



MEMA INFORMATION SERVICES COUNCIL

Special Report Special Report Special Report Special Report

The Frugal CIO:

A Survey of IT Outsourcing Usage in the Aftermarket

by ABeam Consulting (USA) Ltd.

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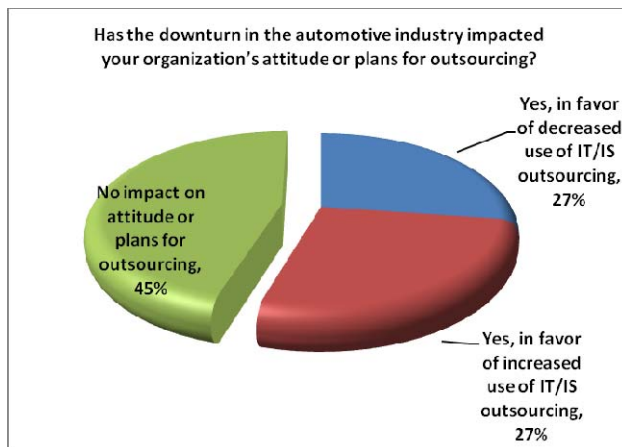
Executive Overview

Big changes in a short time period

In July 2008 the MEMA Information Services Council (MIS council), with support from ABeam Consulting, began working to understand the changing role of the CIO within MEMA member companies. Participants in the initial discussions described an evolution occurring in IT resource requirements. Increased understanding of business processes and better communications skills were cited as being of increasing importance for IT staff. At the same time, the rapid increase in technology choices and the acceleration of technology adoption were prompting CIOs to look to outsource service providers to acquire needed skills, augment staff or reduce IT operating costs.

IT Outsourcing: subcontracting of IT activities related to operation, maintenance or development of IT products and services. Generally replacing activities previously performed by in-house staff but also can be applied to new services for which an organization either lacks required skills or chooses not to use internal resources.

Since the initial meeting, ABeam has worked with MEMA to host forums, collect survey data and directly interview MEMA members to further understand how their companies are adapting their use of IT outsourcing services to meet current challenges. Our goal was to help MEMA members to learn the lessons of outsourcing as experienced by their peers and to help facilitate a discussion of both the best practices and the common pitfalls of going outside your IT organization to meet today's business requirements.



Over the same time period, the world has been radically changed by the onset of a financial crisis, which has forced the automotive industry to enter what many see as the most disruptive and distressing period in its 100-year history. Individual companies have had to respond with breakneck speed to major volume decreases, raw material price swings, customer and supplier bankruptcies, the collapse of credit markets, and the bankruptcies and bailouts of two

of the three American OEMs.

Mixed findings but common theme

Our survey found that it is very difficult to pigeonhole MEMA members into one or two general categories of outsourcing usage. Each survey participant seemed to be at different stages of outsourcing usage and had experienced different results from their outsourcing service providers. In addition, all indicated differing degrees to

which the financial crisis and OEM bankruptcies were coloring their view of the market and their reactions to the changing business environment.

A common theme identified through the research is a trend toward a more frugal CIO focused on exercising restraint and careful use of resources. The Frugal CIO is concerned with acquiring IT products and services in a careful, considered, efficient manner – a CIO who creatively uses already owned skills or contracted services to achieve the IT goals set by the business and to react to new changes as they occur.

As such, the Frugal CIO may be moving toward expanded use of outsourcing or away from existing outsource contracts, which have proved to be too expensive for the changing business environment. But in all cases, the Frugal CIO is looking to optimize service delivery in an environment of hard rationing choices.

Primary Themes

While each story was individual to each company, we did find certain themes and experiences that were often repeated or resonated among the participants as fair characterizations of their experiences and good rules of thumb to apply when entering negotiations for new services or seeking to correct a contract that has suffered from changes in understanding or business requirements.

The primary themes we found were:

1. **Another tool in the toolbox** – as businesses expand globally, outsourcing has become a more natural response to a variety of business challenges, the questions are becoming less about where the skills comes from and more about what skills are needed to meet a current or ongoing requirement
2. **Use the right tool for the job** – make certain skills are sufficient for the assigned tasks and that the service provider’s focus is aligned to your requirements
3. **Contracts can be tricky** – generally shorter term contracts are preferred (1 – 2 years), accurate but flexible scope definition is key to avoiding endless renegotiations, maintaining the option to bring some services or activities back in-house has been important in cases where outsourcing attempts meet with mixed results or inadequate service levels
4. **Maintain contact with people made redundant** – legacy knowledge can become critical and being able to retain access to the individuals who built and ran the systems prior to outsourcing is often helpful

This report expands on each of these themes and provides comments and insights from survey participants as to their experiences.

