



# **Outsourcing Pricing: 3 Pitfalls and 2 Unknowns Enterprises Must Know in 2022**

April 12, 2022

Live Tweeting #EGAnalyst

---

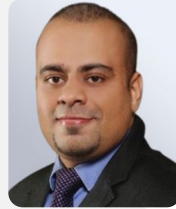
# Introductions



**Rahul Barwe**

Practice Director

[rahul.barwe@everestgrp.com](mailto:rahul.barwe@everestgrp.com)



**Achint Arora**

Vice President

[achint.arora@everestgrp.com](mailto:achint.arora@everestgrp.com)



**Rahul Gehani**

Partner

[rahul.gehani@everestgrp.com](mailto:rahul.gehani@everestgrp.com)



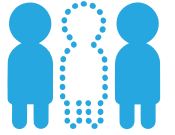
**Abhishek Sharma**

Partner

[abhishek.sharma@everestgrp.com](mailto:abhishek.sharma@everestgrp.com)

# 5 things we've learned

---



1

The talent shortage **remains** complicated



2

There is still no definitive end in sight



3

Input-based pricing models are more impacted from a cost increase perspective than output-based models



4

The number of contracts in which providers are asking for a rate hike has increased significantly over the past six months



5

The solution requires enterprises to take a surgical view, and ascertain the right increase for the right skills

# At what point in the future do you think the talent shortage will become less of a challenge? (choose one)

- It isn't much of a challenge for us now – 4%
- End of 3rd quarter of 2022 – 1%
- End of 2022 – 12%
- End of 2023 – 34%
- End of 2025 – 19%
- It will never be less challenging – 30%



# Discussion points for today

---

**Context setting on  
the past 12 months**






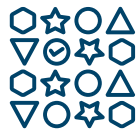




**3 pitfalls  
to avoid**

**2 unknowns  
to navigate**

**Open panel  
discussion**

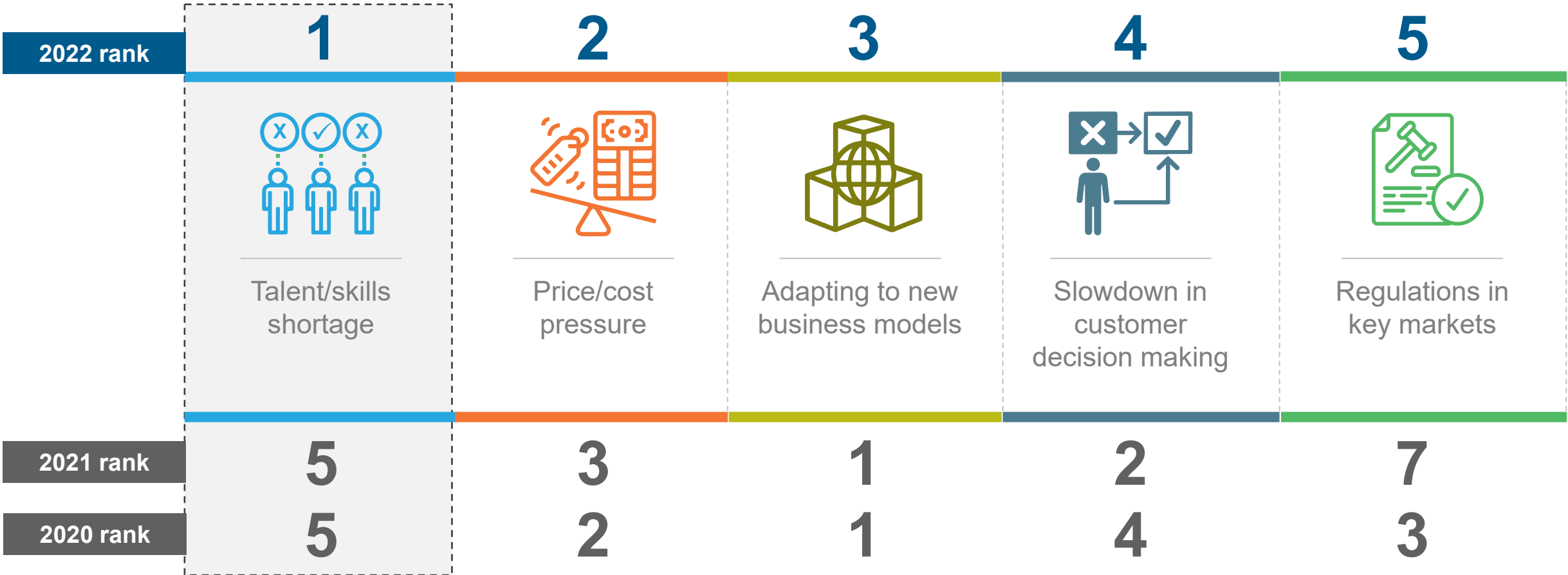


# The environment for outsourced services has taken a rapid U-turn in the last 12 months

April 2021		March 2022	
	Price contraction / rebates		Price expansion
	Demand uncertainty		Demand surge
	Portfolio consolidation		Portfolio diversification
	Employers' market		Employees' market
	Buyers' market		Sellers' market

