

Report
September '22

EXTRACT



EMERGING

Managed
Services:
Delivering on
the Promise

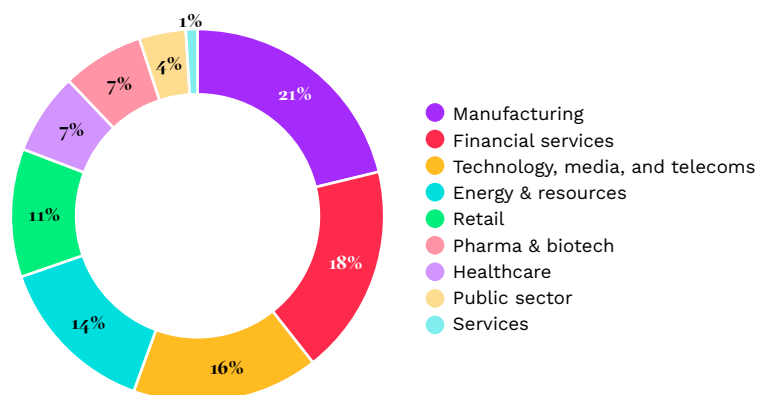


Methodology

The data in this report came from a variety of proprietary sources. In addition to a specially commissioned survey, detailed below, we've also incorporated data from:

- Our annual client perceptions survey, carried out in November–December 2021 and which has around 10,000 responses about individual firms.
- Survey data gathered in June this year for our annual US market trends report.
- Interviews we've carried out with senior clients over the last 3–4 months.

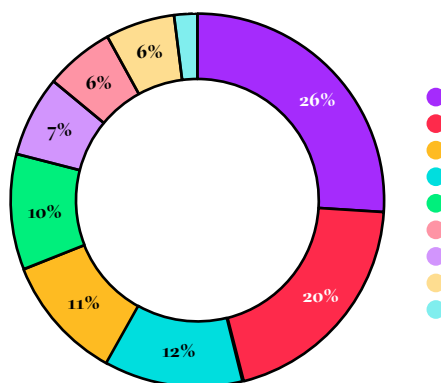
Respondents by sector



Survey sample

The bulk of the data in this report comes from a study conducted in July 2022 of 150 senior executives, all based in the US. All of our respondents worked in private-sector organisations with 1,000 or more employees. Because managed services appeals to mid-sized organisations as well as large ones, our sample for this report is slightly different to the norm: Twenty-eight percent of respondents came from organisations with more than 5,000 employees, with the rest coming from organisations that had between 1,000 and 4,999 employees. All held a “head of department” or more senior position; and all had been directly involved in buying and managing consulting projects.

Respondents by functional role



Interviews with senior leaders

In addition to our quantitative research, we interviewed five very senior consultants, to understand more about how the managed services market is performing and the major trends, changes, and challenges consultants and their clients face. Throughout the year, Source analysts remain plugged in to the global consulting market through our bespoke research and consulting projects, adding further depth to our understanding.

Name	Job title	Organisation
David Brown	Global Head, KPMG Managed Services	KPMG
Paul Clark	Global Vice Chair - Managed Services	EY
Chris McClure	Partner ESG Services Leader	Crowe
Ian McConnell	Partner	PwC
Toby Munyard	Vice President	Efficio

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Part 1: The key components of a managed service

What is a managed service? Definitions inevitably differ, so a good place to start is to ask clients what they think a managed service involves. We did this by asking clients to position their preferences along a number of continuums, each of which reflects aspects that clients have mentioned in interviews.