Survey Method

This survey of outsourcing trends was conducted in four distinct phases. First, ABeam worked with MEMA members in forums to gain an understanding of the types of questions MEMA members were asking about the use and benefits of utilizing outsourced IT service providers. Second, a questionnaire was designed that

reflected the questions heard, and participation was solicited participation through the MEMA Web site's online survey tool. After receiving and analyzing responses from 38 MEMA member companies, it was determined to further expand the survey to include collection of more qualitative information from individuals within the MIS Council via a series of telephone interviews. Finally, findings from the MEMA members were compared to overall trends in IT outsourcing.

While the participation rates of the individual survey activities were limited, it is believed that the consolidated results of all activities resulted in the ability to determine the themes described in this report and that the report fairly reflects the current state of IT outsourcing within the MEMA community.

1. Another Tool in the Toolbox

Despite the attacks on outsourcing of American jobs in the last election, the survey found that most participants were not swayed by the political rhetoric. Instead, most participants struggled to draw a clean line between "outsourcing" and purchasing any other type of service from a service provider. Whether it was looking for external support for application maintenance, network provisioning, help desk services, systems operations or implementation assistance; the primary question the Frugal CIO asked was about ability to meet a need and price. The location of the service provider was much less important than the ability to do the job at an affordable rate and an acceptable level of quality and timeliness.

Commonly Outsourced Services

- Programming
- Application Maintenance
- IT Operations
 - Server Monitoring
 - Backup/Restore
 - OS and DB Management
- Network Management
- Central Help Desk
- Specialized Services (EDI, Tax Table Maintenance, Web Site, etc.)

Virtually all companies participating in the survey indicated that they were no longer looking to reduce internal headcount via outsourcing. Instead, several companies reported efforts to scale back previous outsourcing contracts in order to bring critical

skills back in house. Some reported that their companies had actively managed target head count levels as part of an overall business planning process and that the decision to use internal or external resources for any particular task or project was driven more by the nature, criticality and duration of the task than any management strategy to shift work out of house. Finally, others simply drew support for IT operations and new projects from a pool of both internal and external resources approved by their corporate parents or contracted locally where local skills were important to the task at hand.

When queried about staff reactions to the use of outsourcing, most participants indicated that internal staff members were normally so overloaded with existing tasks that they generally were not threatened by the idea of using external service providers. The bigger concern among both management and staff was that any additional investments or expenses have a clear purpose and achievable benefits. In

short, it is not just the CIO who is thinking frugally these days, but most people within any particular company.

Survey participants uniformly reacted positively to the concept that the use of “outsourcing” has lost much of the FUD factor that had accompanied the idea in the previous decade and has instead become simply another tool in the CIO’s toolbox, which can be employed as needed without much fuss or bother.

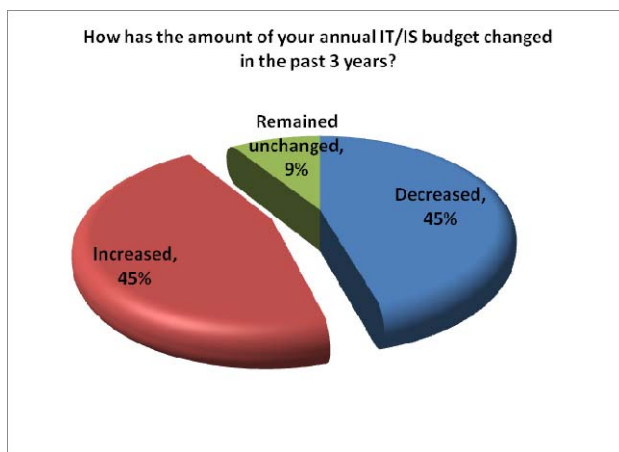
Outsourcing vs. Off-shoring

When it came to differentiating between outsourcing and off-shoring, there was more caution expressed by survey participants. Outsourcing, when defined as “using external service providers to perform operational or project related tasks rather than assigning said tasks to internal resources” was widely accepted. Off-shoring, when defined as using resources from other countries as a form of labor arbitrage, met with more cautious acceptance.

Participants reported very mixed results in the use of lower cost country (LCC) service providers. In particular, efforts requiring local business knowledge or where internal users or customers needed to interact directly or verbally with the off-shore resources were reported by several participants as having caused significant issues in their organizations. Often in these cases, the decision to place the work with an LCC service provider had been made by a corporate parent or at a board level. In the cases where the off-shore services failed or experienced difficulty, the primary cause cited was an overselling of capability by the LCC service provider at a bargain price that eliminated alternatives.

