CompTIA

TRENDS IN MANAGED SERVICES OPERATIONS

FULL REPORT

RESEARCH

DECEMBER 2012

www.comptia.org

About this Research

CompTIA's *Trends in Managed Services Operations 2012* study seeks to gain a better understanding of the key trends in the managed services provider space, including covering areas such as internal operations, software infrastructure selection and general business transformation.

Research Objectives:

- Identify the profile of today's managed services practices, including business lines adopted now and in future
- Identify business challenges for MSPs, including sales/marketing changes and impact of trends such as cloud
- Measure and track operational efficiency of MSP businesses, including what software tools are chosen and used, how pricing is determined, how customers are retained.

The study consists of four sections, which can be viewed independently or together as chapters of a comprehensive report.

Section 1: Managed Services: Market Overview
Section 2: Managed Services: Business Operations
Section 3: Managed Services: Software Tools
Section 4: Managed Services: Sales, Customers, Pricing

Research methodology
The data for this quantitative study was collected via an online survey conducted during October 2012. The sample consisted of 400 IT solution provider or channel firms. CompTIA employed the services of a dedicated research panel provider to procure the sample. The margin of sampling error at the 95% confidence level for the results is +/- 5.0 percentage points. Sampling error is larger for subgroups of the data.

As with any survey, sampling error is only one source of possible error. While non-sampling error cannot be accurately calculated, precautionary steps were taken in all phases of the survey design, collection and processing of the data to minimize its influence.

CompTIA is responsible for all content contained in this series. Any questions regarding the study should be directed to CompTIA Market Research staff at research@comptia.org.

CompTIA is a member of the Marketing Research Association (MRA) and adheres to the MRA's Code of Market Research Ethics and Standards.

TRENDS IN MANAGED SERVICES OPERATIONS

SECTION 1: MANAGED SERVICES: MARKET OVERVIEW

RESEARCH

DECEMBER 2012

www.comptia.org

Key Points

- Business transformation, including the shift to managed services, is a growing factor at the upper end of the channel today. Nearly half of firms with $50M or above in annual revenue identified themselves as undergoing high levels of business transformation, meaning that their revenue mix/product profile has changed significantly in last two years.

- Roughly 4 in 10 characterize themselves as "skilled experts" in managed services today, while just more than half claim to be "competent and getting better." Those optimistic descriptors – while noting they are self-assessed – compare with just 9% of respondents that report being early into their managed services learning curve.

- Four in 10 channel firms that are not involved in managed services today say they are waiting to see the impact of cloud computing will have on the evolution and lifespan of managed services.

Market Overview

Palatable or not, the long-term lifeline for a large segment of today's IT channel depends upon cultivating a successful business that sells and delivers technology services on a recurring revenue basis. This objective marks a shift away from conventional reliance on product-based transactions and/or one-off project engagements to a more predictable operational model that charges customers much like a utility company bills monthly for services-rendered. Burgeoning trends such as cloud computing and mobility, combined with expanded customer choice for procuring technology, are factors hastening this transition urgency in the industry.

For many channel firms, a change in tack has meant a foray into managed services – either as an add-on part of an existing business or as a complete overhaul from what is being done today. The managed services model typically takes of the form of an ongoing contractual arrangement in which the third-party provider (or MSP) remotely monitors, manages and updates a customer's technology infrastructure, systems and services such as email, network and security software, or increasingly more complex pieces of technology such as line of business applications and analytics. IT functions once commonly handled in-house become outsourced, effectively.

After nearly a decade in fruition, managed services is becoming more commonly practiced across the channel and generating demand among end users. It's a steadily growing market that is not going away, despite some uncertainty about the overlap and/or impact that newer cloud-based models may impose.

Expected Change in Managed Services Revenue Next 5 Years

17%	High Growth (75%+ of total)
64%	Medium Growth (Escalating share of revenue)
19%	Flat or Declining Growth

Source: CompTIA's *Trends in Managed Services Operations* study

Consider the following:

- Gartner predicts that worldwide spending for IT outsourcing (ITO) services is on pace to reach \$251.7B in 2012, a 2% increase from 2011 spending of \$246.6B. The fastest-growing segment within that market is cloud compute services, which is part of the cloud-based infrastructure as a service (IaaS) segment. Cloud compute services are expected to grow 49% in 2012 to \$5B, up from \$3.4B in 2011.

- IDC expects that the business process outsourcing (BPO) market will grow at a five-year CAGR of 5.3%, reaching \$202.6B in 2016. The U.S. market is expected to grow at a five-year CAGR of 4.2%, reaching \$92 billion in 2016. BPO often refers to higher-level outsourcing of processes that underpin the running of a business' technology, but do fall within the managed services category.

- In its study, *IT Outsourcing Statistics 2012-2013*, Computer Economics finds that among end user organizations that outsource IT work, the percentage of total IT budget going to service providers rose at the median from 6.1% in 2009 to 7.1% in 2010. It remained at about that level for a year and then jumped to 8.6% in 2012, a move they contend reflects both the cyclical recovery in IT spending and longer-term growth in IT outsourcing.

- While the above market data points pertain to the broader business process outsourcing market, which tends to address mainly large enterprise customers, the typical managed services provider at the IT channel level are much smaller in nature and provide basic IT services such as managed print or remote desktop monitoring to customers in the SMB space. Consider the following: Mindshift, which is the largest US-based pure-play MSP in generated approximately $100M in revenue during 2011, while an Accenture, IBM or other major purveyor of BPO services brings in far higher amounts (in the billions in some cases). Because of these discrepancies in managed services categories and definitions, it's difficult to create a perfect market size estimate.

Managed Services Traction

Today, CompTIA's *Trends in Managed Services Operations* study finds that half of all channel firms report providing managed services either as part of their total business portfolio or exclusively, which is up from 4 in 10 that reported doing so in 2011. Just slightly more than half have been in the managed services business for five or more years. And of those involved in managed services, the prevailing business types are evenly split from traditional resellers/solution provider firms to IT services companies that typically perform break/fix and warranty services to companies that identify primarily as offering software development services.

Much of the switch to managed services is running hand in hand with a general wave of business transformation happening within the IT industry and particularly among channel companies that are fighting margin erosion and commoditization across many of their legacy product portfolios and looking for new ways to generate revenue, attract and retain customers and otherwise compete in what is a quickly changing IT landscape.

Business Transformation Spectrum: Where Do Channel Firms Sit?

24% **High degree of transformation** (revenue/product mix much different than two years ago)

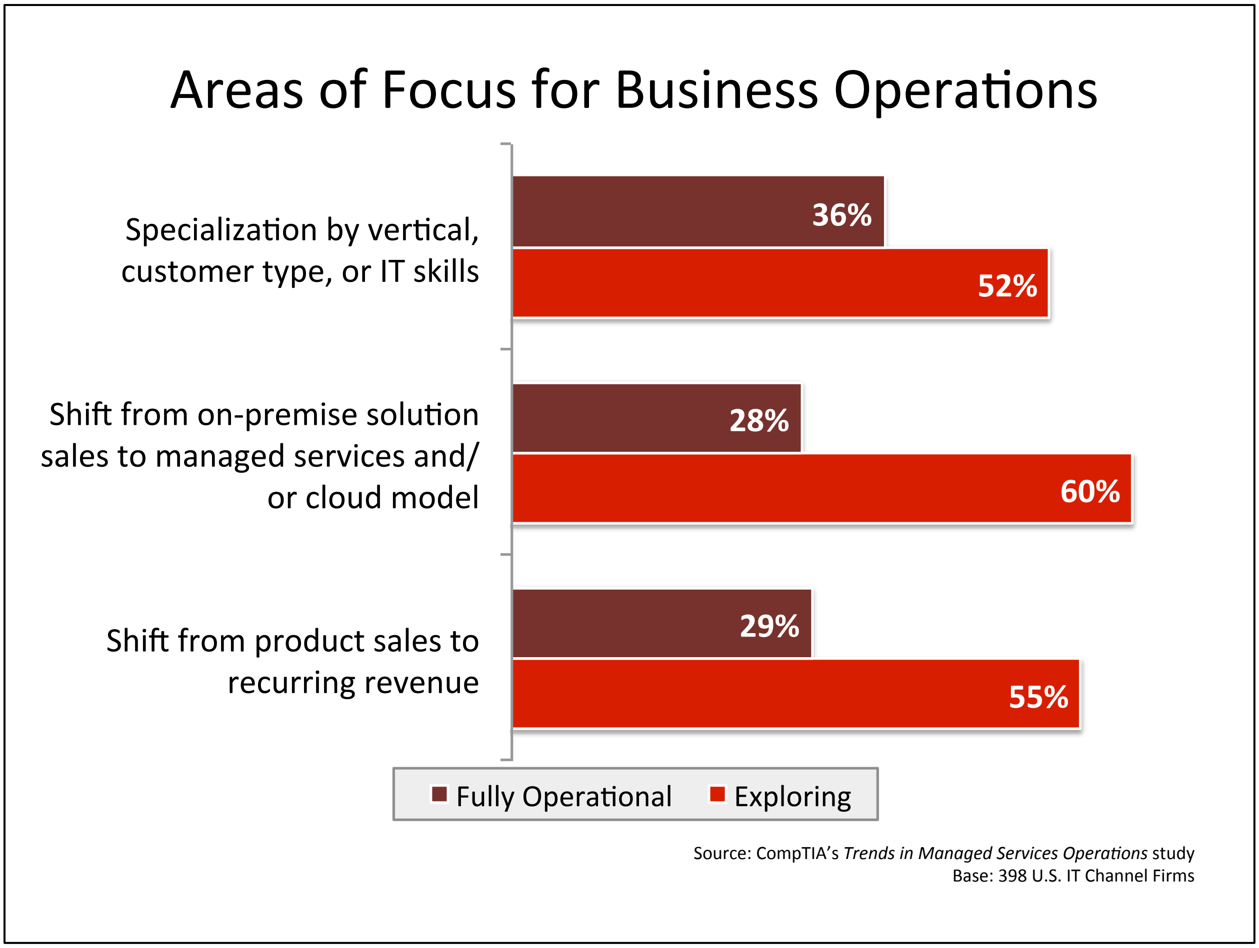
59% **Moderate degree of transformation** (revenue/product mix has changed, but traditional sources of revenue still dominate)

17% **Low degree of transformation** (revenue/product mix has been mostly stable, unchanged)

As found in data throughout all four sections of this report, channel firms characterized by a high degree of business transformation over the past two years are more likely to have committed in depth to managed services or some other new business model. Typically these are the largest companies in terms of overall revenue in the current U.S. channel. Nearly half of firms with $50M or above in annual revenue identified themselves as undergoing high levels of business transformation. That compares to 3 in 10 channel firms with between $5M-$49.9M in annual sales and just 14% of the smallest companies (less than $5M in revenue) that reported being fairly progressed with some form of business model transition.

