

Gartner Says Outsourcing Grows in Declining European IT Services Market

European companies wasted 6 billion Euro due to poor deal structures and poorly managed relationships with IT outsourcing companies in 2002

Egham, UK, 28 April 2003 — Speaking at its annual Outsourcing and IT services summit in London, Gartner today said the Western European IT services market slipped into decline for the first time in 2002, contracting by 0.11 percent. Outsourcing was the only segment within the overall IT services market to see positive growth, expanding by 6.3 percent. The fall in the overall market was primarily caused by the consulting and development and integration services sectors, which together declined by 4.6 percent, but make up a larger proportion of the market than outsourcing. Gartner said the growth in outsourcing reflects the significant and measurable bottom-line gains that can be made from a sound outsourcing strategy, but belies the growing number of problems blocking the emergence of a successful IT outsourcing model. It warned that while outsourcing is growing, satisfaction levels with outsourcing contracts are falling, a great deal of money is wasted on poor relationship management and deals are still signed too frequently to save money in the short-term, without structuring the contract to achieve long-term business goals.

Gartner said the Western European IT services market will continue its current trend of polarization between vendor groups for the medium-term future, with growth at both ends of the market. Large-scale service aggregators and niche providers of specific services will continue to grow steadily. However, space for middle-market IT services companies offering generalist solutions has entered a steep decline.

Business satisfaction with outsourcing falls

Satisfaction with the business benefits from outsourcing contracts fell from 86 percent in 2001 to 50 percent in 2002 among board-level executives in Western Europe, according to Gartner. Although service levels delivered by vendors remain high, short-term thinking means company bosses are failing to see the tangible benefits they had hoped for from their sourcing strategy. Gartner said that European companies wasted 6 billion Euro due to poor deal structures and poorly managed relationships with IT outsourcing companies in 2002, and that relationship management problems can add up to 15 percent to the cost of an outsourcing project.

"Current levels of management in the IT services industry can be compared to the construction industry of around 1860," says Roger Cox, Vice President IT Management strategy and planning research at Gartner.

"The skills and training required to implement and manage ongoing outsourcing projects are not yet mature, and the industry is still going through irreversible changes and development. As an outsourced industry, IT is maturing fast but is still a long way from real stability."

"Outsourcing is not a panacea," continues Gartner's Cox. "Doing it wrongly can be worse than not doing it at all, and wastes a gigantic amount of money. If a business focuses on the short-term accounting target of signing the deal rather than the long-term goal of delivering value to the business, its outsourcing strategy will fail. The companies that outsource successfully are investing time and resources now in the skills, processes, resources and governance structures to manage long-term relationships in uncertain and changing times. A long-term deal with a major service provider is a potential business asset, but can be wasted if not managed effectively."

Auditors begin to probe outsourcing contracts

Problems with outsourced business functions can also have profound knock-on effects on a company far beyond the functioning of its technology. As enterprises become more dependent on outsourcing, investors and financial analysts will start to not only evaluate the enterprise, but also the company they keep. Institutional investors are beginning to demand greater assurances that long-term outsourcing deals will succeed before putting money behind the company and partnerships concerned. Financial auditors will start to investigate more deeply the accounting of major outsourcing deals. Industry regulatory bodies also require firm evidence of consistency and integrity of processes in outsourced scenarios, especially in industries such as financial services and pharmaceuticals, where compliance issues are beginning to arise. Gartner warned that companies that do not rigorously evaluate their outsourcing strategy can find themselves foul of all three groups, resulting in product license obstacles, accounting investigations or even being cut off from funding.

How to evaluate your outsourcing strategy:

Gartner urged companies to focus on three considerations when embarking upon a long-term outsourcing deal:

Take the long view — your service provider is going to become part of your company

The only certainty is uncertainty — build your deals for continuous change

You are probably the biggest problem — invest in the skills, resources and processes to manage these complex relationships

"The economics of IT outsourcing make a viable and attractive long-term business proposition," says Cox, "but significant issues remain to be resolved before this market sufficiently matures to the satisfaction of customers, auditors and regulators. With more fundamental processes managed by outside contractors, the intrinsic value of a company in the future will become ever more dependent on its strategic sourcing capability."