# The talent shortage isn't going away soon

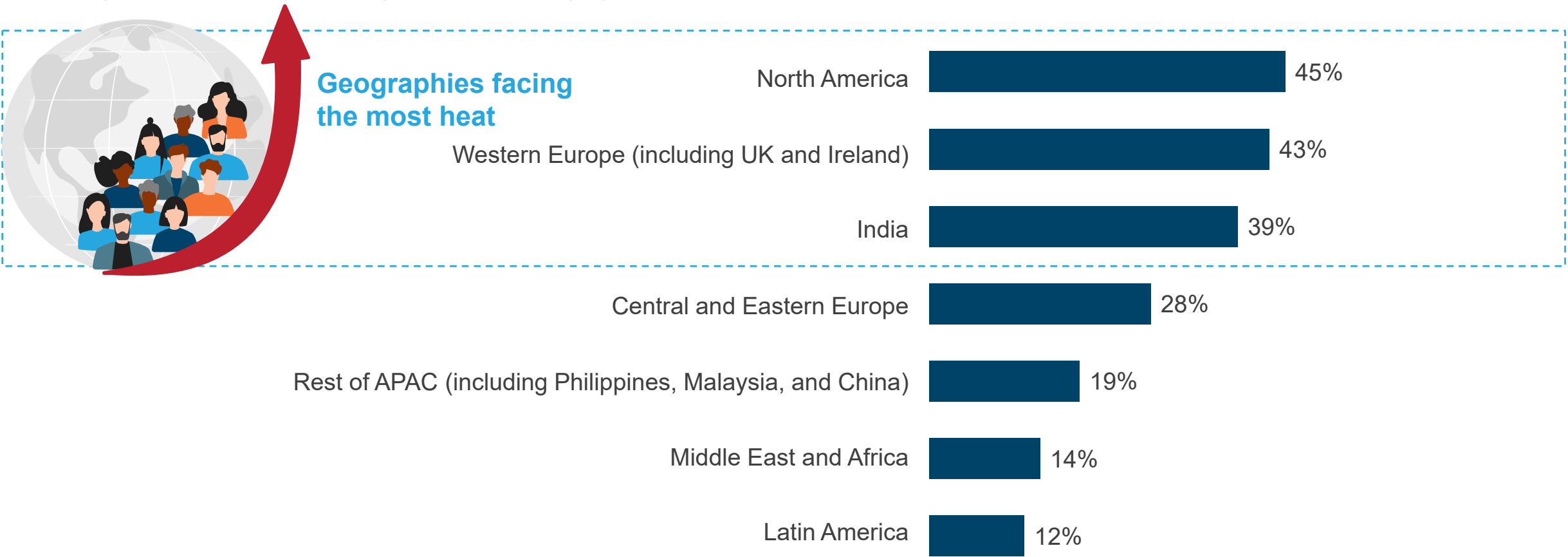
Key business challenges expected in 2022  
Percentage of respondents selecting highly challenging



Source: Everest Group 2022 Key Issues Study. Everest Group 2021 Key Issues Study and Everest Group 2020 Key Issues Study

# Offshore outsourcing is no longer an easy talent availability avenue

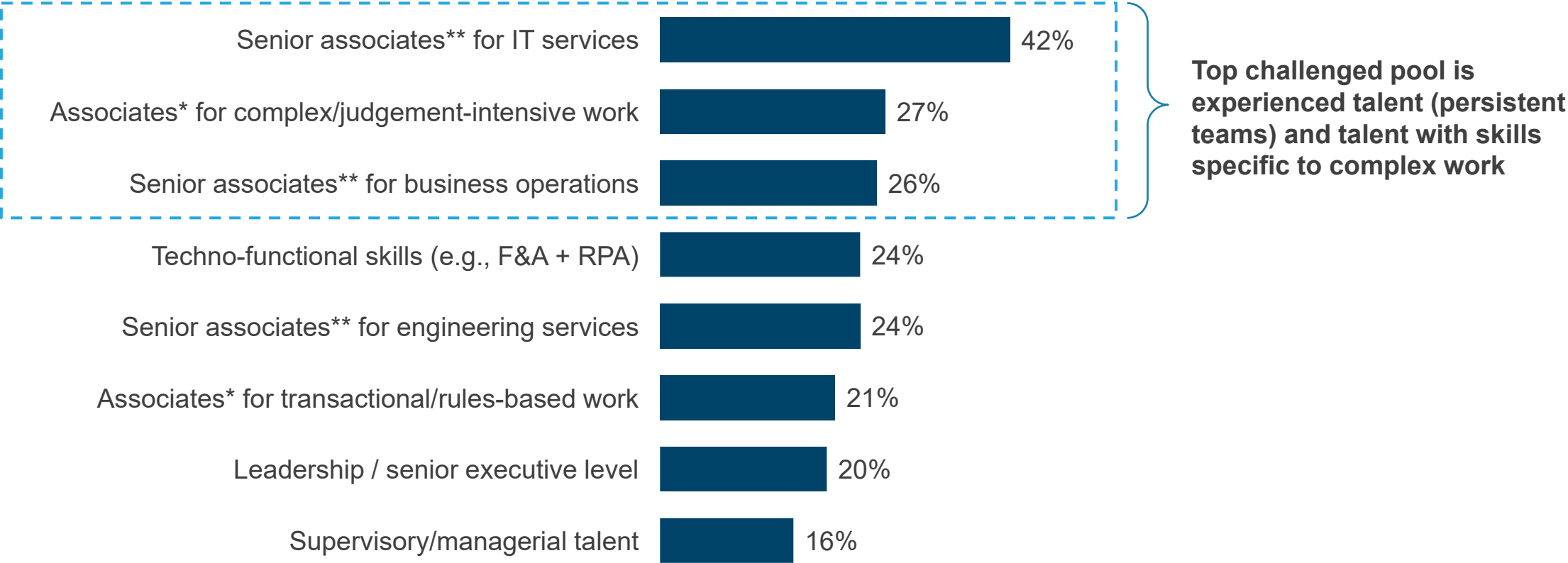
Top geographies with challenges around talent shortages  
Percentage of respondents selecting as most challenging