What types of transformation are taking place? The pursuit of recurring revenue is clearly a priority when making a business change, but other areas such as specialization also loom large on the radar of many firms. Specialization can take the form of several things, from focusing your business skills and offerings on a particular vertical industry or customer segment, such as SMB, to developing a set of solutions tuned to a specific technology genre or subset – often this involves acumen in complex or sophisticated technologies such as unified communications or business analytics. More than a third of companies are operational in some form of a specialization, based on the CompTIA study, while a full half are exploring this route. Specialization can be a significant differentiator for channel companies looking to sell on value beyond their knowledge of product speeds and feeds and vendor brand. And yet, the entry-level cost to train and certify in specific areas can be prohibitive for firms that are still struggling to emerge from the economic doldrums of recent years.

Those making a move to a recurring revenue model include companies adding a managed services component to their business and/or those that might be incorporating cloud options to their current on-premises approach to implementing technology for customers. A full half of the largest channel firms report being fully operational in their transition from product sales to a recurring revenue vehicle, compared with the two-thirds of medium-sized channel companies that said they are still in the exploration phase of that journey.



What's notable is that, despite the length of time that managed services has been visible as a business model for the channel, it nonetheless remains a work in progress for a large segment of companies. Many reasons exist, including the difficulty in making a full-scale transition from a product-centric business to a recurring revenue operation; everything from financial considerations, pricing schemes, sales team acumen and compensation, marketing and technical processes require a do-over. From an investment and training standpoint, particularly in uncertain economic times, the switch can be daunting or unattainable on a wholesale level, especially for smaller channel firms.

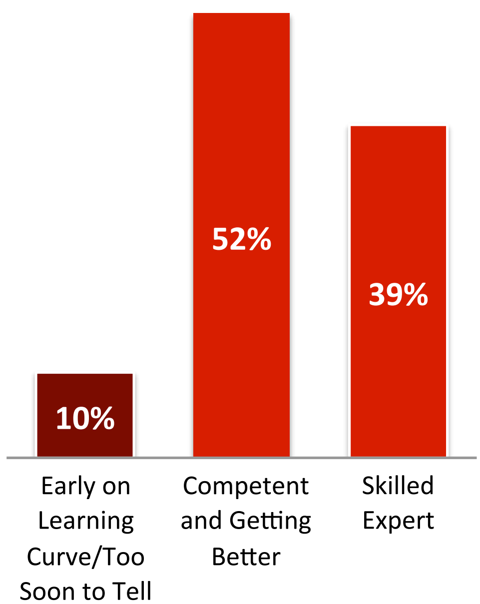
The scenario that has emerged as most viable as been that of a hybrid model, in which many conventional solution providers, resellers, and other channel companies have begun to slowly introduce some measure of managed services offerings into their portfolio, while continuing to foster their legacy streams of revenue. Many, if not most, MSPs continue to sell hardware and other infrastructure to their customers, do the implementation and only then take over management of said devices under a managed services contract.

Despite the evolving nature of managed services, most companies now doing some form of this model are relatively bullish on their competency levels. In fact, roughly 4 in 10 characterize themselves as "skilled experts" in managed services today, while just more than half claim to be "competent and getting better." Those optimistic descriptors – while noting they are self-assessed – compare with just 9% of respondents that report being early into their managed services learning curve.

Not surprisingly, when broken down by business executives versus IT executive responses, the technical staff within channel firms claimed to be skilled experts in managed services in greater numbers. Half of IT-oriented staffers believe their managed services operations to be at this high level compared with just 20% of business office executives. This likely suggests a disconnect in technical understanding levels, but also a relative closeness to the subject enjoyed by technical staff that exist in the day-to-day data center monitoring and managing of customers' technology.

Level of Expertise with Managed Services Model

Self-Assessed Characterization



"Skilled Experts" in Managed Services by Size

71% Large firms ($50M and up in revenue)

30% Medium-sized firms ($5M-$49.9M)

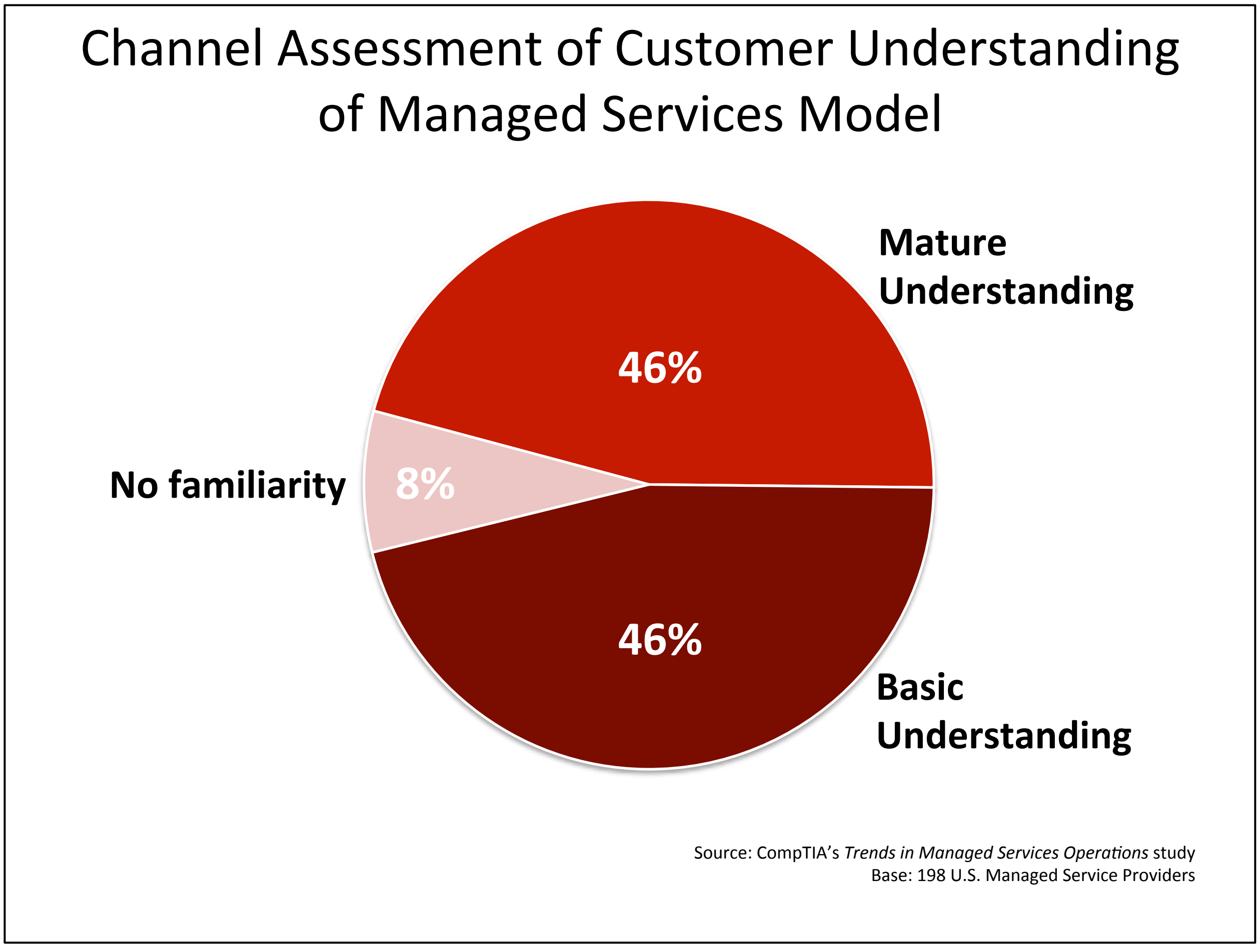
25% Small firms (Less than $5M)

Source: CompTIA's *Trends in Managed Services Operations* study
Base: 198 U.S. Managed Service Providers

The more business transformation that a firm has undergone, the more skilled they assess themselves at their managed services operations. Two thirds of companies with a high degree of operational change ranked themselves high in managed services acumen compared with just 19% of those companies that sit at the low-end of the transformation spectrum. These are unsurprising results, given that companies on the far side of a transition have been at that change for some time now in most cases; time that allows for kinks to be worked out, obstacles overcome and efficient processes to be put in place.

Equally telling, 70% of companies with high levels of business transformation describe their current customers as having a mature understanding of managed services compared with just 4 in 10 firms that have experienced less upheaval in their own businesses. One key piece of any successful business transformation is the ability to raise awareness and educate existing and new customers to the new model your company is launching. This is not always an easy task. Customers can be intransigent, sales reps inside channel firms need significant retraining on message and technique. But once accomplished, channel firms can effectively demystify new models such as managed services, raising awareness to a point where customers see the business benefits of different types of IT decisions. For example: forgoing an upgrade purchase of new servers in favor of signing a managed services contract for outsourced data center management.

