



WHITE PAPER

How to Determine the Right Sourcing Strategy for Hosted Application Management

Sponsored by: AT&T

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EXECUTIVE SUMMARY

As the global economy continues its recovery, businesses are increasingly turning attention to strategic, revenue-generating goals. But at the same time, businesses have not shed their focus on cost-control and bottom-line profitability. This creates tension for IT organizations that are being asked to free up resources to support business' strategic goals while simultaneously cutting costs.

This conflict has implications for application hosting and application management. On the one hand, IT must provide high application service levels necessary to support customer-facing initiatives, while on the other, IT must keep costs down and minimize capital expenditures (capex) as well as operational expenses (opex).

Many organizations are turning to third parties for hosted application management (HAM) as a means to accomplish their corporate imperatives. The benefits of using a third-party services firm for hosted application management include shifting costs from capex to opex, leveraging service provider expertise and intellectual property, and tapping into service provider economies of scale. Using a third-party services firm for hosted application management can yield benefits but also comes with risks. Data security, service provider costs, and trust are the typical hurdles buyers must wrestle with.

Organizations must carefully weigh the costs and benefits of managing and hosting their applications internally or through a third-party service provider. IDC recommends that organizations opting to utilize hosted application management services follow a multi-phased approach that includes anticipating and evaluating needs, building a strategy, articulating the business case, selecting the right provider, piloting an application, and continuously managing the service provider relationship.

