing marginal returns. Limits are being reached on vendors’ ability to achieve further cost reduction – forcing a new focus on operational efficiency. IT Service Management adoption has demonstrated that service-based delivery models can improve IT operations while reducing costs.
- Application Management Services are being extended from operations and maintenance into Application Development Management and IT improvements, as well as broader lifecycle activities.
- Process standardization and maturity, along with improvements in tools, allow AMS providers to build platforms that enable rapid transitioning and drive operations automation.
- Cloud computing creates a new way to pool resources across multiple customers.
- AMS contracts can deliver attractive blended rates, mixing low-cost labor capacity with access to highly-skilled senior specialists to drive innovation and process improvements
- Organizations are defining value layers and Value-Level Agreements to complement traditional AMS. Benchmarking and advanced analytics are being used to baseline organizational performance and expected improvements.
- As the AMS market space has matured, so have buyers’ expectations for contracted value.

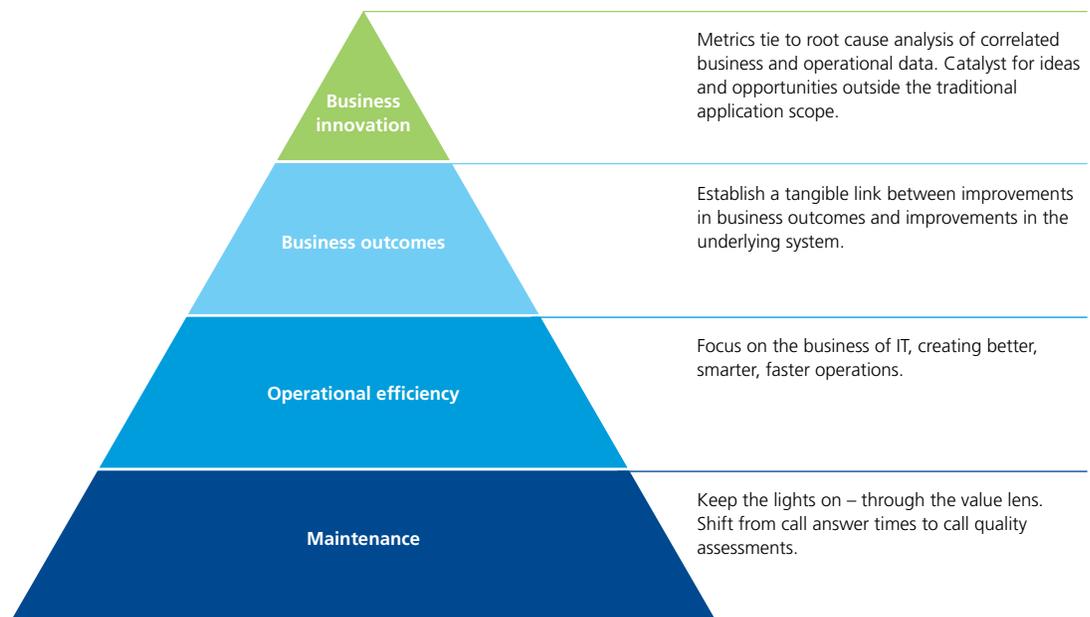


Build to run. Run to improve.

Companies making the shift to Value Level Management see early benefit opportunities as they climb the value chain. The first comes from adopting a value mindset – understanding that it’s possible to extract more value from the expense base. Everybody knows that’s a good habit to have, but it can be tricky for organizations that have spent years focused on cost reductions at the expense of innovation and improvement.

Next comes defining value at every level of the stack – from business results and innovation at the top, all the way down through applications maintenance and scaling. That’s not hard either. Just do what you know is right. Look for value opportunities at every stage of the technology lifecycle – and make the most of them when you find them.

Levels of AMS value



What gets measured gets done

Ask IT executives what matters most in an AMS contract and they will most frequently say “price.” After that, you’ll also hear about Service Level Agreements (SLAs), which are essential for tracking performance against technical service requirements. SLA metrics are easy to define, but that doesn’t mean they’re the most important thing to measure. Worse still, SLAs can actually lock-in applications problems – another revenge effect – instead of solving them. When organizations focus exclusively on SLAs, they rarely get to the root of persistent problems. Issues become opportunities for patches, gradually building up layers of fixes like duct tape on an old suitcase. Configuration tables get complicated, upgrades become difficult and expensive, and performance lags.