The level of educating that has to go on likely depends on whom the MSP is talking to during the sales process. A CIO or other IT manager will most likely have full understanding of what managed services entails, while a CEO, CFO or other business executive's level of knowledge on the topic would be less informed.



Not in the MSP Game

Obviously not every channel firm has embraced nor plans to embrace managed services. The reasons are varied, but one factor stands out this year: The cloud. Four in 10 channel firms not involved in managed services today attributed the reason to waiting to see what the impact of cloud computing will have on the evolution and lifespan of managed services. The unknown clearly is causing some companies to take a wait-and-see approach to any transition at all. There are a number of camps when it comes to making comparisons between managed services and cloud computing business models. Are these models essentially one in the same? Complementary, but different? Directly competitive?

As stated above, the majority of MSPs today continue to sell product alongside contracts for services. Often the hardware or other infrastructure they sell into customers is then added to a managed services contract for monitoring and management on a per-user or per-device recurring fee. Channel firms building a cloud practice have in many instances eschewed hardware sales in favor of reselling applications in the cloud or infrastructure services in the cloud such as storage or disaster recovery. The cloud model is also fragmented, with many different roles emerging, from a referral-based model for the channel to aggregation, which positions the channel company as a one-stop shop for myriad services residing in different clouds.

Even vendors are still trying to figure out if their emerging cloud partner ecosystem falls into the same bucket as their managed services partners. Recently, Cisco determined that they do, merging its Managed Services Channel Program and its Cloud Provider and Cloud Services Reseller designations into a single new program called the Cloud and Managed Services Program.

Reasons Not Offering Managed Services

41%	Waiting to see impact of cloud
31%	Focusing on core competencies
25%	Unsure of the ROI
17%	Lack of in-house expertise
15%	Unsure how to get into the market
15%	Unaware/unfamiliar with what managed services entails

And yet, despite the cloud-related uncertainty, a slow start to managed services does not mean a never-start for the majority of channel firms. Nearly two-thirds said they plan to begin offering some level of managed services within the next year; just 10% acknowledged having no plans whatsoever to go down this path.

What these firms are looking for to accelerate their push into managed services spans a number of items, but notably nearly half are looking for more information about the types of vendor partner program resources available to MSPs, while another 45% are eyeing technical training and nearly 4 in 10 say they'd benefit from business training specifically geared toward best practices in managed services. Clearly, these areas of need suggest a role for the vendor and distributor communities, as well education outlets that assist in training around new business models.

CompTIA

TRENDS IN MANAGED SERVICES OPERATIONS

SECTION 2: MANAGED SERVICES: BUSINESS OPERATIONS

RESEARCH

DECEMBER 2012

Key Points

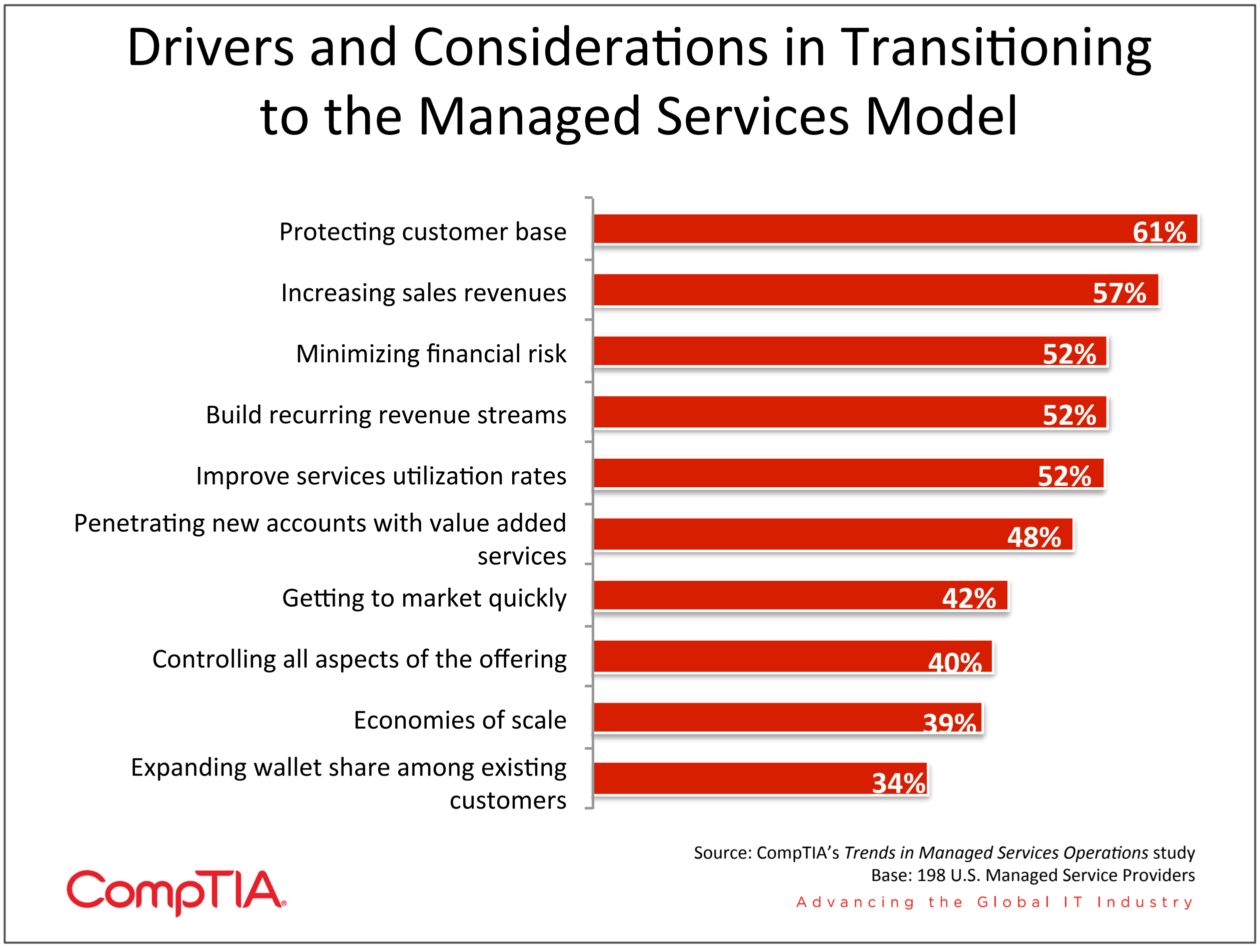
- Nearly two-thirds of channel firms cited the need to protect their customer base to merit the highest importance behind their managed services decision. Other driving factors include the desire to increase sales revenue and build recurring revenue streams.

- High on the to-do list for a managed services transition is retraining sales and technical staff, restructuring sales compensation plans and hiring new sales reps.

- Asked to rate the current operational efficiency of their managed services business, two thirds of channel firms reported that they perform efficiently in some aspects of their operation, while needing work in others. A third of companies consider themselves very efficient and a "well-oiled" machine.

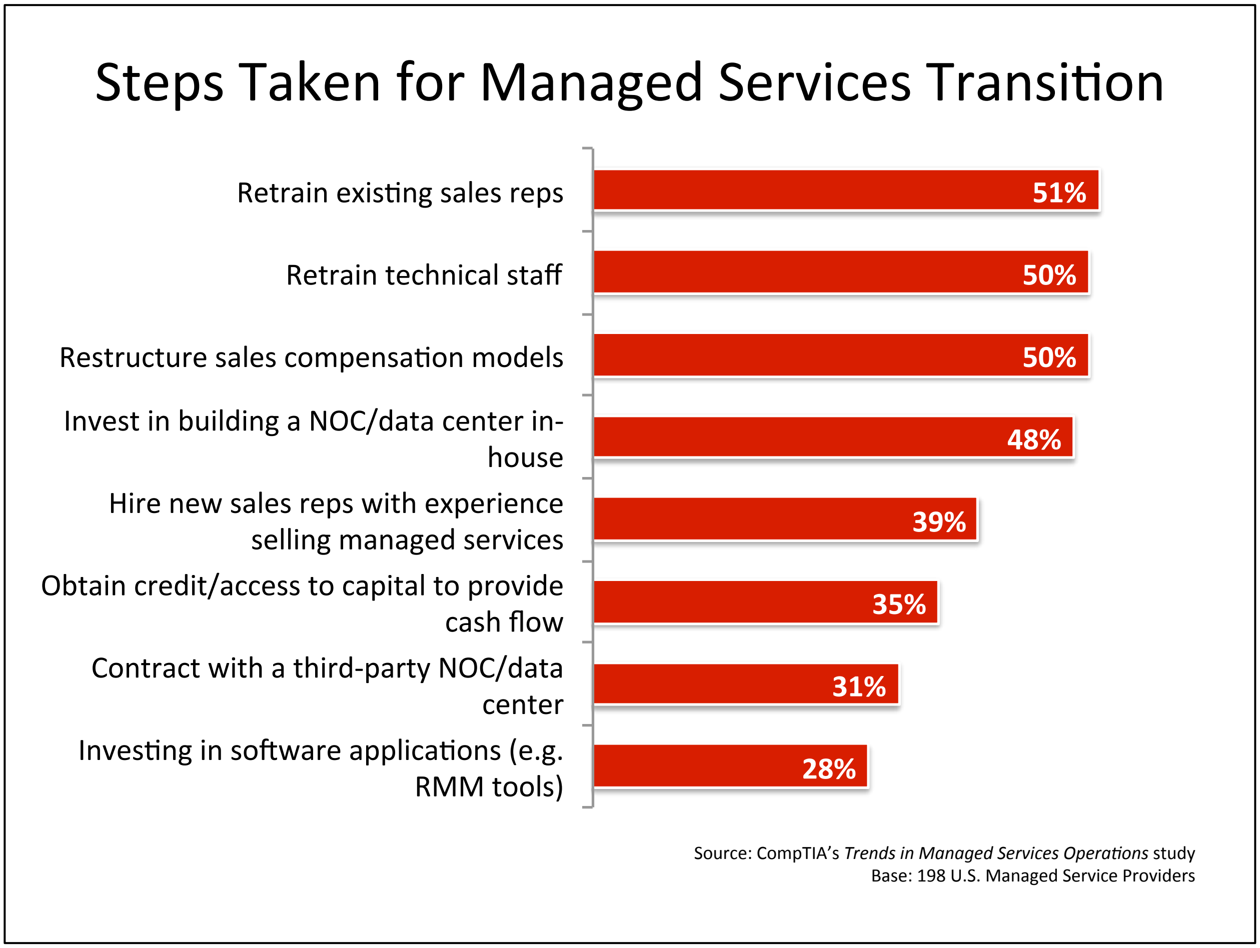
Managed Services Adoption Drivers & Priorities

