2011 SERVICE INDUSTRY OUTLOOK

Impact of the Global Economic Downturn on the Services Industry

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Executive Summary

As a follow-up to our *2009 Service Industry Outlook* report, Service Strategies performed a study to assess the impact of the global economic downturn on the service industry and to gauge the outlook for 2011. This report highlights the results of the study and provides an indication of the actions companies are taking within their service organizations to deal with the ongoing challenges of the economic environment.

Economists continue to have difficulty predicting when the downturn will end. Though things have certainly improved over the course of 2010, the outlook is uncertain for many sectors. Even with the U.S. Government's unprecedented bailouts of the financial and auto industries and the passage of the largest economic stimulus package in U.S. history, it remains unclear whether these actions have had the desired affect and what impact they will have on the economy moving forward.

> *"Based on the great people from the top down and past experience I am confident that the right improvements will be implemented to ensure we are a sustainable business into the future.'*
>
> *-Anonymous Survey Respondent*

U.S. unemployment remains high, running above 9% nationwide, though the stock market has rebounded positively**.** For the second year in a row, bulls ruled Wall Street. When the closing bell sounded on December 31, 2010 the S&P 500 was at 1,257.64, having gained 12.78% for the year. The Dow finished 2010 at 11,577.51, representing an 11.02% year-over-year advance. The NASDAQ wrapped up 2010 at 2,652.87, posting a 16.91% yearly gain. Even with these positive signs from the financial markets and major corporations reporting strong profits, companies are still reluctant to hire.

To facilitate this study, Service Strategies surveyed approximately 200 service executives from around the world. Over 77% of respondents hold executive or management level positions. In addition, approximately 62% are responsible for organizations with 100 or more service employees, while 35% employ more than 500. The respondent profile indicates that they have a clear understanding of the impact the downturn is having on their operations.

Participants answered questions about the impact the downturn had on their business as a whole and on specific areas such as service revenues, staff morale, performance and customer satisfaction. They were also asked about their outlook for 2011 and were given the opportunity to provide general commentary, which has been classified into four unique themes. We hope you find the report informative and useful.

Respondent Profile

Role in the Service Organization

The majority of respondents to the survey, over 77%, indicated they were in management or executive management positions. Executive positions included vice presidents, senior and executive vice presidents and general managers. Only 13% of respondents hold individual contributor or execution staff level positions. As a result, most respondents are likely involved in managing the financial aspects of their service operations and are therefore in a good position to comment on the impact the downturn is having on their service business.

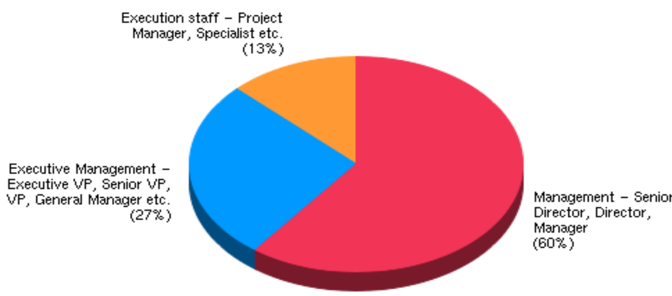

FIGURE 1- ROLE IN THE SERVICE ORGANIZATION

Size of Organization

When examining the size of the organizations that the respondents manage, a majority employ more than 100 service professionals, while 35% employ over 500 service professionals. The respondents provide a good cross section from which to gauge the industry's outlook for 2011, representing a broad range of organizations from small to very large.

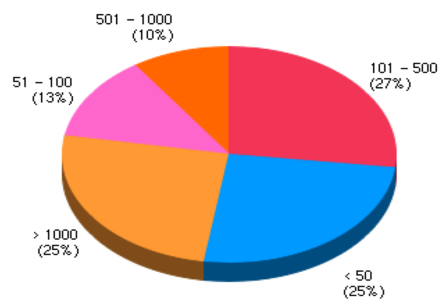

FIGURE 2 - NUMBER OF SERVICE EMPLOYEES

Service Areas of Involvement

Respondents were asked, "*Which areas of the service operation are you involved with?*" Areas of focus included Support Services, Field Services, Professional Services and eServices, with the majority of these, 82%, focused on Support Services. The next highest percentage is involved in Field Service operations at 42% and then Professional Services at 38%. The eService operations, representing 37% generally fit within Support Services. Note that respondents may be responsible for multiple aspects of their service operations. Overall, the respondents represent a good cross section of service disciplines.