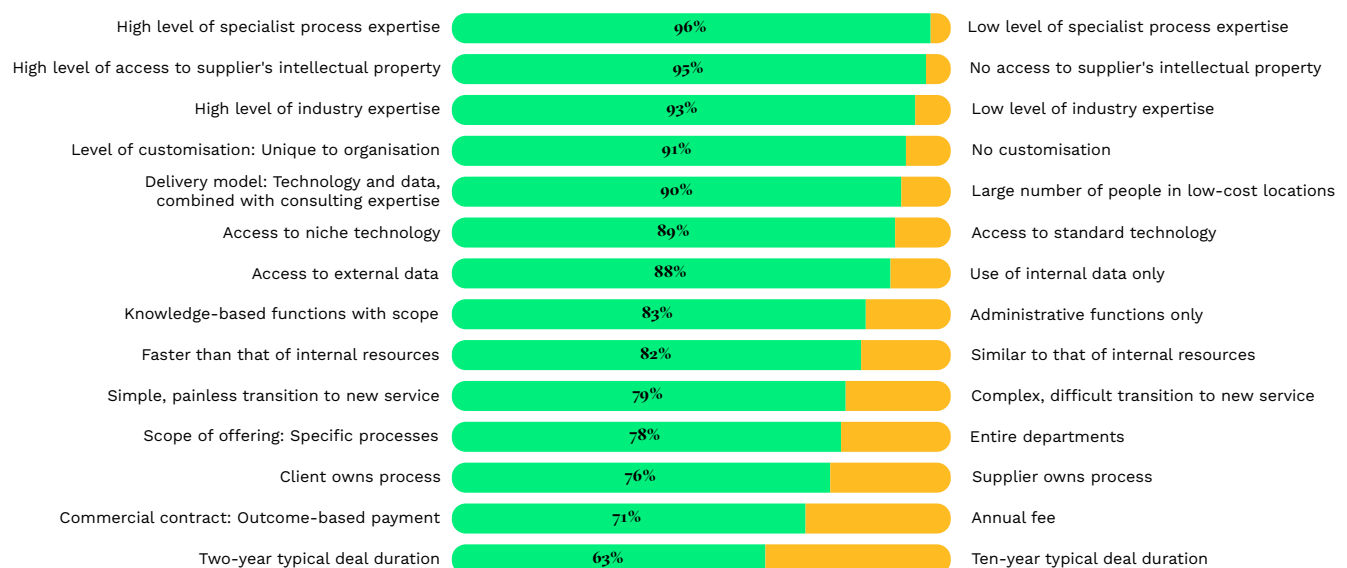
The first thing that strikes you, when looking at the results, is the important relationship between technology and expertise: More than nine out of 10 clients say that a managed service will include a high level of specialised process and industry expertise, access to the supplier's intellectual property, and that it will be a combination of technology, data, and consulting expertise. Organisations are looking for a better solution, not a mess-for-less approach.

The pandemic has highlighted the extent to which clients and, by extension, their suppliers need to work in partnership with other, perhaps more specialised organisations. In an environment facing unprecedented levels of change, no one firm can have all the right answers. Just under 90% say that they expect a managed service to give them access to data outside their organisation and to specialised technology. Eighty-two percent of clients say that a managed service has to deliver work faster than a comparable internal process—a finding that supports other research we've done this year. As clients emerge from the pandemic, only to find themselves facing a whole series of economic shocks, their focus is increasingly on speed: If they're going to thrive in a highly uncertain environment, they have to make decisions and act on them very quickly.

The final cluster of components relate to the way in which the service is delivered, rather than its content. In contrast to traditional outsourcing 10 years ago, clients today are looking to include knowledge-based processes, not just routine administrative ones. They're also focused on specific processes rather than trying to solve all the problems of a department in one go and want to retain ownership of the process instead of handing over responsibility to the supplier. This means that they expect the transition to the managed service to be relatively simple and pain-free. Opinions are more divided when it comes to payment and duration. Just over two-thirds of clients would prefer to pay based on the outcome of the work delivered, rather than via a more conventional fee, while just under two-thirds expect the managed service to last for a shorter period than a traditional outsourcing deal would—two years, rather than 10.

Figure 4

The key components of a managed service, in clients' eyes





Part 2: The appeal of managed services

A resounding 100% of those we surveyed think the managed-service approach is relevant to them, with 51% saying they've already adopted it to some extent. Sixty-four percent of respondents overall said they're already using or will use a managed-service approach in the future, and this rate of positivity around adoption is evenly spread across large and mid-sized organisations.

Figure 8

Would your organisation consider engaging a professional services firm for a managed service as we have defined it?