Source: Everest Group 2022 Key Issues Study

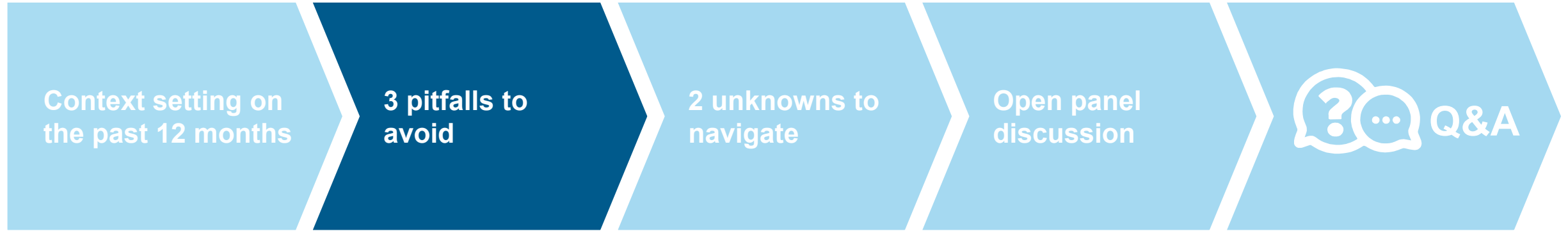
# Experience and specialized skills are the most constrained talent pools

Top segments with challenges around the talent shortage  
Percentage of respondents selecting challenging



\*Associates: <2 years of experience | \*\*Senior associates: 2-6 years of experience  
Source: Everest Group 2022 Key Issues Study

# Discussion points for today



# Pitfall #1

## Uncontrolled role inflation

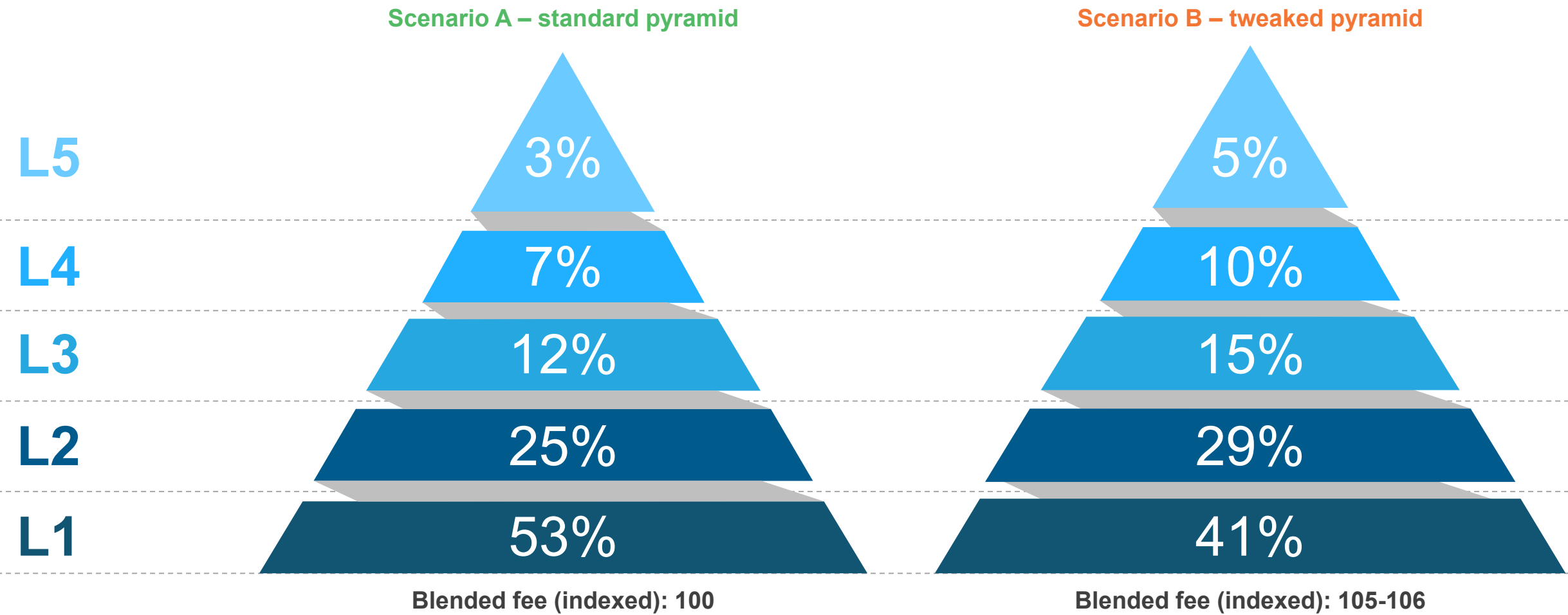
**Note:** Role inflation is when the provider slots resources into a role that is one level senior to what the role requires. For example, pushing for senior developers to fulfill requirements in which a developer is suitable.