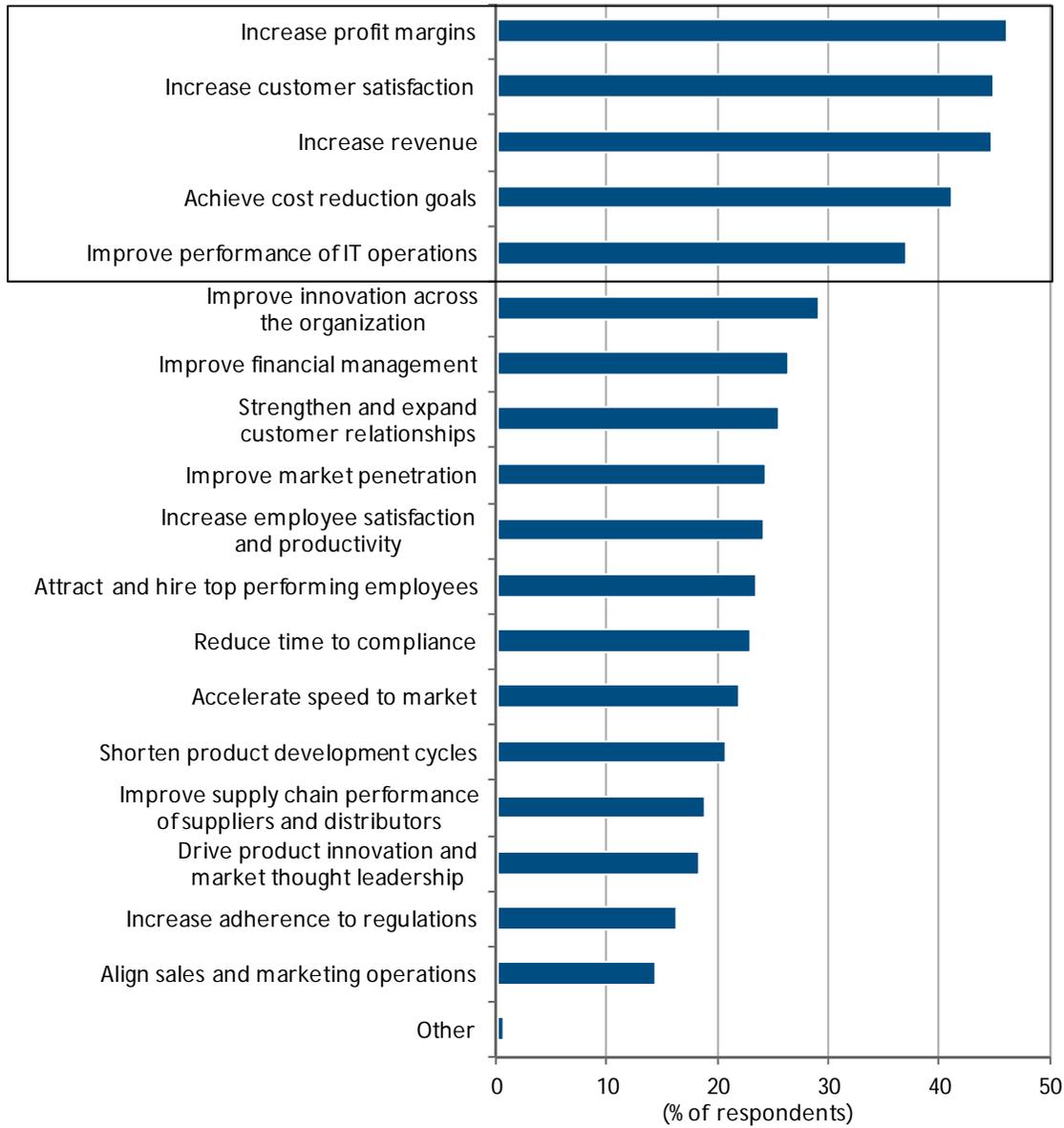
2014 CORPORATE IMPERATIVES AND IMPACT TO HOSTED APPLICATION MANAGEMENT

With a strengthening global economy, enterprises are focusing on a variety of objectives. In fact, IDC's 4Q13 *Application Outsourcing Survey* found that corporate initiatives today span customer-facing, revenue-generating activities as well as bottom-line oriented, cost-cutting activities. The top 5 company imperatives were increasing profit margins, increasing customer satisfaction, increasing revenue, achieving cost reduction goals, and improving the performance of IT operations (see Figure 1).

FIGURE 1

Top Corporate Imperatives, 2014

Q. Please select the top 5 company imperatives over the next 12 months



n = 402

Source: IDC's *Application Outsourcing Survey*, 4Q13

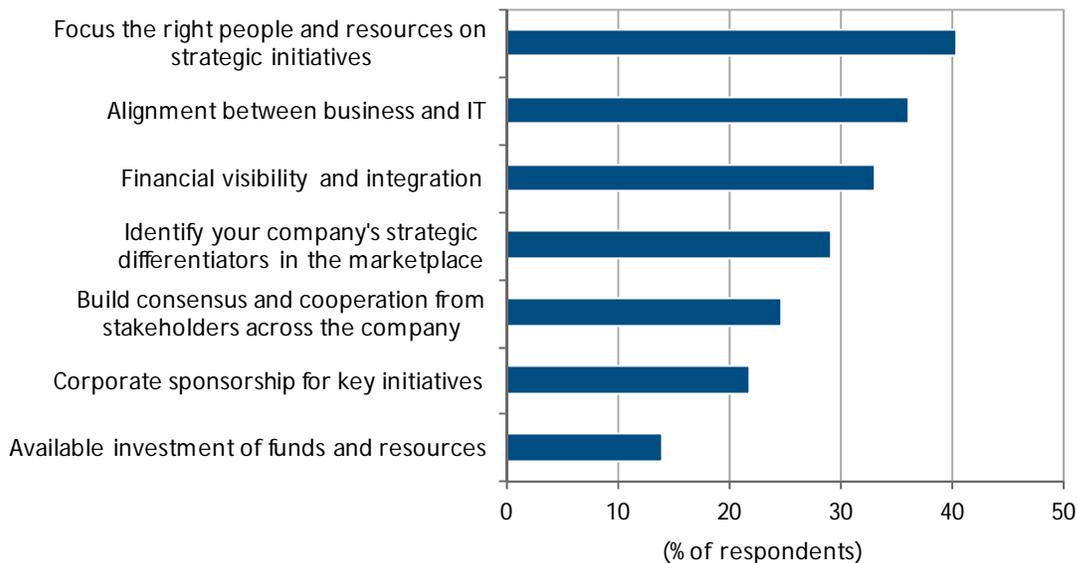
Shifting corporate focus has a profound impact on IT organizations and their approaches to application management. IT and the applications it supports enable business-critical processes across the enterprise, and as businesses shift focus from cost take-out to broader revenue-generating goals, IT must become more strategic in its focus, serving as a true partner to lines of business and enabling new initiatives and activities.