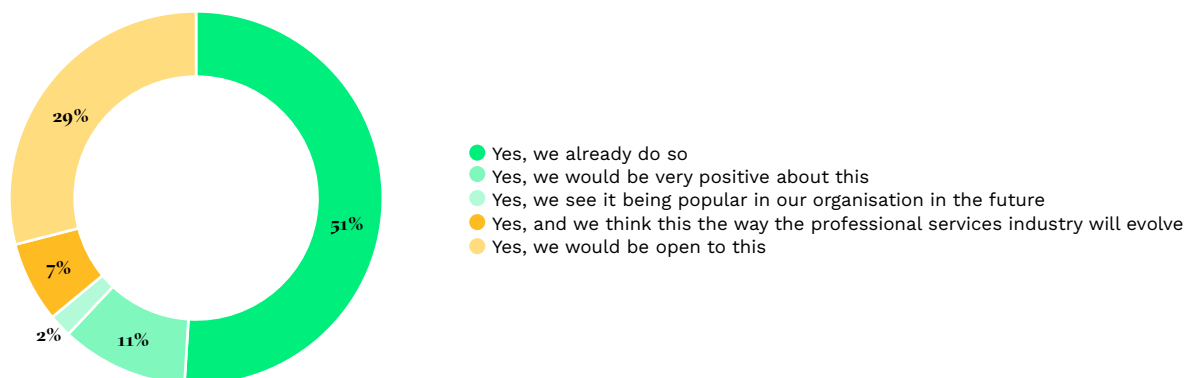
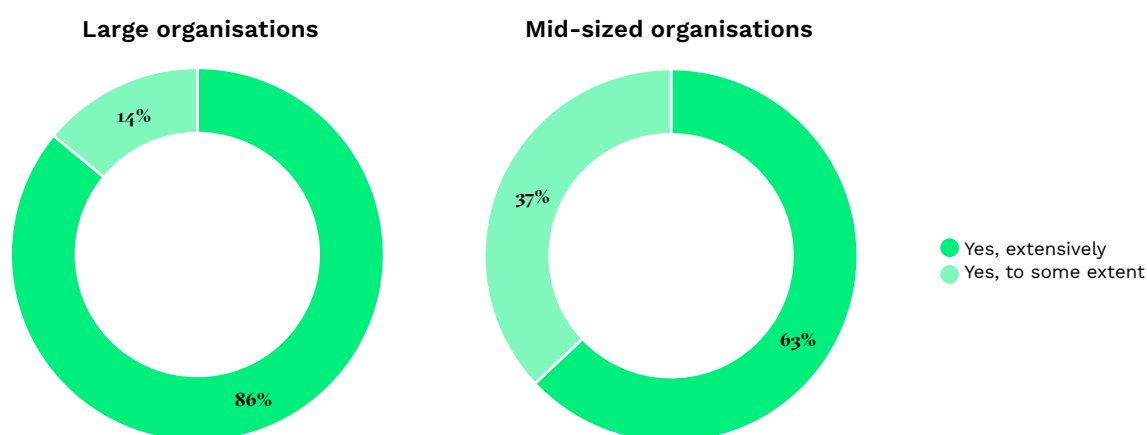


Figure 9

Is your own function already using or likely to use managed services from an external supplier?



Conversations we've had with clients suggests that their decision about whether or not to buy a managed service, as we've defined it here, depends on the extent to which:

- Their organisation has—or does not have—sufficient organisational capacity
- They're prepared to put at least some aspects of their core activities into the hands of external suppliers
- They think that an external solution will be better than an internal one