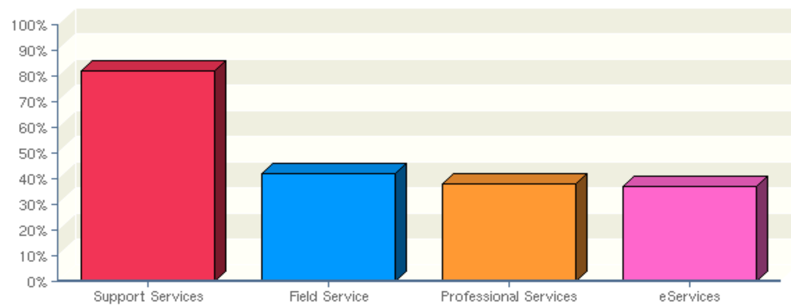

FIGURE 3- SERVICE AREAS OF INVOLVEMENT

Impact of the Global Economic Downturn

With consideration for the numerous influences placed on service organizations due to the economic downturn, respondents were asked to gauge the degree of impact that the downturn had on their operations over the past 18 months. The responses provide a reasonable indication of the overall impact the downturn has had on the broader Technology Services sector.

Impact on the Service Organization

Respondents were asked, "*Looking back over the previous 18 months, what impact did the global economic downturn have on your service organization*?" 70% felt that the economic downturn caused a moderate to significant impact to their business, while 28% experienced minimal impact. The result is in line with our expectation given the severity of the situation as expressed by industry analysts and financial experts. Not surprisingly, only 1% of respondents said they experienced no impact due to the downturn.

"Financials were hit hard, and all but the big boys stopped buying. We used this time to eliminate the bottom 10 % workers, and align organizations better for the expected upswing. We feel we are much leaner, much meaner coming out of this.'

- Anonymous Survey Respondent

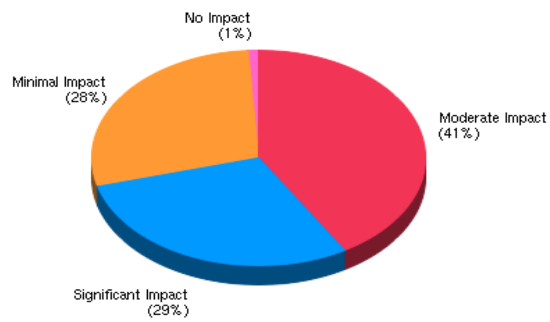

FIGURE 4 - DEGREE OF IMPACT ON THE SERVICE ORGANIZATION OVER THE PAST 18 MONTHS

Operational Areas Affected

When asked, *"Which areas of your operation were affected the most as a result of the global economic downturn (select all that apply)"* staffing levels were the most impacted at 79%. Forced headcount reductions or not being able to replace for attrition were the largest contributing factors. Other significant areas identified were compensation at 68%, which included furlough programs and a freeze on merit increases. Business travel at 67% was curtailed and investment in service technologies and service improvement initiatives at 58%, were delayed. Another alarming impact was that both staff and management training was halted. The cumulative effect of all these cutbacks, couple with reductions in staff, can have a devastating impact on morale and ultimately the quality of service and support an organization can deliver if prolonged over time.

Areas Most Affected by Downturn	Percentage
Staffing Levels	79%
Compensation (Merit Increases etc.)	68%
Travel Related Expenditures	67%
Tools and Technology Investments	58%
Service Improvement Initiatives	42%
Staff Training Investments	41%
Management Training Investments	38%
Conference attendance	1%
Misc.	5%

FIGURE 5 – WHICH AREAS OF YOUR OPERATION WERE AFFECTED THE MOST AS A RESULT OF THE GLOBAL ECONOMIC DOWNTURN (SELECT ALL THAT APPLY)

Change in Customer Satisfaction Ratings

When asked, *"Have your customer satisfaction ratings changed significantly over the past 18 months?"* We saw an unexpected result of 48% reporting no change and further 27% stating that it had actually improved. Only 18% of respondents reported a decline in their customer satisfaction ratings. The results are surprising in view of the painful cuts in staff and operational resources mentioned in the previous question.

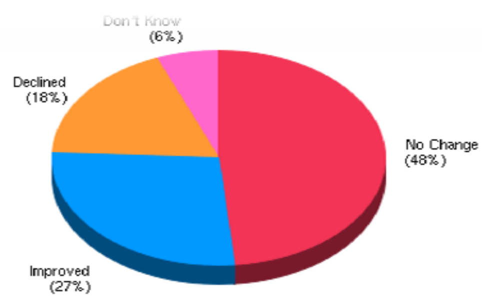

FIGURE 6– HAVE CUSTOMER SATISFACTION RATINGS CHANGED SIGNIFICANTLY OVER THE PAST 18 MONTHS?