# Role inflation is not uncommon, and up to a certain level, is expected to manage staffing and minor commercial adjustments

ILLUSTRATIVE EXAMPLE – AD OFFSHORE PYRAMID

There could be genuine reasons to staff more senior roles, but putting junior resources in a senior bracket should not become the norm



# However, to understand areas in which it should be avoided, we need to understand the efficiency-to-growth continuum of services



## Services for efficiency

Reduce costs / maximize RoI

Get the job done

Reduce risk

Uniform talent demand

Low and short-term pricing power

Procurement / CIO motion



## Services for growth

Maximize transformation value

How to compete

Enhance experience

Dynamic talent demand

High and long-term pricing power

BU heads / CEO / CDO motion

# Generally, the efficiency stack has a wider range of resources with the right skills; it is the growth stack on which enterprises need to keep a close eye

REPRESENTATIVE – FOR DISCUSSION

## Services for efficiency



### Scale-based, process-driven

- The process can make up for some extent of skill gaps
- Resources are important, but not mission-critical
- Relatively good availability of resources at the junior level
- **Low** tolerance for role inflation

## Services for growth



### Transformation-based, expertise-driven

- Success truly depends on the domain and business expertise
- Severe talent crunch, especially at senior levels
- High financial incentive for role inflation, and highest risk for enterprise too
- **Zero** tolerance for role inflation

# How do your software and platform license costs compare to the industry?

Get a complimentary license cost benchmarking diagnostic study (for enterprises only)

Everest Group's license cost benchmarking diagnostic helps enterprises quickly assess the high-level savings potential in their product portfolios

We will look into specific dimensions of your software or platform licensing contract, compare them with market norms, and assess the high-level opportunity size for you.

You can choose any one of the following products:

- Microsoft Office
- SAP
- Oracle
- Salesforce
- ServiceNow



HOW




To request your complimentary benchmarking diagnostic, indicate your interest on the post-webinar survey, or contact **Abhishek or Rahul** (email addresses on an upcoming slide)

## **Pitfall #2**

### **Continued black box pricing**








# At the outset, we can agree that the level of visibility into operational details varies by engagement model...

			
	Input-based	Output-based	Outcome-based
Key characteristics	<ul style="list-style-type: none"><li>• Customers pay for the time and resources leveraged as an <b>input</b> into the solution</li><li>• Easy to implement</li><li>• Limited innovation and value articulation possibility</li></ul>	<ul style="list-style-type: none"><li>• Customers pay for the operational <b>output</b></li><li>• Provides assurance around paying for deliverables, not time</li><li>• High dependency and low transparency by design</li></ul>	<ul style="list-style-type: none"><li>• Customers pay based on the <b>business outcome</b></li><li>• High risk, hard to implement, but immense business impact if done right</li></ul>
Typical examples	<ul style="list-style-type: none"><li>• Managed capacity</li><li>• Time &amp; material (staff augmentation / advisory roles)</li><li>• Time &amp; material (projects such as implementation or run support)</li></ul>	<ul style="list-style-type: none"><li>• Fixed price (for a particular set of volumes or defined deliverable)</li><li>• Application-based pricing</li><li>• Menu-based or package-based pricing (service catalog)</li><li>• Unit-based pricing (ticket, per story point, etc.)</li><li>• Fixed + variable hybrid</li></ul>	<ul style="list-style-type: none"><li>• (Fixed + variable) fee linked to percent of savings achieved, or other impact metrics being met<ul style="list-style-type: none"><li>– For example, fee linked to accuracy in predicting wear and tear of a part (ER&amp;D services)</li></ul></li><li>• Purely variable fee linked to percent of savings achieved, or other impact metrics being met</li></ul>
Operational visibility	High	Low to Medium	Low

# ...having said, pricing transparency can and should be achieved in every kind of engagement model

REPRESENTATIVE – FOR DISCUSSION

Our experience suggests that in most IT and BPO contracts, the level of pricing transparency available is sub-optimal!

Pricing component		Details that should be clearly available to the enterprise
Run charges		What are the units driving the fee? What part of it is at risk?
Transformation charges		What is the associated business impact commitment? What part of it is at risk if the impact is not achieved?
Tool & platform fee		What is the pricing structure for tool usage, and what does it include? What is the monthly/annual fee applicable for each specific tool?
PMO charges		What (if any) are the applicable PMO/governance charges? What value/activities are driven by these resources?
Additional/ad-hoc charges		How are any additional SMEs/ad-hoc services priced? What are applicable hourly/transaction rates?

A single black box pricing can cause major issues in assessing relative competitiveness and when adjusting fees to reflect any addition/reduction in service scope

# The innovation fund should also include detailed information around how it will be utilized to create value

## Service provider commitment to the innovation fund is critical

Service provider commitment to the innovation fund

**1-5%** of the Total Contract Value (TCV)

**Alliance with customers for co-innovation**

- Partnership-based engagement for continuous innovation
- Ideation, innovation, co-investment for transformation

**Investment in CoEs, labs, and competencies**

- Domain-focused CoEs, training and certification, etc.
- Set up typically for digital and similar next generation capabilities

**Transformation office**

- A transformation team of 5-7 resources
- Pooled for pilot projects on newer areas

## Clarity enterprises should expect

Enterprises should demand a clear articulation of how the investment will be used

### Example #1

- \$XX on \_\_\_\_\_ (tool) implementation
- \$YY on delivery model transformation
- \$ZZ on co-innovation fund
- \$PP on transition investment

### Example #2

- \$AA on implementation of next-gen tools \_\_\_\_\_, \_\_\_\_\_, \_\_\_\_\_
- Co-innovation fund equal to X% of AD revenue, managed via an innovation council

## **Pitfall #3**

**Lack of mechanisms to adjust  
pricing for inflation/market volatility**



# Having a no COLA<sup>1</sup> policy does not necessarily mean a competitive deal – it could have serious implications for cost and quality

*REPRESENTATIVE – FOR DISCUSSION*



## Commercial impact

- The service provider will have baked in the risk already, leading to a high rate to start with
- Ad-hoc rate increase requests, the size for which may be higher than what is justifiably needed
- Low levels of rate predictability, especially in the current situation when it is imperative for service providers to increase rates



## Service quality impact

- High risk of poor service quality, as the service provider may cut corners to retain margin
- Lack of (or delayed) access to resources, as the service provider may staff them elsewhere
- Less service provider interest in pursuing and growing the relationship; providers are much more aggressive today in letting go of unprofitable clients!