Cost of Outsourcing is Rising, Benefits Diminishing

Several participants mentioned that their decisions to use outsourcing has been impacted by rising costs for outsource services. As the supply of qualified, off-shore



resources has started to lag behind demand for these resources, vendors have been increasing unit costs and in many cases, smaller contracts no longer justify the additional costs required to use off-shore resources (i.e., costs for network connections to the service provider, administrative burden required to transfer requirements off-shore, additional iterations in requirements definition / development cycle due to

“telephone game” effects, additional layers of management needed for contract administration and vendor management).

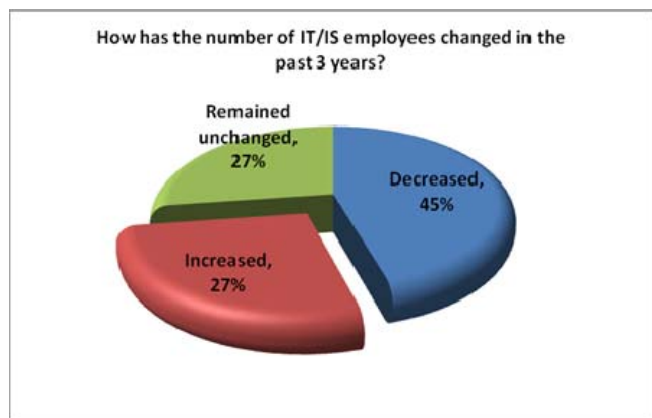
2. Use the Right Tool for the Job

The second theme to emerge from the survey centers on the need to choose a service provider with the correct skills and business focus for the task at hand. Very good results were reported where the requirements and skills were closely matched. Poor results occurred when the service provider either did not have the required skills or where the service provider's business focus did not align with the immediate need.

Skills Mismatch

In the case of skills mismatches, the issue most often cited by participants was a lack of understanding of local or industry business practices or a lack of understanding of legacy systems for which they had assumed operational or support responsibility.

Service providers were seen to assign individuals with adequate technical training in packaged applications or software development techniques, but often deep knowledge of specific localization requirements (e.g., state-to-state tax law differences, invoicing terms, EDI formats, etc.) and/or industry practices (e.g., automotive release management, serial / lot traceability, etc.) was concentrated in only one or two team members, creating a bottleneck in the ability of the service provider to address users' needs in a timely manner.



When service providers were tasked with taking over support of existing "legacy" systems, often they struggled to develop a sufficient understanding of the thinking that went into the initial development and implementation of the legacy applications and systems. Members reported reduced user satisfaction as the most common concern when service providers took over legacy systems. Inability to respond in a timely manner to system disruptions or business changes was also listed as a concern.

Conflicting Business Priorities

In other cases, participants described situations where an outsource provider took on a project or operational responsibility in order to get a foot in the door, but it quickly became clear that the service provider's real focus was on setting up a longer term contact or expanding their footprint within the participant's company. In the worst cases, it became clear to the CIO that the service provider's key person was being evaluated and motivated by his or her executives to focus efforts on setting up the future opportunity at the expense of delivering the contracted service. In these situations, the service provider was generally shown the door.

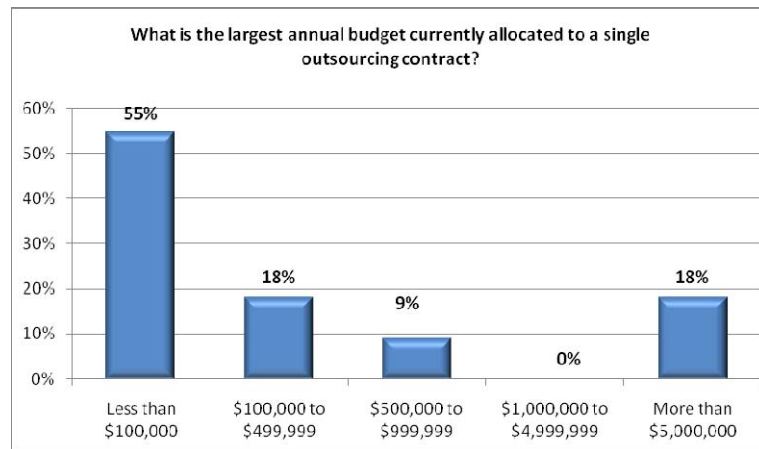
3. Contracts can be Tricky

Several survey participants commented on the need to be careful when contracting with outsource service providers. Issues were noted both with the vendor's contracting practices and with contracts executed when the business requirement was not fully agreed within the participant's organization. This was especially true for the first outsourcing contract executed.

Shorter Contracts Tend to be More Successful

When asked about the optimal duration of contracts, most survey participants favored shorter duration contracts. Generally contracts of not more than two years duration were seen as preferable to those that exceeded two years.