Impact on Staff Morale and Performance

When asked, *"How has the downturn impacted staff morale and performance"* The majority, 66% indicated that morale had declined, while 29% indicated no change. This result is not unexpected based on staffing reductions, lower compensation, lack of training and other operational impacts discussed earlier in the study. Even with the decline in morale, 61% indicated that staff performance had not changed and in fact 23% indicated that it had actually improved in spite of the economic situation.

"Significant pressure to improve operational efficiency of existing staff and systems to enable support of an increasing customer base with the same (or potentially fewer) resources as we have today.'

- Anonymous Survey Respondent

Area Affected	Improved	Declined	No Change
Staff Morale	5%	66%	29%
Staff Performance	23%	16%	61%
Average %	14.1%	40.9%	44.9%

FIGURE 7–HOW HAS THE DOWNTURN IMPACTED STAFF MORALE AND PERFORMANCE?

Impact on Service Revenues

When asked, *"How did the downturn impact your service revenues"* 40% indicated that revenues did decline, while 28% indicated no change. This is easily explained based on the premise that service revenues typically lag new product sales. This decline started back in 2008 and is now having a noticeable impact on service revenues. The minority of respondents, 24% indicated that revenues had actually increased, which may be attributed to the fact that while new product sales are down, customers recognize the need to maintain and access service and support for the products they already own, thereby protecting the technology investments previously made.

FIGURE 8– HOW DID THE DOWNTURN IMPACT YOUR SERVICE REVENUES?

Looking Forward to 2011 and Beyond

As can been seen from the survey results so far, the economic downturn had a significant negative impact on the majority of service operations. Overall, service revenues declined, consequently budgets were cut and reductions in personnel and operations were made that affected staff morale. Somewhat surprising is the fact that customer satisfaction rates remained unchanged, which is a testament to the dedication of the service teams ability to do more with less. However, this situation will be difficult to sustain over a long period. The second part of the study was intended to formulate a perspective from service leaders on their outlook and plans for 2011 and beyond.

"We acknowledge that the world has changed permanently for our customers and that the outcomes they require demands more from us in terms of value for money…"

- Anonymous Survey Respondent

Economic Outlook for 2011

Participants were asked *"Looking forward to 2011, how do you see the economic environment changing?"* There appears to be a cautious optimism among respondents, with 54% foreseeing improvement for their organizations. A further 23% didn't know and 16% didn't anticipate any changes. Indications from Wall Street during the last quarter of 2010 also show positive signs of economic recovery, though the high unemployment rate continues to represent a major concern.

FIGURE 9– LOOKING FORWARD TO 2011, HOW DO YOU SEE THE ECONOMIC ENVIRONMENT CHANGING?

Budgeting for 2011

Respondents were asked "W*hat changes do you estimate in your overall operating budget for 2011?*" The majority, 45% plan on an increase, where 30% expect their budgets will stay the same. There were still a significant number, 25% that anticipate a further decrease in their budgets, which indicates that their market sector has yet to experience signs of a recovery.

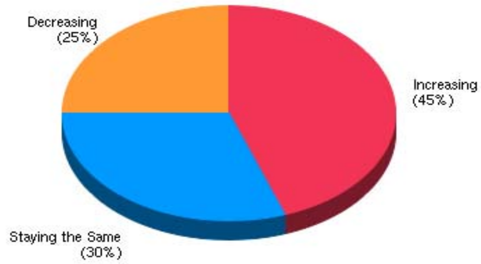

FIGURE 10– WHAT CHANGES DO YOU ESTIMATE IN YOUR OVERALL OPERATING BUDGET FOR 2011?

Maintenance and Support Revenues in 2011

Respondents were asked *"What changes do you estimate in your maintenance and support revenues in 2011?"* The majority, 55% anticipate an increase, where 33% expect service revenues to stay the same as the previous year. Only 12% predict a decline. Overall, the results indicate a positive trend, which infers that product revenues must also be growing thus creating more opportunities to sell service contracts. Generally when this happens, companies are more willing to invest in their service operations to retain existing customers and build loyalty.