<sup>1</sup> Cost of Living Adjustment.

# The talent crunch and rising wages are leading to a reversal of the former trend of no COLA contracts and ad-hoc COLA waivers



## Analysis of deals in 2018-20

Function	With COLA	Without COLA
IT applications	<div><div></div><div></div><div></div><div></div><div></div><div></div><div></div><div></div></div>	<div><div></div><div></div><div></div><div></div><div></div><div></div><div></div><div></div></div>
IT infrastructure	<div><div></div><div></div><div></div><div></div><div></div><div></div><div></div><div></div></div>	<div><div></div><div></div><div></div><div></div><div></div><div></div><div></div><div></div></div>
BPO	<div><div></div><div></div><div></div><div></div><div></div><div></div><div></div><div></div></div>	<div><div></div><div></div><div></div><div></div><div></div><div></div><div></div><div></div></div>

Prevalence meter (proportion of deals) Low High

- Prior to 2017-18, deals without COLA were even less common, but their prevalence rose in 2018-20
- In deals where COLA was present, waivers/holidays were common in 2020, but service providers started pushing back in Q2 2021

# FX can be an ally too, as high inflation is often accompanied by exchange rate depreciation

Currency	September 2021 – March 2022 change
INR	▼ 4.2% against USD
MXN	▼ 5.0% against USD
PHP	▼ 5.2% against USD

The approaches enterprises use can vary depending on the specific contractual language



## Full or shared FX risk with the enterprise

- Assertively use FX rate depreciation to lower the impact of inflation-related rate adjustment
- Typically, a simple conversation as it is acting on what is already agreed in the contract



## Full FX risk with the service provider

- Negotiation lever to partially negate the size of the rate increase
- Enterprises should take into account both historical trends and future projections when negotiating

# Discussion points for today

Context setting on  
the past 12 months

3 pitfalls to  
avoid

2 unknowns to  
navigate

Open panel  
discussion



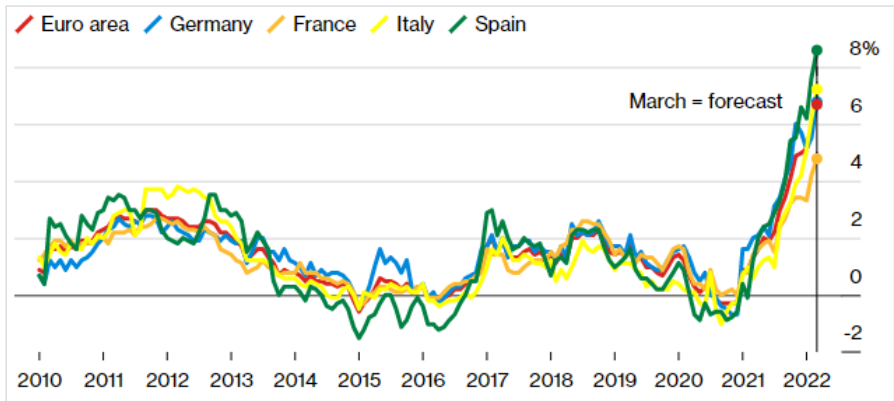
**Unknown #1**

**Sudden demand reduction,  
causing prices to drop?**



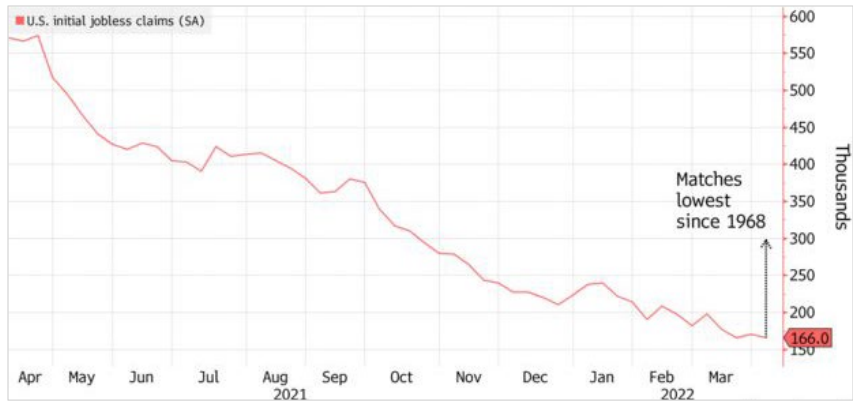
# Leading market indicators suggest probability of a global recession