However, as corporate imperatives evolve, organizations can face several challenges in accomplishing their objectives. IDC's *Application Outsourcing Survey* found that the top 2 challenges organizations face in executing their corporate strategy were focusing the right people and resources on strategic initiatives and aligning business and IT (see Figure 2).

FIGURE 2

Top Challenges for Executing Corporate Strategy, 2013

Q. Please select the two greatest challenges to execute your corporate strategy.



n = 402

Source: IDC's *Application Outsourcing Survey*, 4Q13

The implications of these corporate imperatives and challenges in executing corporate strategy on application management are multifaceted. They include:

- Performance.** Applications are critical tools that support customer-facing resources and business processes. Organizations must employ methods that ensure application uptime and accessibility so that customer-facing resources are able to generate high customer satisfaction through their customer interactions and can build the top line without any disruptions to tools they utilize to help them execute their business process tasks.

- **Cost-effectiveness.** Organizations must contain application management costs and find innovative ways to contribute to cost reduction and increased profitability.
- **Resource optimization.** Focusing on top-line revenue-generating activities requires the freeing up of IT resources. But as application infrastructures get more complex, managing and monitoring them becomes more burdensome, requiring greater IT staff attention and resources. Strategies such as outsourcing application management to a third party or using application management tools that provide high degrees of automation are effective ways to mitigate this burden.

The bottom line is that IT organizations must possess agile, reliable, and operationally resilient capabilities in their application management function. IT organizations need a solution that reduces their IT burden to ensure they can contribute their part to overarching corporate imperatives.

KEY TRENDS IN HOSTED APPLICATION MANAGEMENT

Today's IT environments are marked by application and system heterogeneity. This has been brought about by a variety of factors including M&A, the existence of "pockets" of IT, and the need to support demanding and rapidly changing business environments with increasingly sophisticated yet flexible applications and solutions. Organizations have built massive inventories of applications over time, and the complexities in servicing and managing those applications have stressed organizations. Moreover, effectively servicing these increasingly complex application environments has driven infrastructure and activity costs higher: IDC studies consistently show that more than half of IT staff's time is spent simply "keeping the lights on," crowding out room to support more strategic initiatives.

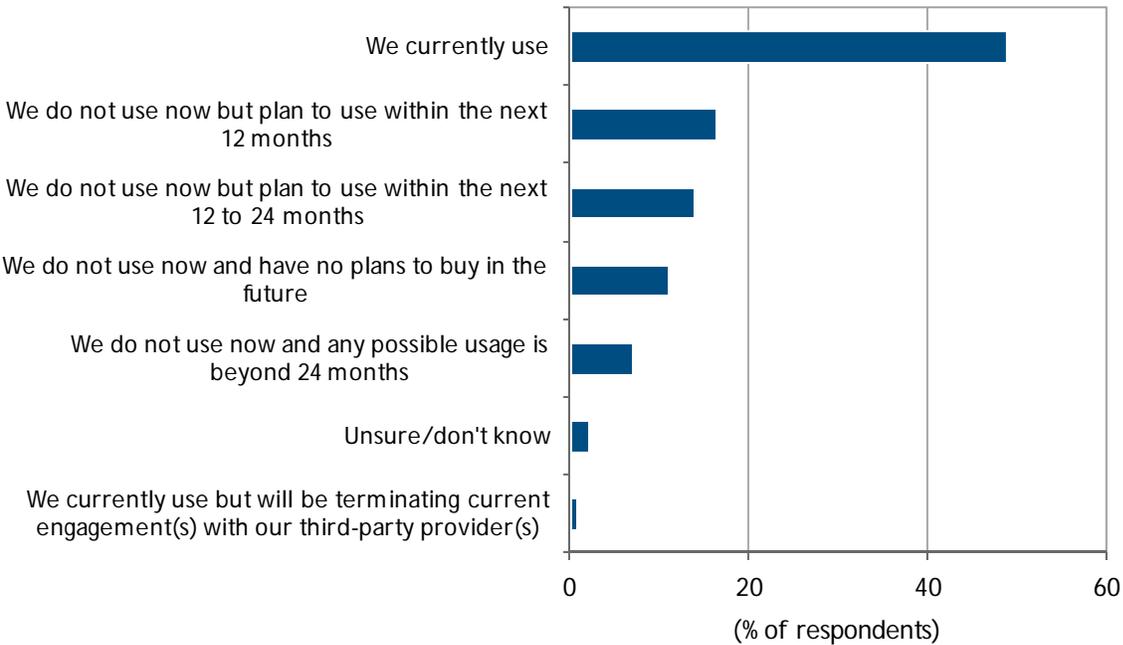
To deal with this, organizations are pursuing a variety of strategies. One particular strategy is outsourcing infrastructure and application management to a third-party service provider. According to IDC's *Application Outsourcing Survey*, almost 50% of organizations currently utilize third-party service providers for hosted application management. Another 16% don't currently use third parties for HAM but plan to do so in the next 12 months, and 14% plan to use third parties for HAM in the next 12-24 months (see Figure 3).