While recurring revenue is most often cited as the primary reason channel firms decide to break into the managed services space, it's certainly not the only one. Confronted by cloud computing's momentum, an unpredictable economy, margin erosion and evolving customer choice, many channel companies see no choice but to transform their business into something more sustainable for the long-haul. For many, including the already up and running to those just starting out, the compass points to managed services. From a strategic perspective, the drivers for managed services are largely financial: the desire to increase sales revenue, to build recurring revenue and penetrate new accounts with value-added services. But the factors behind the shift also reflect new realities in the industry. Case in point: Nearly two-thirds of channel firms cited the need to protect their customer base to merit the highest importance behind their managed services decision. These companies are recognizing the fact that end customers have more leverage in today's market when it comes to how they procure technology, how they pay for it, and who, if anyone, they will engage to implement and manage it.



Customers that are increasingly mobile and tech-savvy at the line of business level of employee have more choice today than ever in how they buy and deploy technology, including the very real option to access the cloud directly for a raft of applications and infrastructure services. They also want flexibility in payment options, preferring in many instances to pay as they would for a utility – monthly, based on usage or flat fee, for example. Channel firms are recognizing the need to adapt to new customer realities; with managed services they can maintain the "trusted advisor" level relationship they have built with current customers, while meeting some of their newer demands. Across the board, channel firms of all types -- small MSPs to large MSPs and both firms with low and high degrees of business transformation – ranked the need to lock in existing customers as a major objective of their managed services offerings.

Once high-level objectives and goals are established, most companies need to think about next steps involved in establishing managed services as part or all of their portfolio. Littering the top of the to-do list are a series of actions involving sales operations, including retraining sales reps and restructuring the sales compensation model. These are non-trivial endeavors; by its nature, managed services requires a very different type of sales conversation and style than the one used successfully to close transactional product or project deals. The sales cycle is typically longer, involves selling an intangible product – remote, third-party services – and is typically rolled out as a long-term contract. Sales reps skilled at the landing the largesse of a one-off product win don't always carry transferable skills to the managed services arena. Reflecting this reality, 4 in 10 channel firms said that one of their initial transition steps in adding managed services was hiring new sales reps, presumably with the skills required for the model.



Likewise, sales compensation structures for the transactional world aren't readily transferable to the managed services model. Many channel firm CEOs are grappling with the best and most fair ways to structure these compensation agreements so that they are able to manage cash flow reasonably while also keeping sales reps content with the new system. It's a dicey challenge. Sales reps selling products are used to a percentage commission on total sale, which works out well if the customer is buying, for example, a large-scale server farm infrastructure upgrade. But customers in a managed services engagement typically pay a fee per month based on a flat rate or some other metric such as usage or per device. Apply the same commission percentage to the monthly fee and the sales rep's portion turns out to be fairly small in terms of dollars and cents. Over the course of a year, it might add up to the same amount as a one-time transaction payout, but reps are often impatient with small checks coming in each month. As a result, various compensation plans have emerged to address managed services, though as yet, no best-practice standard exists. Some companies pay sales reps upfront on the first year of a customer contract; others pay quarterly. It varies.

Beyond sales, channel firms pinned their attention on investments in network operation centers (NOC) to be the command and control point for managed services operations. Companies that have experienced a high degree of business transformation placed particular emphasis on NOC investment, either by building one of their own (64% of respondents) or contracting with a third party to host data center operations (half of respondents). Conversely, lowest on the action items for firms at all points in transformation, size and business type was investing in software to help run their managed services operations such as remote management & monitoring tools or professional services automation packages. Fewer than 30% undertook such a purchase initially, which suggests that the need for formalized software is either not apparent or the cost of these applications is prohibitive.

Assessing Operational Efficiency

The other major force behind the shift to managed services is the desire to wring more out of daily business operations. Similar to addressing the buzz about business transformation, channel firms can't ignore the siren call for improved operational efficiency – both within their legacy lines of business as well as across new ventures and processes being put into place. CompTIA has published a number of studies and white papers that address the issue of operational efficiency challenges for both managed services-oriented firms as well as traditional solution providers. Please see comptia.org and the research section of the Member Resource Center for these detailed documents.

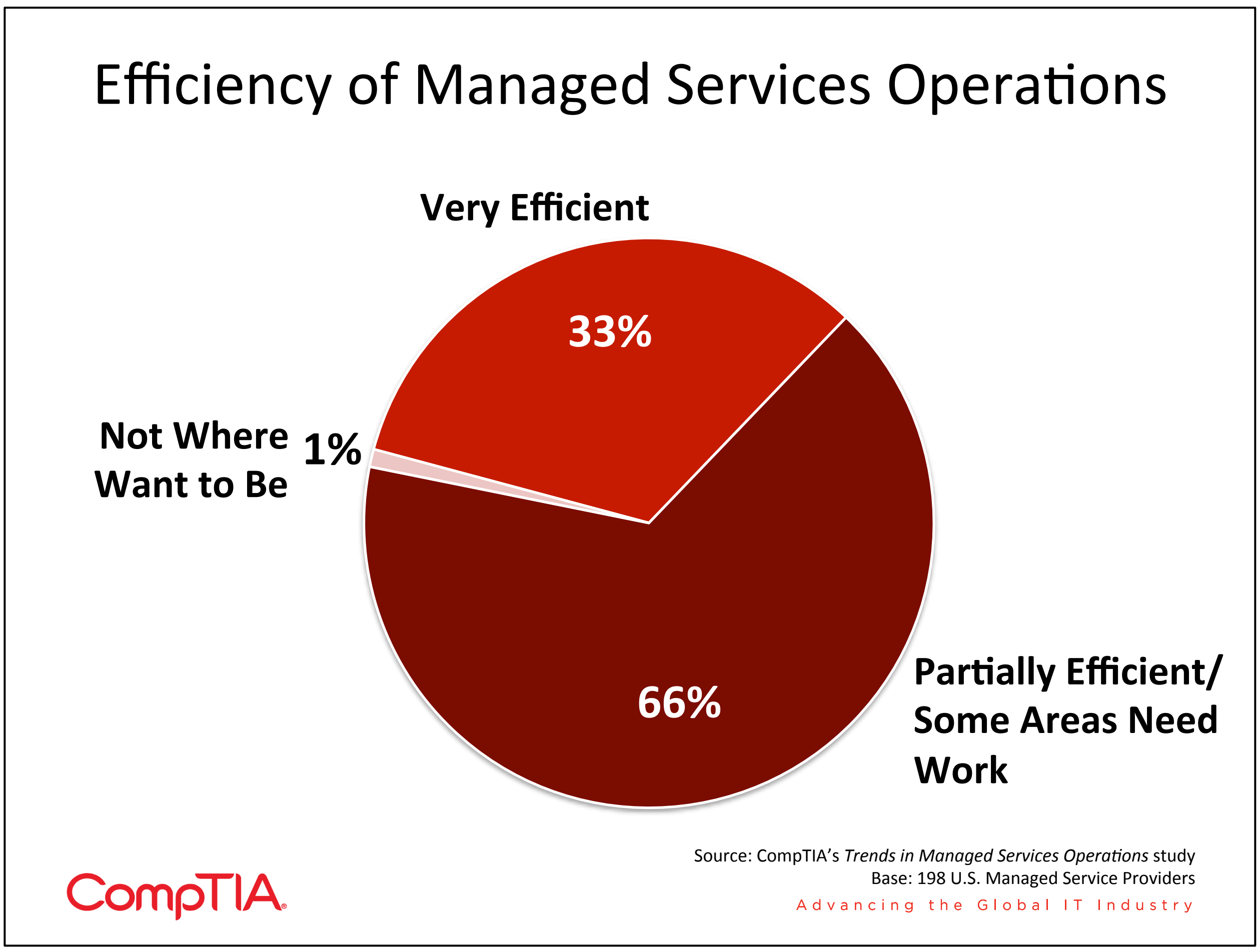
For MSPs, attaining optimal operational efficiency is a tricky challenge, in large part because the model represents a very different set of metrics, processes and priorities than a transactional product- or project-based business. Asked to rate the current operational efficiency of their managed services business, two thirds of channel firms landed squarely middle of the road, reporting that they perform efficiently in some aspects of their operation, while needing work in others. A third of companies consider themselves very efficient and a "well-oiled" machine.