**CPI:**  
Consumer prices across Europe soared in March 2022



Source: National Statistics Office, Eurostat, Bloomberg

**Initial jobless claims fell last week, matching a 54-year low**



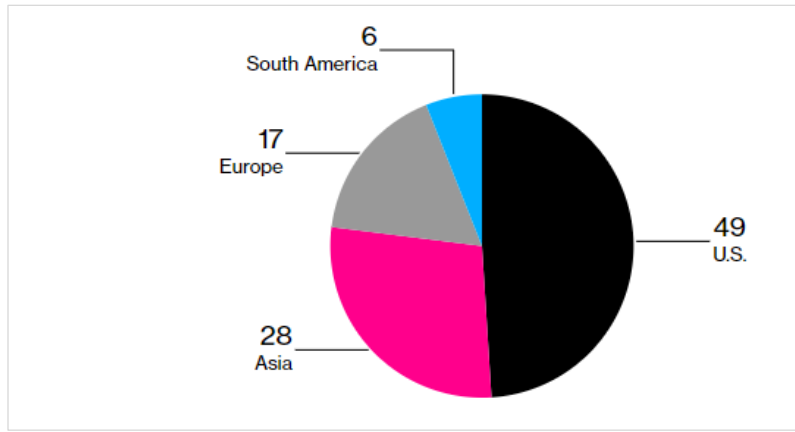
Source: US Labor Department, Bloomberg

**Fourth Inversion?**  
Treasury 2-10 yield curve has inverted three times since 2000



Source: Bloomberg

**100 firms pull \$45 billion of financial deals<sup>1</sup> since the war in Ukraine war**



<sup>1</sup>: Number of delayed deals includes IPOs, bond, loan, asset-backed securities, M&A transactions  
Source: Bloomberg

# Cyclical or event-driven demand reduction could cause yet another U-turn in the pricing environment

*HYPOTHETICAL – NO EVIDENCE THIS WOULD HAPPEN*



**Consistent price increase  
from 2020 levels**



**Sudden decrease to  
below-2020 levels**



**The overall impact could be a rate reduction  
of 8-15% from the peak at that point**

## **Talent implications for the market**

- Sudden over-supply of currently hard-to-find skills, which typically results in a buyer's market
- Hiring freezes across the board, which could lead to cooling off in wages
- Talent model (location/type of pool) restructuring

## **Pricing implications for enterprises**

- Sudden fall in market rates
- Some enterprises could be stuck with high rates they may have recently negotiated
- Predatory pricing by service providers to retain book of business and/or drive growth

# To manage this situation, enterprises should have practical benchmarking clauses, which should be used for ongoing quick course correction

## Why one-time, sporadic benchmarks do not work

**Enterprises could be in permanent catch-up mode in relation to market norms**

- Significant cost and time investment to select benchmarker and execute
- Enterprises could overpay for years before an objective correction/recalibration happens
- Even after that, the gap is rarely closed, and it is down to the discussions between both parties



## Why an ongoing focus on pricing is needed

**Contracts and associated engagement/pricing models are constantly evolving**

- Multiple change requests and addition of scope instances during a contract's tenure
- Sudden event-driven market pricing changes need quick rectification
- Significant value capture opportunity at multiple points as the contract progresses

**Adopt a seamless mechanism to constantly gauge where the market is and use it to constantly adjust terms with the suppliers. The longer the delay, the harder it is to correct.**

**Unknown #2**  
**Hyper-inflation due to**  
**geopolitical/oil situation**



## What impact is the current situation in Ukraine likely to have on your outsourcing portfolio? (choose one)

- No impact – 30%
- Minor impact (e.g., very little work is done for us from that region, and we have alternatives) – 37%
- Material impact (e.g., some work is done for us from that region, and we may be able to find alternatives) – 15%
- Major impact (e.g., a lot of work is done for us from that region, and we do not have any immediate alternatives) – 8%
- Not sure – 10%

# Geo-politics can exacerbate the already precarious talent demand-supply situation in the global services industry, leading to hyper-inflation in pricing



## Current situation in the global services industry

- Multi-year demand for digital transformation
- Talent crunch
- Wage inflation

**Increase in pricing**

+



## Recent geo-political triggers in the global economy

- Covid-led supply chain shocks impacting revenue growth
- Oil price shock
- Escalating commodity prices (steel, aluminum etc.)

**Severe margin contraction for enterprises**

=



## Potential impact on the global services industry

- Resurgence of cost takeout sourcing initiatives
- Further increase in talent requirement
- Reduced talent supply due the situation in Ukraine
- More global wage inflation

**Hyper-inflation in global services pricing**

# The solution to the situation lies in what we call a “surgical view” on where to raise rates and by what amount



## How competitive is your deal already?

Some enterprise clients may already be paying their providers much higher than market ranges. In such cases, it is important to not blindly agree to rate increase requests. The converse could also be true; a super-competitively negotiated set of rates should be examined for equitable increases.

## What are the most impacted scope areas?

Wage inflation is not the same across every skill set and even geography. Enterprises should assess the most critical skill sets for their businesses and determine which are seeing the most significant talent shortages. This process will help to prioritize focus areas for rate discussions.

## What is the justifiable magnitude of increase?

Use contemporary price benchmarks to ascertain the correct increase for each location and function. Avoid paying specialty skill premiums for mature skills and avoid across-the-board rate increases. Remember, FX can be your ally!