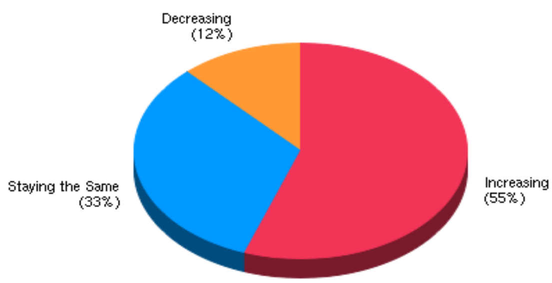

FIGURE 11– WHAT CHANGES DO YOU ESTIMATE IN YOUR MAINTENANCE AND SUPPORT REVENUE FOR 2011?

Operating Budget Allocation for 2011

Respondents were asked *"What is your budget outlook for the following areas in 2011?"* An encouraging sign was that 48% indicated increases in staffing levels followed closely by investments in staff training. Management training, compensation adjustments and travel weren't expected to be changed from 2010 levels. A slight majority, 52% anticipate an increase in service improvement projects as well as some investment in service tools and technologies. Overall, the results provide another positive indicator that companies are forecasting growth in 2011 and are willing to reinvest in their service operations.

Forecasted Changes	Increasing	Decreasing	No Change
Staffing Levels	48%	16%	30%
Staff Training Investments	46%	7%	35%
Management Training Investments	30%	9%	43%
Compensation Levels	29%	3%	48%
Authorization to Travel	25%	17%	52%
Service Improvement Initiatives	52%	2%	32%
Tools and Technology Investments	41%	8%	37%

Figure 12 – What is your budget outlook for the following areas in 2011?

Top Initiatives for 2011

Respondents were asked *"Describe the top three initiatives your operation is planning in 2011?"* Optimizing processes at 75% is clearly an imperative for service executives. They view such initiatives as a way to streamline operations in an effort to handle existing service demand with current staff resources. In addition they understand the importance of increasing the technical expertise of the staff through training and by investing in Knowledge Management systems as indicated by these initiatives being selected by 60% and 54% of respondents, respectively. Service leaders have also realized that product quality has a significant impact on service demand (47% selected this initiative) and that by participating in the quality assurance process, their organization can help to eliminate unnecessary service requests and contain service costs.

Increasing the adoption of existing online services, which is a key to driving greater usage of self-service options and deflecting service demand, was selected by 47% of respondents. Another 33% indicated that implementing new online services was a major initiative for 2011. The decision to outsource service workload offshore to low cost global regions or to local third party vendors is still top of mind for many service leaders. Even companies that already use outsource providers are reevaluating their options on an annual basis to ensure service objectives are being meet in terms of quality and value.

Top Initiatives for 2011	Percentage
Optimize Existing Processes	75%
Increase Technical Expertise of the Staff	60%
Implement Knowledge Management Initiatives	54%
Improve Product Quality to Reduce Demand	47%
Increase Adoption of Existing Online Services	47%
Implement New Online Services	33%
Offshore More Work to Low Cost Regions	17%
Outsource More Work to Third Party Providers	15%

Figure 13– What steps are you taking to improve your service operation in 2011?

Respondent Commentary

Respondents were asked to provide commentary based on the question *"Do you have any additional comments on how your organization will adapt to the changing economic environment?"* Provided below is a selection of the most pertinent comments, which have been grouped by "Theme." The themes include "*Execution and Strategy", "Increased Efficiency", "Improved Customer Focus", "Resource Management and Development"* and *"Survival."*

Theme - Execution and Strategy

- ✓ *"The open source software movement continues to chip away at proprietary software development practices and procedures. Realization of this fact needs to be embraced and understood before it's too late."*
- ✓ *"We acknowledge that the world has changed permanently for our customers and that the outcomes they require demands more from us in terms of value for money. We need to tailor our offerings to reflect this, such as offering cloud based services and online service options."*
- ✓ *"This is the time to ensure that we have the right services and focus on the execution of such. Our challenge will be to increase our revenue in light of these tight economic times, but [we] will do so by providing excellent value and helping our customers save money and time."*
- ✓ *"Based on the great people from the top down and past experience I am confident that the right improvements will be implemented to ensure we are a sustainable business into the future."*
- ✓ *"Reappraise approach to different market segments. Reorganize along technical, rather than geographic, lines."*

Theme – Increased Efficiency

- ✓ *"We will increase our focus on streamlining processes and improving tools, but our product serves as a significant cost-saving tool, so our forecasts are likely to thrive in a poor economy."*
- ✓ *We will continue to utilize our global systems and teams to provide high quality support in the most efficient means possible."*
- ✓ *"Do more with less - driving efficiencies and quality to realize better satisfaction levels."*
- ✓ *"Continue to look for new markets and opportunities, strengthen our current offerings, and look for ways to work more efficiently through the downturn."*