Participants that had engaged in long term contracts (three or more years' duration) reported the need to suspend or significantly change the terms of the contract after one or two years. The renegotiations were triggered by unanticipated changes in business need or due to the contract not being flexible enough to accommodate new or changed service requirements.



Keeping Arms around Scope Is Key

Contracts with unclear or overly specific scope definitions tend to be reported as having caused issues in execution. In either case, execution of the contracted services was often impeded by a continuing need to interpret or renegotiate the contract terms. Trying to strike an acceptable balance between specificity and flexibility continues to be a challenge.

Best practices for contract scope cited included:

- Get internal agreement, starting with an IT request that is agreed between IT and the business unit helps to ensure that the final contract reflects both the needs of the business and the needs of the IT organization.
- For more complex contracts, really read and understand the contract. Ask questions and seek clarification for any areas that are ambiguous. And in all cases, make certain to seek sufficient legal review.
- Consider all activities and costs that could be associated with the contract. Make certain that there is clear agreement as to which party is responsible. Hidden costs can significantly change the benefit of an outsourced service.

- Plan for contract amendments, as changes are inevitable. Have a clear process and policy for initiating and executing changes to scope or terms.

Finally, participants agreed that for contracts where the initial scope is hazy or difficult to define, it is best to work in smaller stages with fixed durations or clear interim deliverables until a full service level agreement can be adequately agreed by all parties.

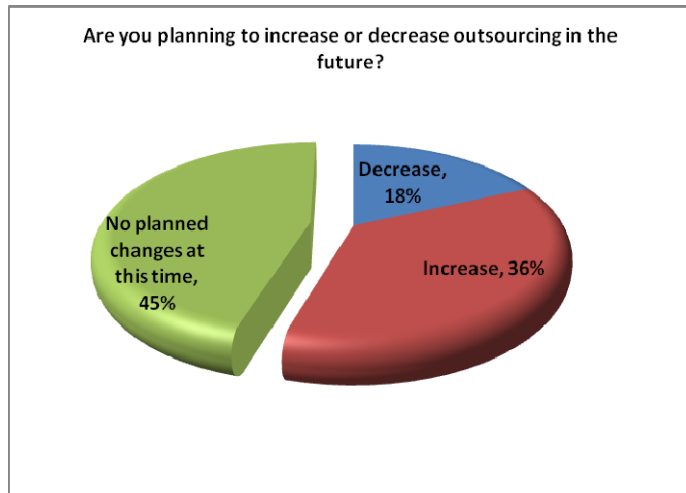
Some Things are Best Done Internally

In a few cases, survey participants reported that they decided to change the contracted services in order to bring key activities or services back in-house. In most cases, this was driven by a realization that internal resources were more convenient or capable of providing the service at more acceptable quality and service levels.

The most frequent activities brought back in-house were Level 1 help desk support and ERP architects / systems analysts. The trend was to use internal staff for activities that directly interacted with other business units and to outsource those activities like programming or IT operations which tended to be performed without involvement of other business units' personnel.

4. Maintain Contact with People Made Redundant

A final piece of advice provided by a few of the survey participants was to make certain to maintain the ability to contact or call upon the services of long-term employees or subject matter experts displaced by outsourcing efforts. There were several instances noted where former staff had been recalled or contracted to provide emergency support for the systems they had built or operated, as the outsource vendor was not able to provide sufficient support in a timely basis.



About the MIS Council

The MEMA Information Services Council, a peer group of the Motor and Equipment Manufacturers Association (MEMA), serves as a medium for industry interaction, education and idea exchange regarding matters of common interest to information technology (IT) and e-commerce professionals in the automotive aftermarket industry. It provides industry leadership and information through semi-annual conferences, committee activities, monthly newsletters and IT education.

About MEMA

Suppliers manufacture the parts and technology used in the domestic production of millions of new cars and trucks produced each year, and the aftermarket products necessary to repair and maintain more than 247 million vehicles on the road today. MEMA supports its members through its three affiliate associations, Automotive Aftermarket Suppliers Association (AASA), Heavy Duty Manufacturers Association (HDMA), and Original Equipment Suppliers Association (OESA). For more information on the motor vehicle parts supplier industry, please visit www.mema.org.

About ABeam Consulting

ABeam Consulting provides business transformation services that create strategic advantage, improve business processes, leverage technology innovation, and enhance organizational performance for leading multinational and domestic companies worldwide. ABeam partners with clients to diagnose and solve their real challenges with solutions that combine industry and operational best practices with technical expertise. Pragmatic approaches ensure that clients gain measurable value more quickly. Headquartered in Tokyo, ABeam's 3,800 professionals serve 700 clients in 21 countries. For more information, please visit www.abeam.com.

ABeam Consulting is a member of the Automotive Aftermarket Suppliers Association, an MEMA affiliate organization.

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