Part 3: Use of managed services

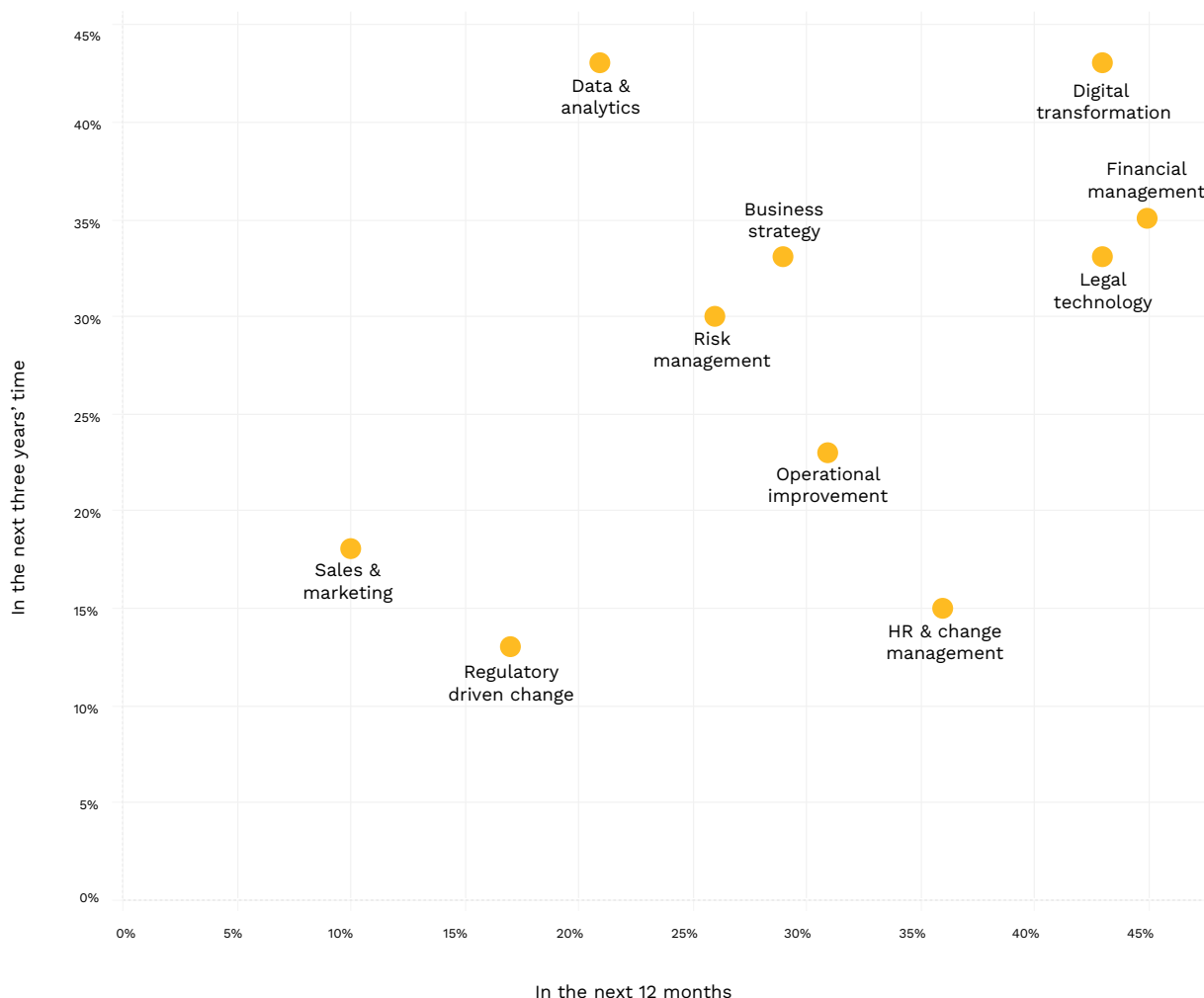
The different motivations that underpin the adoption of managed services in large and mid-sized organisations are likely to affect the type of managed services these organisations buy.

The charts below compare the extent to which clients expect to replace traditional consulting with a managed services approach in the next year (the horizontal axis) with their expectations about the next three years (the vertical axis). Large organisations are most likely to use managed services in their digital transformation programmes, and it's something they're already doing and expect to continue to do to a similar degree. The most significant area of long-term growth will probably be in the data & analytics space, where the 21% of clients saying they are likely to use managed services in the next year almost doubles to 40% when it comes to the next three years. However, there are areas, such as HR & change, where relatively high levels of activity in the short-term may result in lower growth over the next three years.

Among mid-sized organisations, whose investment in digital transformation often lags behind that of large companies, the extent to which they use managed services in that space is likely to grow. Offset against this, however, appears to be a lower rate of growth in the future in HR & change management, operations, and regulatory-driven managed services.

Figure 14

Which traditional consulting services do you think are most likely to be delivered as managed services in your organisation? Large organisations only





Part 4: The key challenges?