A better approach is to shift to a focus on business results and outcomes, not just service levels. That requires an AMS delivery model designed from the ground up to uncover value opportunities and implement improvements throughout every phase of the application lifecycle. Think of it this way: If the real value opportunities emerge when an application stabilizes, why then should that be the time to put that application out to AMS pasture?

In practical terms, the difference between a service-levels approach and value-levels approach rests on choices about what to measure. For example, tracking the rate of billing accuracy and improving it from 95 to 98 percent has much more value impact than tracking how quickly a call center answers the phone. Measuring satisfaction with the resolution of problems taps into a higher value level than measuring the duration of the conversations involved. Until you’re able to link knowledge gained in the back office to the outcomes expected in the corner office, you’ll never break out of the downward spiral.

Is it harder to track and manage value levels? Not really. Service Level Agreements are well-established in the AMS sector. Benchmarks and metrics for Value Level Agreements (VLAs) are just now finding their way into the language of outsourcing contracts. Expect to see more of them.

As you would expect, value metrics work most effectively when tailored to specific functions, industries, and IT organizations. For example, measuring performance improvements from ERP applications management would include tracking how quickly the finance organization can close the books. Value metrics for CRM or HR outsourcing, on the other hand, would track improvements in customer satisfaction and employee utilization rates.

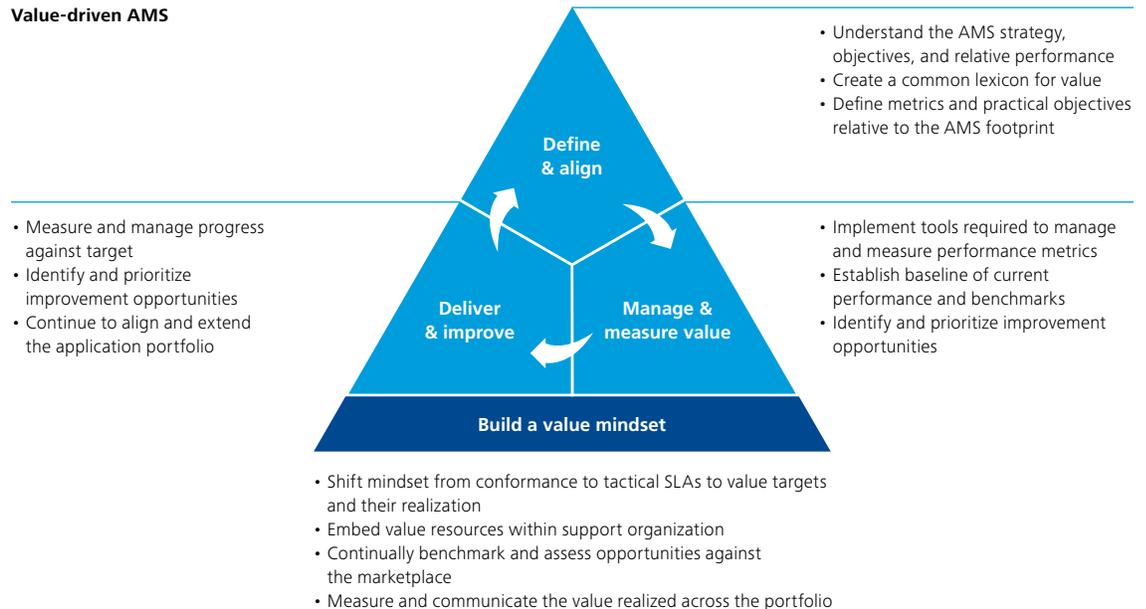
SLA → VLA

One letter makes
a world of difference



Getting into action

Value-driven AMS



Some things in business are really complicated – but value-driven AMS isn't one of them. Nothing could be more straightforward than tracking value opportunities surrounding valuable assets – and then executing on those opportunities as business conditions require. This is work you do every day.

So at the risk of reminding you of something you already know, here's a playbook for making the shift to value in applications management services.