Not surprisingly, those most likely to give their operations the highest marks were firms that have undergone the highest degree of business transformation in the last two years – in other words, they've been tinkering with things longer and more intensely than many of their counterparts. Half of this group rated themselves as very efficient versus 29%, respectively, of firms experiencing both medium- and low-degrees of business transformation.

Meantime, the smallest MSPs overwhelmingly rated their operational efficiency as mixed. Eight in 10 said they perform well in some areas of managed services, while needing work in others. Perhaps hedging their bets a bit, just 18% of firms with less than $5M in revenue consider themselves to be very efficient today, compared with 38% of medium-sized MSPs and 45% of large firms. A number of reasons could account for this less-than-optimistic – or perhaps, realistic – self-assessment. For smaller firms, the likelihood of already having a fully operational NOC from which to remotely monitor and manage a customer's environment is less common than among larger firms. This means a capital outlay to buy data center infrastructure, which is prohibitive for many small firms, or contracting with a third party for hosted data center capacity. Navigating these decisions could delay reaching the type of efficiencies enjoyed by a company that already has the infrastructure in place to roll out managed services.

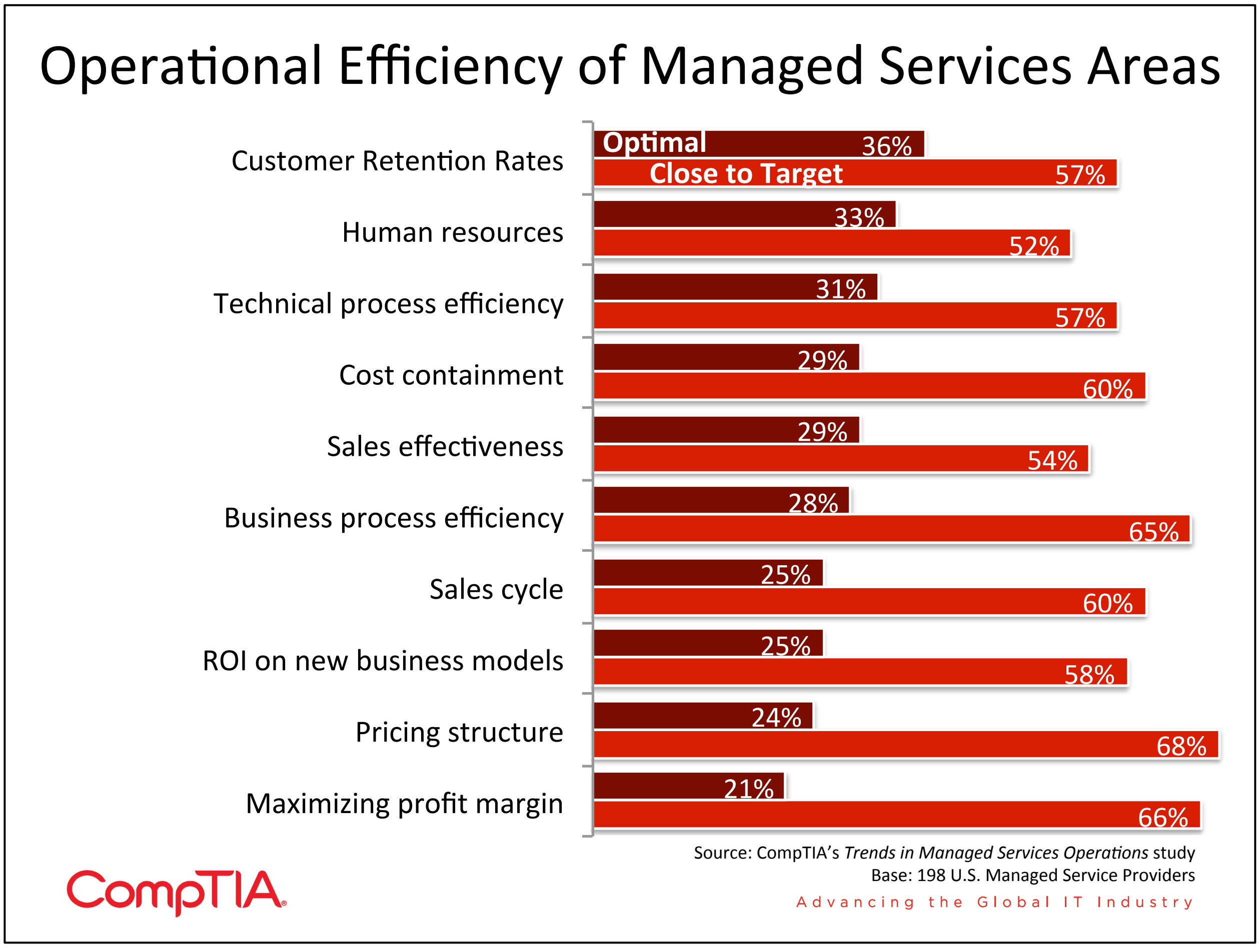
On a similar note, smaller MSPs were far less inclined than their larger counterparts to have deployed commercial software such as remote monitoring & management (RMM) tools or professional services automation (PSA) packages from companies such as Connectwise, Autotask or Level Platforms. These packages can be expensive for companies with a smaller budget, but undeniably they do assist in streamlining many of today's managed services functions when used.

Business managers were less optimistic about the level of operational efficiency their managed services line had achieved than their counterpart managers on the IT side of the house. Twice as many (4 in 10) IT managers rated their state of efficiency as well-oiled versus just 2 in 10 business managers that said the same. Perhaps this reflects the proximity the IT-related employees have to the daily operations and functions taking place as part of their managed services operations; likewise, the disparity could suggest a likelihood for business executives to impress a continual need for improvement.



The umbrella term operational efficiency obviously breaks down more granularly when applied to individual functions within an organization. In general, most channel firms appear to be on a similar track with respect to specific functions and their degree of attained efficiency, with roughly a quarter to a third believing they are on target with such things as maximizing profit margin, cost containment, technical and business process efficiency and customer retention.

But certain areas stick out as less far along and not surprisingly they involve sales functions and human resource areas around hiring and retention of people with the necessary skills to be successful in a managed services business model. Seventeen percent of channel firms cited sales effectiveness as an area they are not on target for efficiency; similarly, 15% cited inefficient sales cycle performance and HR functions. These "people" issues were shared across MSPs of all sizes.



Profit margin maximization is always a litmus test for operational efficiency. Two thirds of channel firms believe they are close to their target goals in this area, with another 21% reportedly right on target. But drilling down into certain data segments reveals some differences in how profit margin maximization is perceived by different parties. For example, among business executives, this category was pronounced not on target by 18% of respondents, perhaps yet another indication of this group's tendency to focus on continual improvement and resetting of the standards bar.

As would be expected in this uncertain economy, profit margins in general were somewhat volatile across various business models, including managed services. Three in 10 channel firms reported an increase in profit margins across all lines of their business in the past year, while 14% experienced erosion throughout. A quarter saw a decline in margin for product- and project-based business, but an uptick for managed services, while 19% saw the exact opposite trajectory.

One of the more notable pieces of profit margin data involves firms that report having experienced a high degree of business transformation in the last two years. Of those firms, 30% said that profit margins had dropped across all lines of their business. This level of erosion suggests a couple of chicken and egg scenarios: It might be the case that significant business transformation imposes initial tumult (margin loss) on a company. Or it may be that companies in the most trouble already margin-wise are more likely to embark on serious transformation of their business. Firms attempting to maintain a legacy stream of revenue while simultaneously introducing new business models such as managed services might bleed temporarily until operations are more mature and stabilized. Lesson to be learned? Companies in middle of a transformation need to be capitalized well enough to weather the initial inefficiencies that will sap profit margin.

Managed Services Offerings

The palette of offerings that MSPs are providing today is growing more and more varied, branching out beyond low-hanging fruit such as network monitoring and management to email services such as Microsoft Hosted Exchange. Increasingly, MSPs are looking to move up the food chain to offer services in the applications space – either custom application development or the management of mission-critical software services such as CRM, ERP or business analytics.

	Currently offer		Plan to offer in next year	
Type of service	Small MSPs	Large MSPs	Small MSPs	Large MSPs
Network management	52%	78%	21%	12%
Security management	58%	73%	22%	10%
Server management	59%	83%	23%	9%
Software/patching	52%	71%	27%	20%
Storage management	58%	67%	31%	22%
Desktop management	61%	61%	13%	24%
Email	55%	67%	26%	18%
Help desk	60%	71%	19%	16%
Database management	66%	88%	22%	6%
Custom app dev	52%	73%	29%	16%
Application management	63%	82%	25%	10%
Business continuity/DR	52%	59%	25%	33%
Managed print	42%	49%	28%	35%
Mobile device management	39%	43%	36%	39%

In the coming year, channel firms expect to broaden the menu of offerings even more. Nearly half said they intend to increase the number and type of managed services offerings they have in their portfolio; 17% expect to increase in some areas, while decreasing in others; another 36% expect to hold steady with what they are currently offering. Firms with the highest degree of business transformation plan to be the most aggressive in their pursuit of diversity; 62% plan to increase offerings across the board.

TRENDS IN MANAGED SERVICES OPERATIONS

SECTION 3: MANAGED SERVICES: SOFTWARE TOOLS

RESEARCH

DECEMBER 2012

www.comptia.org

Key Points

- Half of channel firms offering managed services today report using commercial RMM and/or commercial PSA software. More than half (56%) use systems management software – typically these are vendor-based applications that companies of all types use to monitor their own networks internally. Roughly 4 in 10 firms are using their vendor partner's MSP-provided tools or relying on homegrown systems.

- The No. 1 business function priority MSPs look for in software is a tool or platform that manages efficient problem resolution for customer's IT issues. Nearly two-thirds of firms value this essential function, which lies at the heart of an MSP's credibility to assume responsibility for remotely managing an end user's IT environment. Other function areas of importance are customer billing capabilities and trouble ticketing.