So far so good: The pandemic hasn't dented clients' enthusiasm for managed services; if anything, their interest in alternative delivery models is now being strengthened by a lack of in-house capacity, the need for new, fast-moving skills, and a growing sense that a managed service might be a better solution than conventional consulting.

However, no market is without its challenges, and the data we've gathered for this report highlights four of these that consulting firms should at least consider.

Challenge #1: Positioning around price

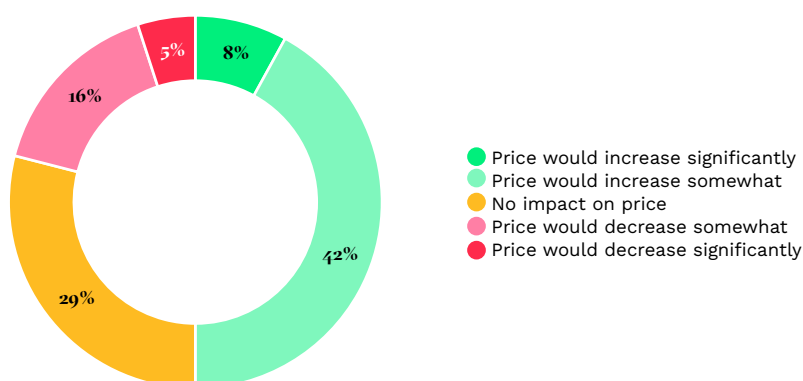
Despite the boom in demand for consulting services in the last 18 months and the supply-side talent crisis, many clients remain stubbornly unwilling to countenance price increases. Looking at the overall US consulting market, the 40% of clients who expect fee rates to rise is higher than it was a year ago. However, just over a third of clients think prices will fall, roughly seven times the percentage it was before the pandemic. And it's the pandemic that's largely to blame for this situation: Around three-quarters of clients come up with their first reasonable estimate of the cost of a project before they've scoped it, let alone sent out a request for proposal. That initial estimate is based on past experience—which at the moment is being informed by heavy discounting during the COVID crisis, and which will take some time to recede from clients' memories, meaning that pressure on prices is likely to persist for this year and on into next.

Pre-pandemic, pricing was the biggest challenge for firms trying to grow their managed services businesses. In research we did at the time, we typically found that around a third of clients expected a managed service to be cheaper than a conventional consulting one. There were two reasons behind this. The first is that clients' views were—again—informed by past experience: Like traditional outsourcing, the first generation of managed services was designed to cut costs, not add value. The second reason was that clients assumed that suppliers were trying to switch to a different delivery model to cut their own costs, that the introduction of software assets into the consulting process meant less need for junior staff, and that they—the client—should be able to benefit from this increased efficiency.

Post-pandemic, the picture around the pricing of managed services looks somewhat different. Overall, around a half of the clients we surveyed said they'd expect to pay more for a managed service, as opposed to fifth who said they'd expect the price to be lower.

Figure 17

What impact on price would you expect to see from this move to managed services?



Part 5: Is there a winning formula?

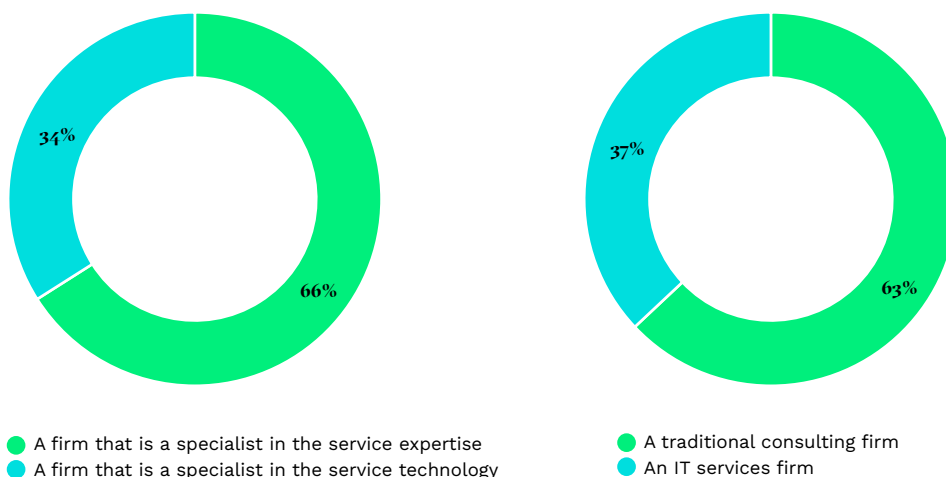
Every challenge is, of course, an opportunity. Consulting firms that can find solutions to the issues discussed in the previous section will steal a march over their slower-to-respond competitors. But how do clients see this? To what extent will the preferences they have today shape the managed services market of the future?