- 1 Align stakeholder objectives. Sounds like jargon, but it's fundamental. Lots of people have a stake in applications running smoothly and efficiently. Get them all at the table.
- 2 Assign metrics. Tap into a good catalog of Value Level Agreements and get clear about which metrics matter most for the targeted function in your industry and sector.

- 3 Establish baseline of current performance and benchmarks. Get the snapshot you need going in – so you'll be able to track improvements.
- 4 Stand up the tools required to manage the metrics. You probably already have most of them in place. Just make sure they're sharpened.
- 5 Execute on the low-hanging fruit that came out of the first baseline. Companies invariably see immediate opportunities for improvement. Be prepared to move quickly to capture early value.
- 6 Use the metrics to identify and execute on efficiency opportunities in terms of labor leverage, automation, and consolidation. You'll likely have more opportunities than you know you can effectively handle. Plus, execution in one area will affect operations in another. Keep one eye on the big picture.
- 7 Continue to align and extend the application portfolio. Value gets built over time, not in one fell swoop. Don't turn your back on legacy.

Value Level Management in action:

Merger Integration

A recently spun-off technology company is finally free to grow – with a strong pipeline of critical acquisitions in play. What’s a smart way to manage applications while rapidly integrating new businesses and IT organizations? What’s a short path to unified customer management, supply chain integration, and rationalized product management across the new business – and across the full range of functions and business processes?

The traditional AMS approach

Solutions are isolated in offshore operations, maintained by a separate “keep the lights on” organization focused on technology break-fix and maintenance. Business liaisons, technical architects, project managers, and other skilled resources responsible for IT integration are quickly redeployed to other initiatives. Because of the perceived difficulty in driving deep integration and continuous improvements, the business turns to new custom platforms, while legacy systems become more cumbersome and unresponsive. The expected synergies and benefits of the merged companies don’t materialize.

Using value-driven AMS

The ongoing operating model, information assets, and integration plan can be addressed together at the outset – as can be business capabilities, with attention on dependencies and critical relationships. Process owners and business architects are assigned to drive to value, during and after integration. “Steady state” technology, process, and information governance teams work closely with the merger integration team – delivering a smooth transition to the support organization. Tools for incident, request, change, and problem management are established and leveraged throughout the integration. This enables refinement and continuous improvement once the business stabilizes – all according to the value drivers identified up-front by the business.



Bottom line?

Use value-driven AMS to create value from your expense base

Traditional AMS focuses only on labor-driven cost improvement. That's great as far as it goes, but it doesn't go far enough. Especially when efficiency-driven cost savings and top-line value creation are well within reach. More importantly, the transition to a value-oriented operating model is transformative in nature. It not only can help shift your organization toward service-driven IT, it can also provide a holistic view across projects and ongoing operations and maintenance – helping to drive business alignment no matter how dynamic the operating environment. Organizations that embrace value-driven AMS can expect benefit opportunities in three specific areas.

Business aligned application management

By working with the business to define objectives, value, and associated metrics, organizations have the opportunity to embed those metrics into every application decision. This moves operational activities toward a convergence of service levels, efficiency levels, and value levels – and helps embed Value Level Management into the full lifecycle of operating processes.

Lower costs, improved quality

Industrialization of AMS is the foundation for extending value beyond labor driven cost improvements. It allows you to find efficiencies from the transaction level up, to help add value in the hand-offs, eliminate wasted time, and streamline feedback to drive continuous improvement. Additionally, value can ignite when industry and business knowledge are used as catalysts to reduce the amount of effort required to return the desired result.

Improvement and innovation

One of the big challenges of large-scale AMS operations is their inability to share knowledge up the value chain. Getting that done requires designing services for effective hand-offs. Patterns in value metrics can become the fuel for targeted improvements and innovations – but only if you've built in an operating model that identifies those patterns in the first place.

Make the shift

Value Level Management can help preserve market arbitrage benefits for the lower-level operations of any AMS contract. Vendors must continue to match cost structures and service levels as table stakes. But beyond cost and scale, the value-driven approach can provide a vehicle for enabling business results – allowing for resource fluctuations, distribution of risk, and a full blend of specialized skill-sets that can be accessible at any time.

The shift from service-level maintenance to value-driven management is a significant one – and can help IT transform from a cost center to a strategic partner to the business.



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