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From the Editors’ Desk

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A broad array of optimization strategies are currently being utilized by the financial services industry. From platform-based solutions to innovative pricing models, these strategies vary from organization to organization and can provide an insight into the future direction of the industry's technology and business focal points. This survey-based article highlights the outsourcing trends in IT optimization among the financial services organizations across US & Europe.

The survey was conducted in July 2009. There were 26 respondents, and 12 of the world's largest financial institutions were represented.

Introduction

In the ultra-competitive financial services space, technology innovation is increasingly driving business growth. Organizations are finding that in order to streamline a business process, launch a new product, or provide a new service, IT must first be optimized, agile, and scalable. In many cases, IT optimization is critical to the success of the enterprise. To further understand the IT optimization priorities of the financial services industry, a survey was created to poll clients on their strategies and optimization plans in the short and medium terms. This article highlights and analyzes these findings.

Cost reduction continues to be the key driver

Cost reduction is the most important factor driving sourcing decisions today. About 50% of the responding IT organizations indicated that their key driver for outsourcing is cost reduction—above other factors such as lack of in-house resources, leveraging technical expertise, gaining competitive advantage, cheaper man power, consolidating assets, and increased flexibility. An interesting trend emerges when comparing this year’s results to those compiled a year ago: While the key driver for outsourcing continues to be cost reduction (reduced from 64% to 50%),
there is an increased focus on competitive advantage (from 6% to 16.7%). This reinforces our belief that the near-term sourcing focus for most organizations is cost reduction, while the long-term focus is shifting towards gaining a competitive advantage.

**New pricing models gaining importance**

Strategic cost reduction measures find innovative ways to peg expenses to business activities. We believe that this is best achieved by implementing a structured approach to cost reduction, supported by strong governance and program management and backed up with synergetic pricing models.

IT Organizations are encouraging value-based pricing models that enable both the client and vendor to share the risk and reward-allowing them to work together towards the common goal of improving efficiency and bringing in predictability and flexibility. Of the respondents, 55% have indicated that Fixed Price (FP) managed services with risk/reward model is the preferred pricing model to work with.

The Managed Services model helps clients focus on their core business while also reducing costs. It indicates a shift from a focus on effort and inputs (time and labor) to a focus on outcomes. This allows IT service providers the flexibility to deploy their frameworks and processes to provide cost savings to IT organizations. Other newer, more innovative pricing models—Transaction-based and Outcome-based—are also gaining traction, with about 15% of respondents preferring each.

**Innovative solutions for gaining competitive advantage are becoming a priority**

A competitive advantage is primarily achieved by focusing on innovation, branding, and relationship building. New technology solutions, such as cloud computing and platform-based solutions, provide standardized offerings which require minimum upfront investment and allow clients to pay based on usage, reducing the need for large capital expenditures, improving an organization’s ability to scale,
and facilitating in the creation of competitive advantage. This is a key determinant for superior performance, and it ensures survival and prominent placing in the market.

Emphasis on building new capabilities to fuel further growth is on the rise, with more than 79% of respondents viewing that to be of strategic importance.
A good business strategy and resources are critical to sustain a competitive advantage. Of the respondents polled, 92% indicated that managing business cycles and processes through IT solutions is important to them. **IT-BPO integration** can help ensure that the business strategy is in synergetic alignment with its implementation.

There is an increasing trend towards the usage of **platforms** and third party products over custom-built applications. Of the organizations surveyed, 75% think that “ready to deploy solutions or platforms” are the way forward.

These results indicate that “Managed Services” and “utilities” which provide standard, hosted, and serviced platforms are on the rise, with an emphasis on standardized IT architectures, data designs, messaging, data feeds, and process logic. Platform-based solutions can go a long way towards reducing costs and quickening the innovation cycle. They help lower the total cost of ownership, achieve faster time to market, provide scalable solutions with high customization features, and facilitate building new capabilities which will help fuel future growth.

The monetization of Intellectual Property (IP) assets and the creation of joint ventures with pay-as-you-go options are two popular emerging strategies—with 25% of the respondents showing interest. In order to monetize their selected assets, clients are looking for partners who can provide upfront remuneration for the sale of IP on these assets and leaseback services to support the assets. IT organizations are also showing interest in joint venture agreements, wherein the IT services partner takes over the organization's technology assets. This helps reduce technology spend, as the organization would only pay for the business usage of these assets; the onus of maintaining and supporting the asset lies with the partner.

**Current snapshot of outsourcing spending across service lines**

Organizations were also polled to gain a deeper understanding of the extent of
outsourcing within five service lines—Testing (Independent Validation Services), Custom Application, Development and Maintenance (ADM), Infrastructure Services, Enterprise Solutions & System Integration, and Business Operations.

The percentages denote the level of outsourcing in organizations. A higher percentage in the 50-70% and 70-100% brackets denotes an increased focus on strategic outsourcing. Figure 5 highlights the findings.

**Infrastructure management** is the highest outsourced service line amongst the surveyed financial services organizations. Traditional infrastructure management has been heavily outsourced due to the maturity of its associated processes and metrics. Infrastructure continues to be the biggest area of focus which will contribute significantly towards IT optimization. Consolidation and virtualization of infrastructure and investment in remote infrastructure management will remain priorities.

Of the respondents, 75% indicated that enterprise and system integration solutions are more than 20% outsourced. This indicates that clients are increasingly able to leverage the advanced platform capabilities of IT services providers.

It was also found that testing services are relatively more outsourced compared to ADM services - 42% of the respondents say that more than 50% of their testing services have been outsourced, compared to only 15% for ADM services.

**Business operations** have the least outsourcing, with 42% of the respondents saying that outsourcing is less than 20%.

India continues to be the preferred outsourcing destination

With 75% of the respondents, India continues to be the most preferred destination for companies looking to outsource their technology and operations. However, China, Philippines, Mexico and Brazil are making their presence felt as alternative outsourcing locations.
Clients are increasing geographic diversity in their service delivery locations as newer service delivery geographies are emerging with niche capabilities. In the coming year, more clients will look for alternatives to India to de-risk their service delivery models which are otherwise geographically limited.

**Conclusion**

Moving from a laser sharp focus on cost reduction to co-creation along with service providers, there is a clear shift in priorities for technology solutions. From new pricing models, to cloud computing, to IP monetization and co-creation, innovative solutions are enabling firms to respond to market challenges effectively by reducing costs, achieving faster time to market, and developing a competitive edge while the market recovers. Furthermore, the increased focus on building competitive advantages signals that organizations are building for the future.

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IT OPTIMIZATION