- Nearly 7 in 10 MSPs look for security and risk mitigation capabilities in choosing a commercial RMM or PSA software package for their firms.

Managed Services – Under the Covers

A hallmark of any successful managed services practice is a foundation of automation and process efficiency. Without streamlined processes in place that are repeatable across all new and existing customers, the managed services model doesn't hold up well cost-wise. It might seem counterintuitive to a typical solution provider, but the less "hands-on" time an MSP spends with any individual customer's technology in fact translates into more profit in their wallets.

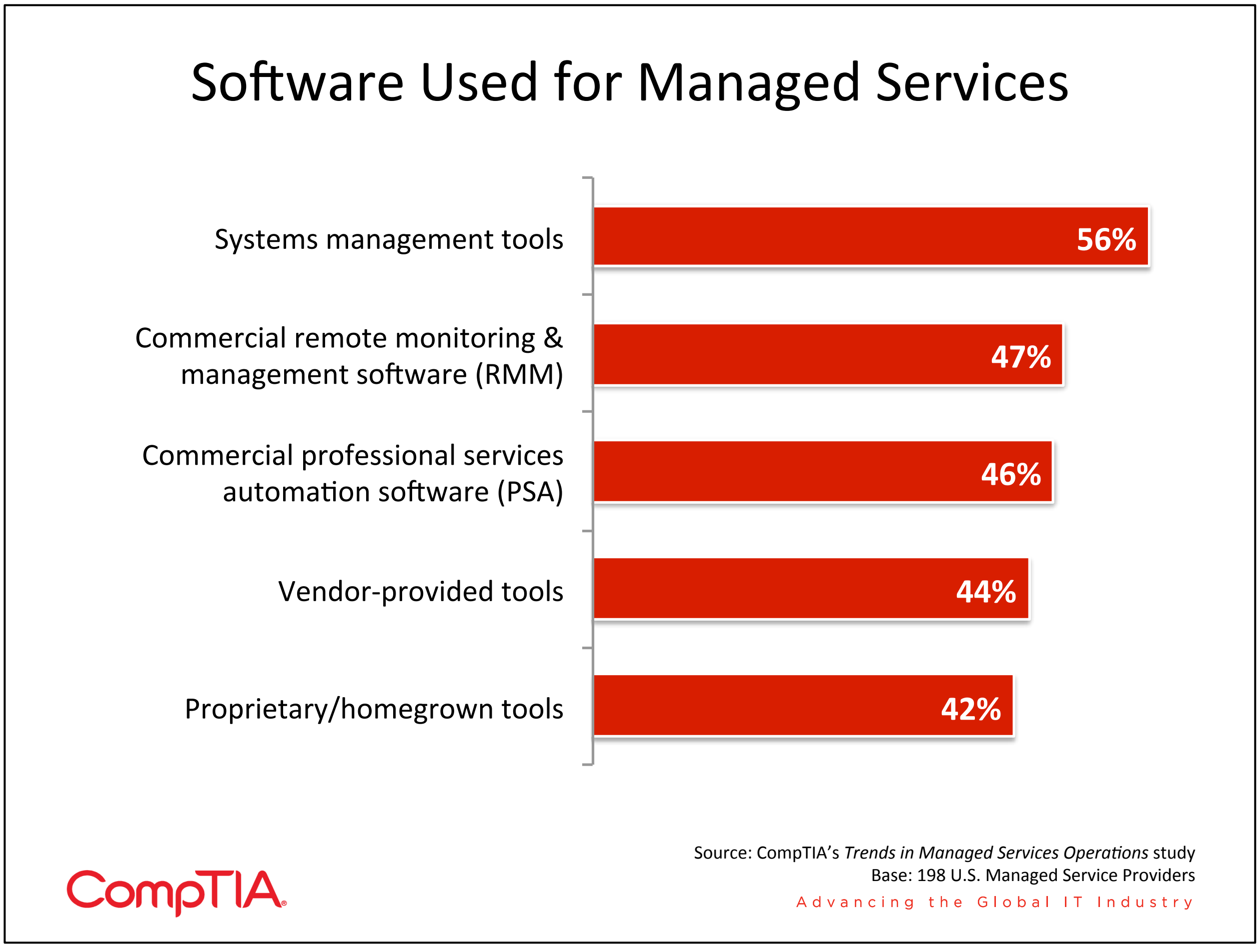
Consider the following: Conventional channel firms that focus on product- and project-oriented transactions and deal in break/fix engagements typically bill based on the number of hours worked on site, in addition to the cost of the hardware or software they are selling. It makes perfect sense that they want to maximize their time – professionally, as necessary -- working on an individual customer's IT issues in order to bolster consulting- and break/fix-related earnings. With managed services, however, this model gets turned on its head. In a managed services scenario, the recurring revenue model is usually set up so that customers pay a flat fee for services delivered on a monthly basis, much like a utility company does for electricity, for example. There are variations to how this pricing scenario works – per device, per user, per usage – but essentially you are talking about relatively predictable accounts receivables each month.

Bottom line? Most MSPs receive a set payment per customer each month regardless of whether that MSP's technical staff spent 40 hours or 40 minutes troubleshooting, optimizing or otherwise managing events going on with the customer's IT environment. All things considered, it behooves the MSP to automate as many of the technical monitoring and management processes that they can in order to keep human intervention on basic tasks to a minimum, thereby containing costs as well as expanding capacity to handle larger volumes of customers.

There are a number of tools that can assist in this type of process automation; software that effectively allows for the "managing" of a managed services business, both to address customer's IT needs and also handle an MSP's internal operations such as billing, CRM, accounting. This section of the report focuses on the software choices that MSPs are making to help run their business.

CompTIA's *Trends in Managed Services Operations* study found that today's MSPs are employing a host of different software tools, including commercial packages as well as proprietary tools that some MSPs build in-house. Commercial remote monitoring & management (RMM) tools and professional services automation (PSA) software from the likes of vendors such as Connectwise, Autotask, Level Platforms, N-Able and others have grown steadily in popularity among MSPs over the past five years in particular. Both categories of software have seen market gains, especially among large-sized MSPs.

Half of channel firms offering managed services to one degree or another report using commercial RMM and/or commercial PSA software. More than half (56%) use systems management software – typically these are vendor-based applications that companies of all types use to monitor their own networks internally. Roughly 4 in 10 firms are using their vendor partner's MSP-provided tools or relying on homegrown systems. Channel firms that have experienced a high degree of general business transformation over the past two years were more likely to have invested in a commercial RMM or PSA package – about 6 in 10 of them did – compared to less transformative organizations, but they too continue to avail themselves of other types of tools that don't necessarily fall into the popular packages from vendors cited above. More than half, for example, blended their commercial packages with proprietary tools they had also developed.



Integration is critical to the successful rollout of managed services-specific software. The various MSP-related tools must tie together along with legacy systems inside the MSP's organization such as accounting or CRM. Integration, however, is just one area of consideration when making a software-buying decision as it turns out. The data find that MSPs are evaluating software tools across two specific categories: Technical feature priorities and business function priorities.

Business functions priorities are the demand drivers behind the implementation of software tools to run the MSP operation. Broken down, these functions more or less define the key services that are part of the value that an MSP brings to the table over and above the technical capabilities such as storage or email or disaster recovery that they provide customers as part of the managed services contract.

The No. 1 business function priority MSPs look for in software is a tool or platform that manages efficient problem resolution for customer's IT issues. Nearly two-thirds of firms value this essential function, which lies at the heart of an MSP's credibility to assume responsibility for remotely managing an end user's IT environment. If storage capacity is running dangerously low, proper software tools via a system of agents and alert mechanism trigger an automated response to add capacity, for example. Any delay in this response – or non-recognition of it – could result in lost data and/or lost dollars to the end user business, which will likely break the terms of the MSP's service level agreement.

Other functional areas that more than half of MSPs seek to address through software is the management of customer billing and payments and the effective handling of trouble tickets and help desk requests. The latter situation often involves IT needs that go beyond the capacity of automated remedy and instead require manual intervention by someone on the MSP's technical team.

More than half of respondents value software that enables them to generate customer-facing reports on corrective and other actions they have taken over the course of a month or a quarter. This is a critical function because more than other channel firms, MSPs often need to go out of their way to show their work. It's ironic, but the more competent an MSP is at serving the customer, the less visible they often become to that customer. Think about it: IT problems that are pre-empted before impacting the customer go sight unseen, so it's important for MSPs to regularly update and remind their clients of the services they are providing and any disasters that have been averted, be they security threats or insufficient Web site capacity during peak usage. Routine reporting and communication on actions taken establishes a history and visibility with customers that can be invaluable when it comes time to renew the managed services contract. Many of today's PSA and RMM packages include this function.