# Discussion points for today

Context setting on  
the past 12 months

3 pitfalls to  
avoid

2 unknowns to  
navigate

Open panel  
discussion



# Discussion points for today

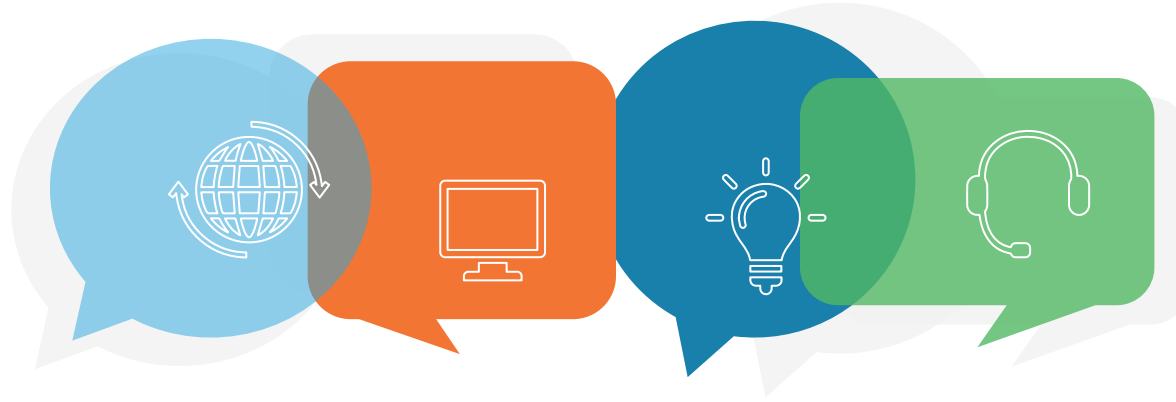
Context setting on  
last 12 months

3 pitfalls to  
avoid

2 unknowns to  
navigate

Open panel  
discussion

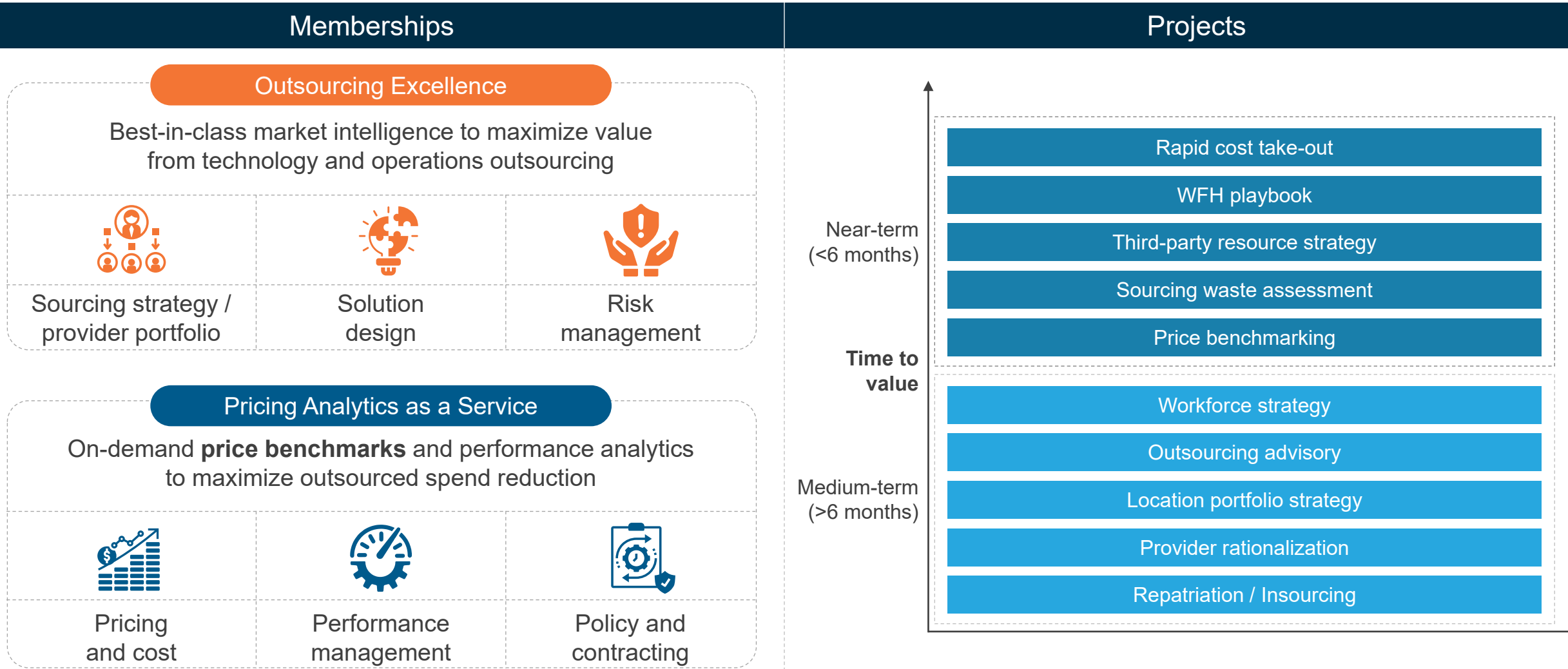




### To ask a question during the Q&A session

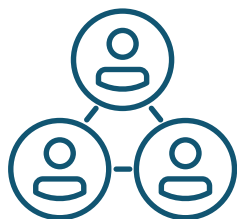
- Access the **Questions** panel within the Zoom console, which is typically located on the bottom of your Zoom window.
- Type your question in the dialogue box, then select **Send** to submit the question to our session Organizers/Panelists
- Attendees will receive an email with instructions for accessing today's presentation
- To ask a specific follow-up question, please contact:
  - Rahul Gehani, [rahul.gehani@everestgrp.com](mailto:rahul.gehani@everestgrp.com)
  - Abhishek Sharma, [abhishek.sharma@everestgrp.com](mailto:abhishek.sharma@everestgrp.com)

# Everest Group assists procurement teams in capturing value from their services spend through memberships and focused projects