This tendency to outsource application and infrastructure management functions together has fueled the growth of the worldwide hosted application management market. IDC estimates that the worldwide application management services market reached an estimated \$10.6 billion in 2013, growing 6.7% from an estimated \$9.9 billion in 2012.

FIGURE 3

Use of Application Management Services

Q. *Hosted application management – Which of the following third-party application services does your organization currently use? And which does it plan to use in the stated time frames?*



n = 405

Base = all respondents

Notes:

Data is not weighted.

Use caution when interpreting small sample sizes.

Source: IDC's *Application Outsourcing Survey*, 4Q13

Benefits and Drivers of Hosted Application Management

What steers organizations to utilize third-party service providers to manage and host their applications rather than manage and host them internally? The drivers tend to center on three areas:

- **Reducing capex.** Managing applications internally forces an organization to make long-term capex investments in application infrastructure hardware, software, and operating environments on which they run. Infrastructure, like any asset, has a useful life. By outsourcing infrastructure management for their applications, organizations can trade capex costs for a steady, predictable stream of opex payments.

- **Offloading burden to update resource skills on latest tools and technology.** As older hardware and software environments need to be decommissioned and replaced, new hardware and software need to be installed and tested. As a result, internal IT resources' skills must be frequently updated to keep up with technology change and support application management service levels. By outsourcing ongoing infrastructure and application management activities, the burden of continuously investing in training and day-to-day operational management of platforms and processes is shifted to the third-party provider.
- **Generating economies of scale.** Application hosting providers often can leverage their application management infrastructure, technologies, and processes across a range of clients, thereby providing economies of scale to buyer organizations, which can be highly difficult for individual enterprises to achieve on their own in fully dedicated and traditional application environments. These economies of scale accrue to the technology platforms themselves as well as to the IT staff and the skills and training required to perform the management tasks.

By outsourcing application and infrastructure management, organizations can focus internal IT resources on other more critical corporate initiatives. They can leverage service providers for more standardized, less mission-critical tasks and be more strategic in their resource management.

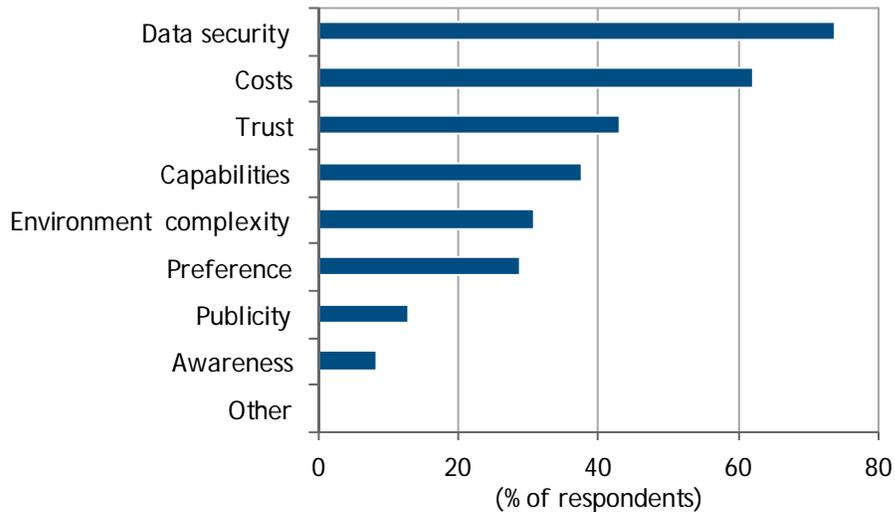
Challenges with Hosted Application Management