Importance of Software Functionality

Software Function	% of Companies Viewing as Important
Managing efficient problem resolution	62%
Managing customer billing/payments	58%
Generating reports on IT actions/corrective steps taken	55%
Managing customer trouble tickets	54%
Managing internal financial/accounting systems	52%
Managing CRM systems	51%
Managing internal sales and marketing systems	47%

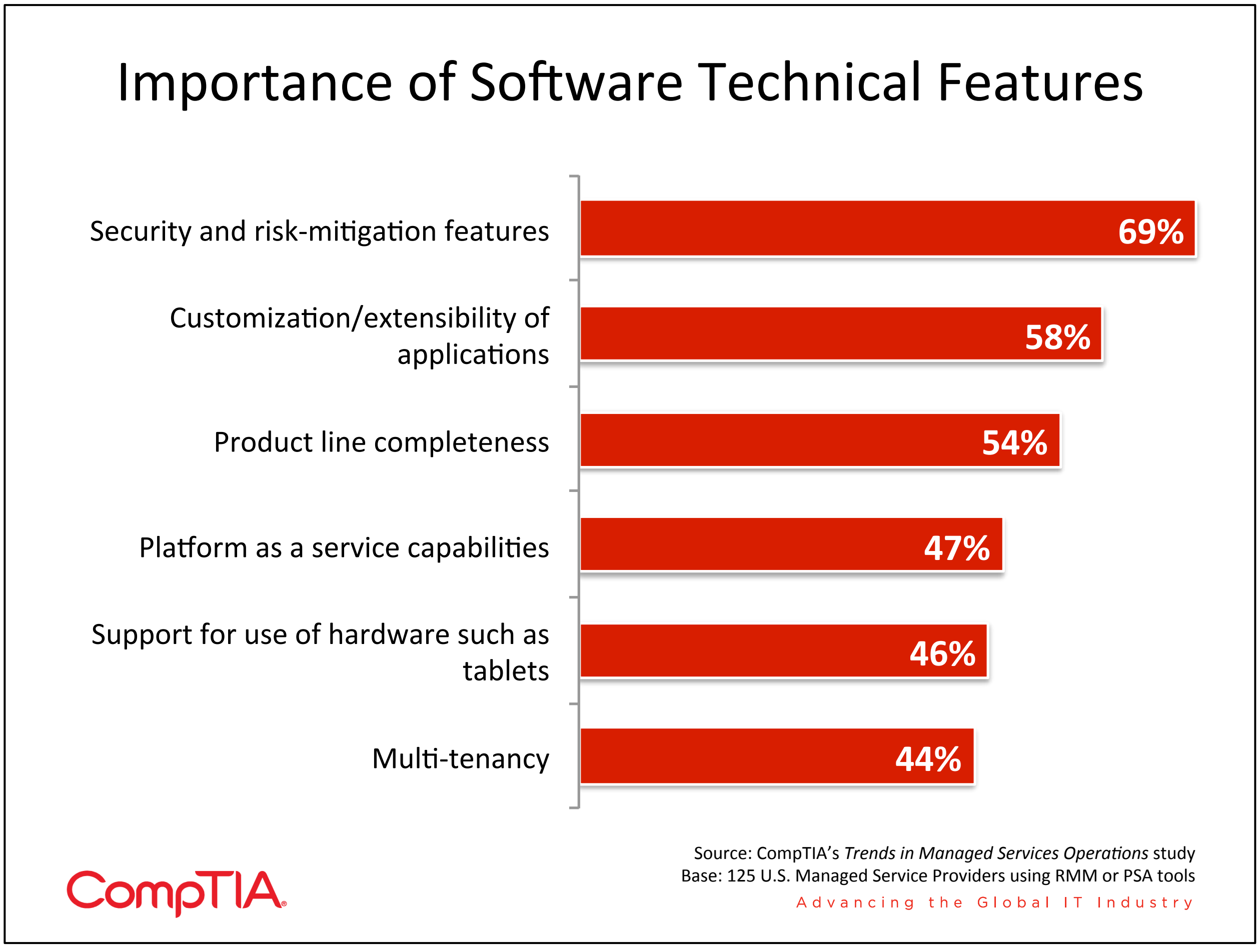
Source: CompTIA's *Trends in Managed Services Operations* study
Base: 126 U.S. Managed Service Providers using RMM or PSA tools
Advancing the Global IT Industry

While the majority of the above software functions were valued across the ecosystem of channel firms in the survey, there were some differences in priorities. For example, medium- ($5M-$49.9M in revenue) and large-sized ($50M+) MSPs placed nearly double the premium on software that manages their CRM systems and generates reports on corrective actions than the smallest MSPs. One possible explanation is that larger MSPs are dealing with higher volumes of customers, therefore software to help automate and manage those relationships more easily – CRM capabilities – is crucial to efficiency.

Likewise, a higher volume of customers raises some challenges for effective communication; automated report generation keeps track of the history of actions across all customers in a more manageable way.

Technical Must-Have Features

The other evaluation measure MSPs use in determining what software tools to use involves technical capabilities. First off, software needs to include robust security and risk-mitigation features. Customers can be skittish to outsource their IT functions – especially mission critical applications and data – to a third party. The security discussion is almost a given in any sales conversation. Software in place that backs up a service level agreement and allays security concerns is a plus for many channel firms considering or doing managed services.



Meanwhile, an MSP's ability to customize and extend a software platform is highly prized. As discussed previously, RMM and PSA software, whether commercial packages or homegrown, need to be attached to any number of other pieces of software – both within the MSP's environment and that of the customer. The extensibility of an application here makes the job a lot easier.

Additionally, MSPs can cement a stronger relationship with their customers if they are able to customize and individualize the tools they use that face the customer, including such things as billing, activity reports and other collateral. Software malleability is an important feature that a majority of MSPs today seek.

Underscoring the sharp momentum behind mobility in business, nearly half of MSPs said they look for software that provides support for hardware such as tablets. No longer are managed services flooding into an on-premise office only, but these services need to be available to customers who are traveling, working from home or otherwise on the move.

While half of MSPs using commercial PSA and/or RMM software said they choose to go with a single vendor's package to handle multiple functions, the other half reported combining multiple vendors best of breed products and modules.

Sources Used to Select MSP Software

53%	Recommendation of vendors/distributors
23%	Demos at trade shows
13%	Recommendation of other MSPs
10%	Reviews in trade publications

Opting Out of Commercial Software

For a variety of reasons, a percentage of MSPs do not deploy a commercial RMM or PSA package to run their business. The data suggests that the main reason to forgo a package of this nature is that some MSPs are satisfied with the job that their own proprietary system is doing. Four in 10 non-commercial software users said this was the case. Many of these are MSPs that are smaller in size, which explains why 30% of them said that their organizations were not large enough to need a commercial offering and that the packages were too expensive. Cost considerations loom for channel firms of all sizes, but for the smallest it's often prudent to wait until the need to scale up in capabilities and capacity occurs before investing in a software package that might supersede current needs.

CompTIA

TRENDS IN MANAGED SERVICES OPERATIONS

SECTION 4: MANAGED SERVICES: SALES, CUSTOMERS, PRICING

RESEARCH

DECEMBER 2012

www.comptia.org

Key Points

- The difficulty existing reps have selling managed services as opposed to products ranked as the sales challenge of greatest magnitude among channel firms, with more than a third citing it as a major factor in sales restructuring along with another 42% that said it was at least a minor factor.

- 6 in 10 channel firms selling managed services pay their sales reps a commission percentage based on the recurring payments that come in monthly from customers. Three in 10 are paying out a percentage on the total amount of the customer contract at the time the deal is closed, while a smaller group, just 13%, pay their reps a portion of the total contract amount at time of closing, then award the balance at a later time.

- Customer retention rates range, with 3 in 10 MSPs saying 60-70% of their customers renew their contract on average, while 26% claim between 71-80% renewals and 20% report it being above 80%.

Developing an Effective Sales Structure

Of all the operational changes prompted by launching a managed services business, the restructuring the sales organization is often one of the trickier for channel firms to navigate. This task can be especially challenging for conventional channel firms whose business model to date is predicated on product- and project-based transactions. Making the switch to selling long-term contracts for IT services is a major adjustment for many of today's sales reps, as is the necessary tinkering of sales compensation models and training investments that channel firm owners face.

The difficulty existing reps have selling managed services as opposed to products ranked as the sales challenge of greatest magnitude among channel firms, with more than a third citing it as a major factor in sales restructuring along with another 42% that said it was at least a minor factor. Not surprisingly, 4 in 10 resellers and IT services-based firms singled this out as a major factor among the sales challenges faced in adding managed services. These two types of businesses are historically transactional in nature, either selling product to a customer or serving in a break/fix repair role as needed. Transactional selling of a tangible product such as a rack server or an office-full of desktop PCs is much different than selling what are essentially outsourced IT services that will be billed on a recurring basis.

Chief Obstacles in Restructuring Sales Teams to Fit Managed Services Model

	Not a factor	Minor factor	Major factor
Current sales reps inability to sell services vs. products	21%	42%	36%
Cost of retraining sales reps	19%	47%	34%
Sales rep retention	25%	44%	31%
Restructuring compensation models to provide technical staff with commissions	25%	46%	29%
Inability to recruit right sales reps	28%	47%	26%
Push back about change from sales reps	31%	51%	18%

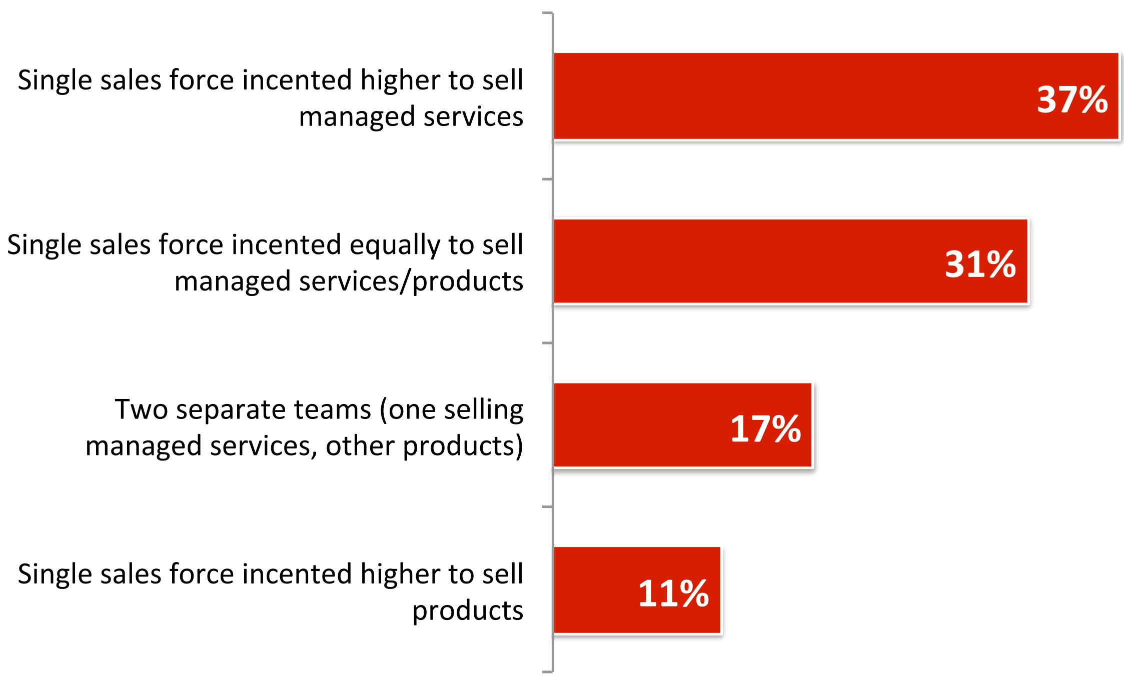
Push back from existing sales reps was most prevalent among firms having undergone a high degree of business transformation, with **40%** of those companies saying sales compensation restructuring was a major challenge.