# Pricing analytics as a service for IT-BPS Services

## IT-BPS services pricing database snapshot



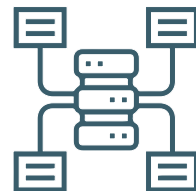
300+ roles



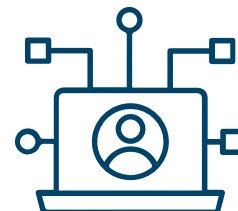
~50 locations



40+ sub functions



150+ RUs



375,000+ data points




1,000+ skills covered

## Illustrative functions covered

*not exhaustive*

BPS	IT-Apps	IT-Infra
F&A	DevOps	Workplace
Procurement	Testing	Cloud services
CXM	AMS	Cyber security
Human resources	Engineering	Network
Industry BPO	Data & analytics	Mainframe

Key features
Rate cards (T&M / staff augmentation)
Resource Unit (RU) / output- based pricing
Effort ratios and solution insights
SLA, KPIs, XLAs
Delivery metrics including shoring pyramids, and productivity
Contract T&Cs



Peter Bendor-Samuel

Founder & CEO

✉️ 🐦 📘

### Why Areas of Enterprise Services Spend Will Increase in 2022 | Blog

DECEMBER 9, 2021 | SHARE [f](#) [t](#) [in](#) [d](#)


When looking at the market outlook for services spend in 2022, I see several areas that will change dramatically. It is clear there are two price drivers: the changes to the post-COVID-19 situation and the need to be more strategic in a digital world. Both drivers will change the way companies spend next year, and both will increase the cost to operate. Here is my overview of the coming changes.

[Read more in my blog on Forbes](#)

PRICING

SERVICE PROVIDERS

TALENT



Achim Arora

Vice President

✉️


### How Much Will Your Next Outsourcing Deal Cost? Understand These Seven Factors That Impact Pricing for Services | Blog

SEPTEMBER 29, 2021 | SHARE [f](#) [t](#) [in](#) [d](#)

With outsourcing activity again picking up after slowing when the pandemic hit, now is a good time to gain a better understanding of pricing for services. To help ensure your enterprise gets the right value out of your next outsourcing deal, read on for expert pricing tips and experiences.

Below are seven common trends we see that can impact the pricing of outsourcing services:

- Of course, it's the economy:** Without a doubt, the economy plays a major role in the movement of deal pricing, especially as COVID-19 can throw away all previous estimates on the futures of pricing rate cards. The pandemic forced many companies to renegotiate their contracts, and mid-term invoice discounts while others used it as an opportunity to renegotiate their existing contracts. As market travel bans are resulting in upwards movement in pricing at high-cost locations while pricing for digital talent at low inflection point and is expected to turn around.
- RFP versus sole-sourced deals:** First, there is nothing wrong with a sole-sourced deal. It can be more efficient, show greater value compared to an RFP-led scenario, given you have a trusted relationship with a vendor of choice. By introducing an overall bidding process, an RFP can often be more effective in getting the best pricing. However, due to excessive delivery during delivery may not be what was promised during the talks or negotiations.
- Cross subsidization of accounts:** Often, vendors subsidize their loss-making accounts through their profit-making accounts. It is important for enterprises to benchmark regularly to see how prices compare against market peers and the overall industry.



Ashutosh Dhoot

Senior Analyst

✉️ 📘

### Everest Group's 5S Framework: Choosing the Right Software Licensing Strategy | Blog

FEBRUARY 9, 2022 | SHARE [f](#) [t](#) [in](#) [d](#)

*With the myriad of cloud software choices on the market, determining the right licensing strategy is more complicated than ever. Don't let confusion and indecision prevent your enterprise from getting vendor discounts and fully optimizing your resources. Learn how Everest Group's 5S Framework can help your organization choose the right license model.*

Organizations are increasingly dependent on various software for productivity, automation, security, and other critical enterprise needs. Google pioneered the move to cloud-based applications with G-Suite. Today nearly every major enterprise platform or productivity suite has a cloud-based version.

The rapid transition of enterprise applications, tools, and platforms from on-premise to the cloud has simplified commercial models and invoicing. But it has also made subscribing to the right license all the more complicated and important.

Having a plethora of licensing options available for each software often leads to indecision by organizations in selecting the right fit. While this task can be arduous, having the right licensing strategy will lead to higher savings and optimized resources.

Enterprises are frequently at a disadvantage in negotiating better prices and discounts because they don't understand the licensing nuances, which often leads to vendors overselling features that are then underused.

After analyzing the key licensing models prevalent in the market, Everest Group developed its comprehensive 5S Framework. This simple yet effective approach to choosing the right license model works as a guiding principle to reduce associated risks and helps enterprises build the optimal licensing strategy.



## Stay connected

### Website

[everestgrp.com](http://everestgrp.com)

### Social Media

 [@EverestGroup](https://twitter.com/EverestGroup)

 [@Everest Group](https://www.linkedin.com/company/everest-group)

 [@Everest Group](https://www.facebook.com/EverestGroup)

 [@Everest Group](https://www.youtube.com/EverestGroup)

### Blog

[everestgrp.com/blog](http://everestgrp.com/blog)

### Dallas (Headquarters)

[info@everestgrp.com](mailto:info@everestgrp.com)  
+1-214-451-3000

### Bangalore

[india@everestgrp.com](mailto:india@everestgrp.com)  
+91-80-61463500

### Delhi

[india@everestgrp.com](mailto:india@everestgrp.com)  
+91-124-496-1000

### London

[unitedkingdom@everestgrp.com](mailto:unitedkingdom@everestgrp.com)  
+44-207-129-1318

### Toronto

[canada@everestgrp.com](mailto:canada@everestgrp.com)  
+1-647-557-3475