Looking beyond clients' assumptions

There are many types of firm that could offer clients a managed service, including business process outsourcing and other outsourcing companies, systems integrators, technology consulting firms, the Big Four, and traditional management consulting firms—and that leads to considerable confusion on the client side. One message that does emerge from our data is that firms with deep expertise have an advantage. Asked if they'd prefer to work with a firm that has expertise in the topic on which the managed service is focused or a firm that has technology in that space, 66% of clients say the former. That then translates into 63% of clients who say they'd prefer to work with a consulting company rather than an IT services firm (which they might associate with old-school managed services).

Figure 24

Which are you more likely to use for managed services if all else was equal?



However, if we take a bottom-up approach, asking clients to rate firms against the components they thought important in a managed service, then aggregating their responses, we get a different picture. Technology firms do better, being selected by 56% of respondents, compared to the 34% that picked a traditional consulting firm.

Figure 25

In your opinion, which type of firm is the best for each of these aspects of a managed services offering?



Part 6: Insights with Managed Services Leaders



David Brown, Global Head, KPMG Managed Services, KPMG

We define managed services as continuous support to a client through a combination of expertise, data, and technology to address an ongoing need. Is that the definition you would use at KPMG?

That's pretty much spot-on, especially the part about ongoing support. Traditional outsourcing has focused on transactions, but today's managed services focus on transformation, helping clients continue to evolve their business functions and stay ready for whatever comes next. Of course, traditional outsourcers also had some tech, but it was more about increasing efficiency and maximising their profits than providing insights to the client. Today, leading managed services providers use their expertise, tech, and data analytics to bring new value to processes, including insights on areas like growth opportunities, competitive position, and risk.

Do you think clients understand the evolution of managed services?

Broadly, not quite yet. I'm very well-versed in the evolution of the outsourcing market because I've helped clients in this area for about 20 years, and when many see the phrase "managed services," they still think of low-cost transactions through labour arbitrage. But modern managed services are very different from that legacy model. Today, companies can outsource knowledge-intensive processes to a provider's platform on a subscription, as-a-service basis, while taking advantage of the provider's expertise and analytics, and going beyond cost savings to drive outcomes like growth, resilience, and stakeholder trust. This is the kind of work we want to become known for.

Take customer due diligence, for example. There is a lot of transactional work in there, but there's also opportunity to advance the business. Instead of lifting and shifting a compliance process, smart managed services providers could use the data they're collecting to help clients better understand their customers and get insights for new products and services.

Do you think the pandemic has pushed it faster in that direction?

Yes, and the momentum was increasing even before, with a build-up of pressure in the quest for talent, along with big shifts in regulatory requirements. Then the pandemic brought profound marketplace changes, including remote working at scale. For example, a lot of clients previously weren't willing to give some work to third parties because they were in a different location, but now they're doing the same with their own work-from-home teams. Third parties have also shown they can deliver work remotely, outside of a cleanroom.

So now we have new ways of working, new customer behaviours, and a fast-changing market, which means companies need to continually reshape their business—it's not a one-and-done. Managed services provides this ongoing support, helping companies keep up with evolving technology, talent requirements, and changing priorities.

For example, we're seeing a lot of pickup in cyber managed services. Rather than just helping clients once a threat has been identified, providers deliver ongoing threat monitoring and response. This is a compelling alternative to continually investing in cyber tech and hard-to-find staff to keep on top of these things.

How do you see KPMG being different from its competitors?