CompTIA Advancing the Global IT Industry

In many cases, the very concept of what managed services is needs to be explained to a potential customer as pockets of very low awareness continue to exist. Then basic contractual terms must be conveyed to the customer, along with negotiating the contents of service level agreements that are critical to any managed services engagement. Customers typically need to be convinced that ironclad security exists for their data and assured of remedies they can seek if services are interrupted for reasons such as Internet downtime. Often, the sales cycle in a managed services model is longer than a transactional sale, which is another adjustment for sales reps to weather.

All of this adds up to a couple of things: For one, sales rep retraining is imperative. Necessary, and often costly, which is why channel firms ranked the investment high up on their list of challenges involved in orienting a sales force to a managed services operation. Another sobering reality is that despite retraining efforts, some sales reps simply can't make the turn, which puts the channel company owner in the position of either terminating reps or keeping them involved with the legacy piece of the business, if that continues to exist.

Current Structure of Channel Sales Organizations



Source: CompTIA's *Trends in Managed Services Operations* study
Base: 198 U.S. Managed Service Providers

Hiring and retention of effective sales reps also pose challenges for today's managed services firms. A full half of firms experiencing a high degree of business transformation in the last two years cited sales rep retention for the managed services practice to be a major hurdle. This might seem surprising given that these firms presumably have already spent significant time retraining legacy reps as they've been in the transformation game longer than many of their counterparts in the channel. And yet they struggle with retention in particular, raising the issue of whether newly trained reps are looking for opportunities to take their effective managed services skills to other employers.

Sales Compensation Models

One reason for discontent among some sales reps might have to do with compensation models, which are often more complicated than a transactional selling scenario due to the recurring revenue nature of managed services contracts. The conventional structure of paying a percentage commission on a closed product sale doesn't translate as neatly to managed services, where monthly, incremental payments from customers come in that, based on the old system, will generate a smaller commission check. It's possible that over a year's time, those smaller commissions add up to the equivalent or a single large-scale product scale, but some reps aren't able to be that patient. So channel firms have had to get creative in how they structure compensation, including in some instance paying reps a percentage upfront on the full amount of the contract or paying some portion of the total contract in commission, such as half, then conveying the balance at the time of contract renewal. Still, the possibility exists that top-notch sales reps will leave a company that has moved to managed services, seeking out a position where the compensation model is more familiar and potentially lucrative.

Today, 6 in 10 channel firms selling managed services pay their reps a commission percentage based on the recurring payments that come in either monthly or some other regular timeframe from customers. Three in 10 are paying out a percentage on the total amount of the customer contract at the time the deal is closed, a structure that requires a level of cash flow on the part of the channel business to be able to compensate reps before billing the customer. A smaller group, just 13%, pay their reps a portion of the total contract amount at time of closing, then award the balance at a later time.

In addition to compensation schemes, companies that operate in a hybrid business model also have to consider how they incent sales reps on their various business lines, from managed services sales to product sales. Nearly 4 in 10 maintain a single sales force for managed services and legacy business sales, but compensate reps higher for managed services deals, suggesting that this is the direction that these firms aim to take their company in the future.

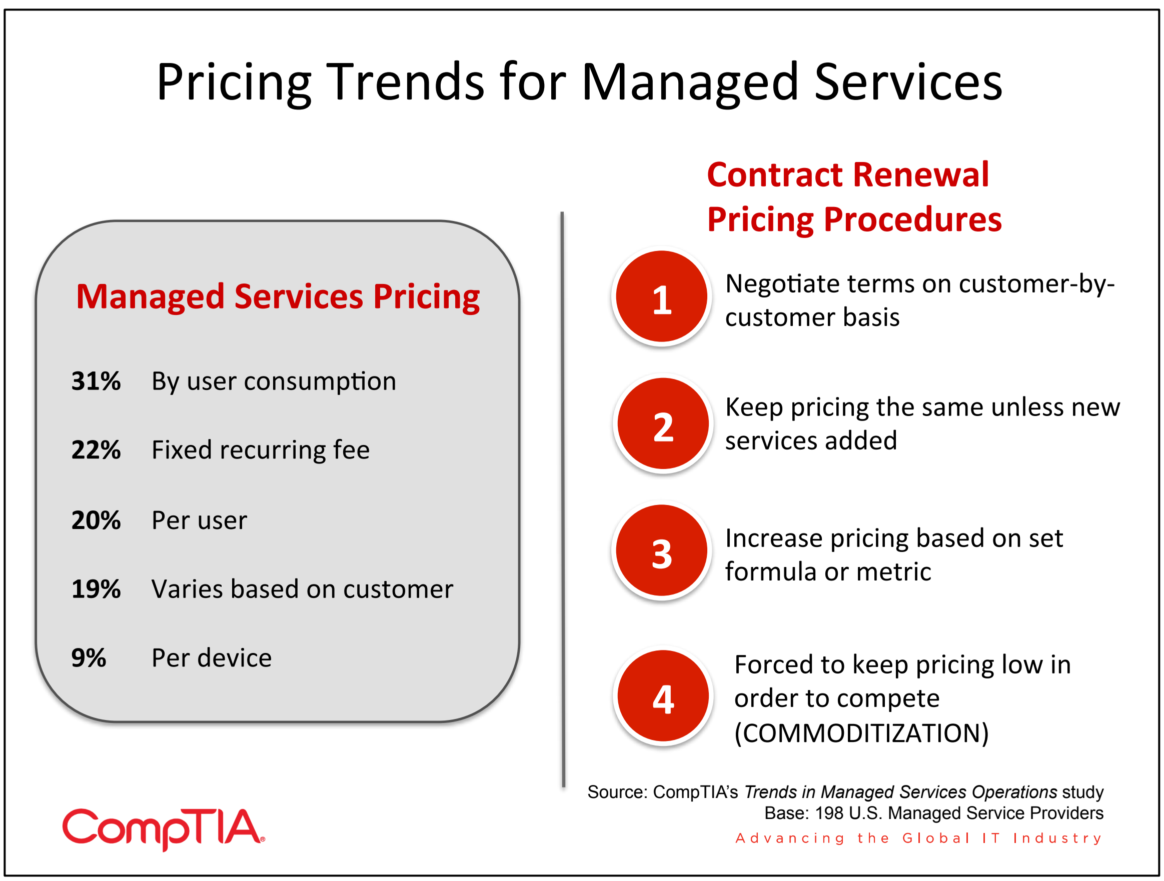
Checking the Pulse of Managed Services Sales Comp Plans

36%	Right where we want to be
53%	Lots of changes happening, but on track
11%	Not where we want to be yet

Another 31% of firms maintain a single sales force, but compensate the reps equally for product-, project- and managed services-oriented sales. A fraction, 17%, field two separate sales teams; one for product sales and one for managed services. For a large organization that has an ample number of sales reps, this approach might work best, allowing the reps to gravitate toward their areas of expertise and therefore be most effective for the company. In just 1 in 10 cases do firm incent reps more to sell products over managed services, another indicator that companies are moving in the direction of recurring revenue over more conventional channel business models.

Managed services sales go beyond the initial contract, however, and most firms institute compensation models across the various other types of value-added upselling, cross-selling and routine renewals that take place. Upselling is critical to increase margins on managed services and more than half of channel firms reward their sales reps for recognizing these opportunities to either sell additional services to customers, to add storage capacity or recommend a new application. One of the key selling points to managed services is its low-barrier to entry; customers can start small with a minor function such as remote patch management or network monitoring, then scale as their business needs grow. That's what make effective upselling such an important part of any sales reps duties. Case in point: three-quarters of channel firms having experienced a high degree of business transformation in the past two years compensate reps for upselling additional managed services beyond the initial contact signing. That compares with 48% of those with a medium degree of transformation and 38% that have not undergone much transformation at all. This suggests that companies that have made a strong foray into recurring revenue models such as managed services understand that generating healthier margins rely not only on signing the contract, but on anticipating customers' IT needs over time so that additional services can be added.

Renewals are an important part of the managed services sales organizations. For many firms, the model has been to involve the technical staff or project manager in the renewal role, allowing the sales reps in the field to focus on new business and significant upsell. Customer retention rates range, with 3 in 10 MSPs saying 60-70% of their customers renew their contract on average, while 26% claim between 71-80% renewals and 20% report it being above 80%.



www.comptia.org