Theme – Improved Customer Focus

- ✓ *"Create the expectation of our customers that we will enhance their quality and production by using our services. And then prove it."*
- ✓ *We acknowledge that the world has changed permanently for our customers and that the outcomes they require demand more from us in terms of value for money. We need to tailor our offerings to reflect this, such as offering cloud based services and online service options"*
- ✓ *"Since the economy has an effect on everyone, we need to take a stance that we are stronger and have a higher level of customer satisfaction to grow our market share."*
- ✓ *""We are continually focused on further investment in Service & Support to help increase sales."*
- ✓ *"Continue to look at customer satisfaction to grow the business in the tough times"*

Theme – Resource Management and Development

- ✓ *"We have done more resource sharing across support, services and development for staff augmentation."*
- ✓ *"Need to closely watch customer demands and their impact on our resources."*
- ✓ *"As a Company, we believe our people are our greatest asset. We plan to continue with merit increases and bonuses for 2011. We also believe the economic challenges are temporary - they always are."*
- ✓ *"Let's hope this does not last too long, otherwise managing Burn Out will become an issue very quickly."*
- ✓ *"Outsource more "low-complexity" work to delivery partners (at lower costs) to free up higher skilled internal resources to take back other (more complex) activities that were delivered through partners before."*

Theme - Survival

- ✓ *"Financials were hit hard, and all but the big boys stopped buying. We used this time to eliminate the bottom 10 % workers, and align organizations better for the expected upswing. We feel we are much leaner, much meaner coming out of this."*
- ✓ *"Significant pressure to improve operational efficiency of existing staff and systems to enable support of an increasing customer base with the same (or potentially fewer) resources as we have today."*

- ✓ *"Developing a contingency plan based on a double dip recession and the impact to our customers, which will have an impact to the services team."*

- ✓ *"Continue to review and adjust the plan quarterly based on current information, sales pipelines, customer feedback."*

- ✓ *"Expenses have already been cut to the bone. As the economy and revenues improves I do not see the company allowing expenses to increase. The increased profit will be used to increase earnings per share."*

Conclusion

We compared the results of the *2009 Service Industry Outlook* study with the 2010 findings. From this it was evident that the situation for majority of service operations had worsened. Staff reductions, further budget cuts and declining service revenues have placed a tremendous pressure on organizations to "do more with less." However, throughout this period customer satisfaction rates have held steady, which is a testament to the dedication and commitment of the service teams and their management. Unfortunately, under resourced service operations cannot function at this level indefinitely without experiencing some degradation in customer satisfaction and a level of staff "burnout."

The second part of this study examined the outlook that service leaders had for 2011 and beyond. These results were far more encouraging and the best way to summarize their opinion would be to say they are *cautiously optimist*. Most indicated that they would be able to increase staffing levels as well as invest in training. The service improvement programs that were on hold have been initiated again along with some level of investment in new technologies. While we may not see an immediate return to the "good ole days," that existed prior to 2008, the lessons learned during these economic times can be applied in the long term and thereby help organizations become more efficient and deliver high-quality service to their customers.

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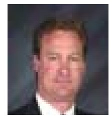
John has more than twenty years of software engineering and service industry experience. He has significant international experience from working in both the Asia-Pacific and European regions. In addition to his support management knowledge, John has a well-rounded background from managing engineering, quality control, and training organizations. He successfully re-engineered a number of large support operations – increasing their efficiency and elevating their service to world class. He has also developed RFP's for selecting support automation technology and managed the implementation of the tools, creating a quick return on investment for support operations.



Greg Coleman
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Greg has over twenty years of experience in the high technology service field. As a principal partner and vice president of strategic programs for Service Strategies Corporation, Greg was instrumental in developing the Service Capability & Performance (SCP) Standards, including the SCP Support, Field Service, Professional Service and eService Standards. Greg has worked with industry sponsors and participating companies to deploy the standards globally and has conducted in depth certification audits and consulting engagements with leading technology service organizations around the world.

About Service Strategies Corporation

Headquartered in San Diego, CA, Service Strategies advances service excellence by providing industry standards, training, certification and consulting services that ensure delivery of consistent, high-quality technology service and support. Service Strategies applies a proven benchmark process to its programs that measures and drives effectiveness for continuous service improvement. Service Strategies' programs help improve the service and support operations of leading technology companies worldwide.

The world's leading service and support providers use Service Strategies' Service Capability & Performance (SCP) Standards as a roadmap for service excellence and a qualitative and quantitative measure of success. Contact us for more information.

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