We talk about our managed services value proposition in the context of "three beyonds" to enable ongoing transformation. First, we go beyond the back office to deliver high-value work across the enterprise—and not just in non-core processes like most competitors but also in core, differentiating activities that may have been traditionally kept in-house. Second, we go beyond cost savings to drive other kinds of outcomes, like improved stakeholder trust through ESG services or improved forecasting through analytics. And third, we go beyond technology alone, bringing our deep subject-matter expertise to everything we do, along with strong experience in change management. In other words, our managed services are tech-enabled but strategy-led. We're ultimately helping clients create successful operational models for growth and advantage.

How much of your expertise is in-house, and how much are you reliant on an ecosystem of alliances and partnerships?

KPMG people have renowned expertise across functions, industries, and tech domains, and we have a robust in-house portfolio of automation. But given the speed of change, we also have strategic alliances with world-class technology, data, and services companies. One reason clients come to us for managed services is because they don't want to take on the investment to keep up with technology, they don't have the discipline to stay on top of the market, and they don't have the resources for an ongoing parade of third parties pitching their tech stacks. So we use our combined expertise and technology—from throughout the KPMG ecosystem—to bring clients the best offering and help them continually respond to disruption.

How do you reach your clients with your managed service offerings? Is it through thought leadership or practical demonstrations?

During the pandemic, a lot of our clients got behind on work due to labour shortages and disjointed processes, so we used our strong relationships with CFOs, CISOs, and other business leaders to step in and help them out. But rather than come in with a staff loan, we used it as an opportunity to demonstrate our managed services operating model. Based on those successes and the confidence that clients have in KPMG, we've earned their trust to provide managed services in additional areas. Meanwhile, we're using our thought leadership to continue educating the market about modern managed services, show what it looks like and change some of the legacy perceptions.

Meet the experts

Fiona Czerniawska

A Co-Founder and Managing Director of Source, Fiona is one of the world's leading commentators on the management consulting industry. Since founding Source in 2008, she has been bringing this expertise to bear on our clients' most pressing strategic projects and business issues. Fiona has published a dozen books on consulting topics, including two for The Economist: *Business Consulting: A Guide to How it Works* and *How to Make it Work* and *Buying Professional Services*.

She has more than 20 years' experience as a management consultant, working primarily in the areas of marketing and strategy. She was previously in charge of strategic planning for EY in the UK and has worked in the consulting practice of PwC. Fiona also has a PhD in 17th century French art and lives in hope that it will be of practical use in business someday.

Fiona Czerniawska

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Catherine Anderson

Catherine is a Principal Consultant at Source in our consulting practice area. Focused on bespoke project work, she turns qualitative and quantitative data into meaningful, strategic insights for professional services firms. Recent projects include identifying opportunities in new markets and analysing client sentiment and how to harness it effectively. She also oversees the Emerging Trends programme, and is often found presenting reports and research on a wide variety of topics. Prior to joining Source, Catherine managed large transformation programmes in the financial services sector.

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About us

**We help professional services firms
understand what really matters when
facing decisions of vital importance.**

The best decisions are based on evidence, objectivity, and a willingness to change. That's why, at Source, we tell you what you need to hear, rather than what you want to hear.

We draw upon our deep roots within the professional services sector to provide firms with a clear picture of their clients' worlds. Through comprehensive research and meticulous analysis, we pinpoint what truly matters and deliver actionable insights that help firms map out the right way forward.

We believe in thriving individually and succeeding together. And we would love to help your firm crack its latest conundrum.

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Programme schedule for 2022

Reports 2022	Market Trends Programme	Client Perception Studies	Emerging Trends Programme
Q1	January	UK US	
	February	Germany Financial Services	
	March	GCC France Healthcare & Pharma	Pricing: Your Biggest Barrier to Change?
Q2	April	Nordics Energy & Resources Technology, Media & Telecoms	
	May	China Japan	
	June		Agility and Multidisciplinary Working
Q3	July	Tax South America	
	August	Risk Tax	
	September	Audit	Managed Services: Delivering on the Promise
Q4	October		
	November	Risk Consumer Products & Retail Healthcare & Pharma	Delivering Value Through Innovation
	December	Planning for Growth in 2023	Relationships in a Hybrid World

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