Although using hosted application management services can be an attractive strategy, it can also come with risks. Data can be a source of competitive advantage, and heightened sensitivity over who sees it and who accesses it is a top concern for application owners. In addition, outsourcing application management comes at a price for buyers, and with two of the top 5 corporate imperatives focusing on cost reductions and margin improvement, providers must offer HAM services that are financially viable as well as generate a business benefit for buyers. The results of IDC's 4Q13 *Application Outsourcing Survey* indicated that the top 3 factors that would contribute to buyer organizations not using any third-party application services were data security (nearly 74%), costs (62%), and trust (43%) (see Figure 4).

FIGURE 4

Buyer Concerns with Third-Party Application Services

Q. Please select the top 3 factors that would contribute to your organization not using any third-party application services, whether or not your organization currently uses them.



n = 405

Notes:

Data is not weighted.

Use caution when interpreting small sample sizes.

Source: IDC's *Application Outsourcing Survey*, 4Q13

AT&T's Hosted Application Management Services

As it continues to expand core offerings beyond providing simple connectivity to being a higher value-added services provider, AT&T has built and augmented hosted application management services. The provider brings multiple areas of expertise that make it an option for organizations considering hosted application management. Key attributes of AT&T's HAM services include:

- **Competencies in datacenter and hosted infrastructure management.** AT&T manages global datacenters and hosting environments on a scale that can dwarf many enterprise IT shops. The provider has built out a spectrum of integrated service solutions that range from infrastructure focused services for colocation, cloud services, and managed hosting and infrastructure to application focused services for managed applications and prepackaged solutions.
- **Application network performance, skills, and capabilities.** A key advantage that AT&T holds over many of its competitors is that its hosted application management services encompass the full stack of application hosting, network infrastructure, and application management. Possessing control and ownership over the full stack of application management components enables buyer organizations to capitalize on AT&T's network performance, skills, and expertise.

- **Multi-tiered support levels.** AT&T's hosted application management support model consists of several layers to streamline and ease customer support. At its core is a named, designated team that provides continuous monitoring, management, and support of the customer's application and the application infrastructure. An added component to the core team is a client executive that serves as the client contact point and manages the customer relationship as well as aligns the appropriate service offerings to the customer's needs to ensure client satisfaction. AT&T refers to its hosted application management support model as "white glove" because of the depth of customer intimacy that the program provides its customers.
- **Trusted business partnership.** With a longstanding heritage in providing telecom services and over 15 years of experience in hosting and managing business applications, AT&T has built a reputation of being a service provider that businesses have come to rely upon and trust.
- **Focus on application reliability and data security.** At the heart of AT&T's hosted application management services is a multi-layered security architecture that promotes high levels of data security. In addition, AT&T's managed application service-level agreements (SLAs) can be tailored to meet a wide variety of application availability and reliability needs.

RECOMMENDATIONS

Using a hosted application service provider can help organizations alleviate application and infrastructure management challenges and allow them to leverage industry best practices and capabilities. But organizations that are considering hosted application management services should plan and continuously manage their service provider relationships to extract maximum value. Key success factors to successfully utilizing an application hosting provider range from setting appropriate application service goals to building the business case and exercising due diligence during the vendor selection process.

Understand Your Organization's Needs and Capability Gaps

If your organization currently manages its applications internally and is considering a move to hosted application management services, the first step is to gather data around its capabilities, strengths, and weaknesses. This can be a qualitative exercise to rate how effectively (internally) your organization manages its applications. Although you may need to do this on an application by application basis, to simplify this step, organize specific applications into groups aligned by business usage and survey key stakeholders from both the business and IT to rate how well the organization meets criteria for containing costs and application availability. From there, you can spotlight where there may be risks and opportunities to improve application management. The key is to identify whether your organization has an issue or opportunity for business gain and where it is and begin sizing it before engaging outside help to execute your strategy.

Use the Assessment to Forge Your AM Strategy

If it appears that your organization may lack sufficient optimization in managing applications internally, begin setting application management goals and objectives that your organization needs to accomplish that alignment with corporate imperatives and alleviate assessment gap areas. From there, outline the overarching priorities and different tactical execution options. Start with framing the strategy around one application, and scale from there. This will aid in creating a strategic framework to help highlight the risks as well as quantitatively measure the business impact and budget structure that shows the business value of outsourcing application hosting and management.

Build the Business Case

Once the strategy has been shaped and articulated, measure the value of hosted application management through a multi-year cash flow analysis. Look at the current costs to manage an application internally, and compare that with using a service provider to manage. Break costs down into hardware and software for the infrastructure and network, as well as activity costs, to create and manage the environment, manage the service provider, and govern the hosting provider relationship. Break benefits down by activity cost savings, productivity gains generated by repurposing resources, and eliminated infrastructure costs, and measure over a multi-year period. Risk-proof your model through evaluating the probability of achieving benefits and reducing or eliminating costs. While this is not a simple exercise, organizations must gain an understanding of the longer impacts of application hosting to understand the potential impact to their cash flows.

Exercise Due Diligence in Vendor Selection

Organizations should approach the vendor decision with a long-term vision and strategy. They should get to know all aspects of the vendor and its service delivery model and do due diligence by speaking with other customers of the vendor. Areas to focus on include:

- **Pricing/cost model.** This is obviously a key consideration, and the vendor's pricing and service delivery model should fit within your overall business plan and financial goals.
- **Service levels, security, and reliability.** Entrusting business-critical data and applications to a third party requires selecting a trustworthy vendor with a solid track record of providing uninterrupted application service levels and ensuring data security.
- **Skills and capabilities.** It's important to understand your vendor's technical expertise and global infrastructure management capabilities. This is especially critical if your overall application strategy seeks to increase reliance on your vendor's application management over time.
- **Strategic fit.** Look for vendors with forward-looking strategies that seek to form a strategic partnership with you, are willing to take some of the risk, and possess values and traits similar to those of your organization.
- **Scale and scope of vendor.** It often makes sense for organizations to consolidate vendors to simplify vendor management and concentrate buying power. Pursuing this goal requires vendors that can maximize the amount of capex they can shoulder.
- **Support model.** Is it clear how the vendor interfaces with you? Who do you work with and how? You should consider the vendor's support availability metrics and how they mesh with the needs of your business.

Choose an Application to Test the HAM Waters

Moving an organization's critical business applications to a third-party hosting environment can be extremely risky. Organizations that have made the decision to use a service provider should take a phased approach to moving their application management to their service provider. Pilot hosted application management first with lower-risk applications to prove out the vendor's service level and value delivered, and then onboard subsequent applications based on risk levels and expected business value.

Optimize Through Continuous Learning and Improvement

After piloting hosted application management with a less risky application, leverage lessons learned from the pilot to evaluate your HAM strategy and approach to service provider relationship management. If the vendor is able to prove capabilities and generate business value for the pilot application, consider how to maximize the relationship further by increasing scale and making overall application governance tasks more efficient. The idea is to tune the organization's overall IT operations engine so that organizational resources are utilized optimally.

CONCLUSION

IT organizations today are under pressure to handle multiple conflicting demands. The demands cross strategic top-line initiatives as well as bottom-line cost-control measures. To support these conflicting demands, sometimes organizations must pursue strategies that offload application management and infrastructure management to a third-party application hosting provider.

IDC's 4Q13 *Application Outsourcing Survey* found that almost 50% of organizations are currently using a third party for hosted application management services, and another 30% plan to do so within two years. While using a third-party services firm for hosted application management has risks like data security, costs, and trust, it also brings multiple advantages that center on enhancing cash flow management, ensuring use of the latest tools and technologies, and tapping into economies of scale.

Organizations that are contemplating the right sourcing strategy for hosted application management should follow a multi-phased approach that includes anticipating and understanding capabilities, building a strategy, creating the business case, selecting the right provider, piloting an application, and continuously managing the service provider relationship.

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