INFORMATION PAPER

Managed services:
Freeing-up IT to focus on core business

Introduction

TECHNOLOGY INFRASTRUCTURES ARE BECOMING INCREASINGLY COMPLEX AS PRODUCT FEATURES PROLIFERATE AND BUSINESS LINES DEMAND MORE CAPABILITIES AND INTEGRATION ACROSS NETWORKS. AT THE SAME TIME, IT RESOURCES ARE BEING SQUEEZED AS DOWNWARD PRESSURE ON COSTS CONTINUES. TODAY'S TECHNOLOGY ENVIRONMENT PRESENTS SIGNIFICANT CHALLENGES TO CIOs AND THEIR TEAMS AS THEY MANAGE NEW RELEASE SCHEDULES, MONITOR PERFORMANCE, ENSURE THE REQUIRED LEVELS OF AVAILABILITY AND MEET BUSINESS TEAMS' DEMANDS.

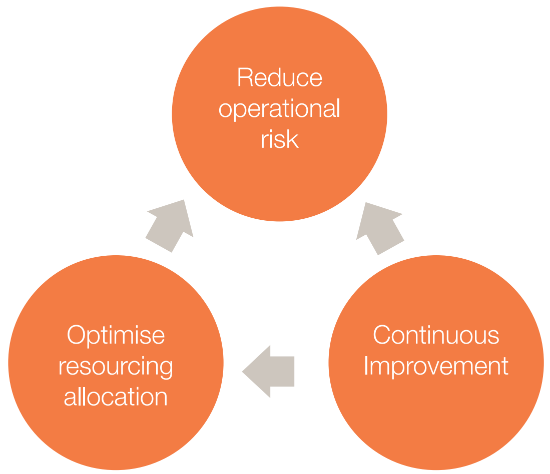
The traditional, in-house management of IT infrastructures is fast becoming prohibitively expensive; an alternative is urgently required. During the past few years managed services and operations have grown exponentially as companies seek greater predictability in their IT budgeting, reduction of operational risk and the ability to better exploit the advanced features of today's technologies.

What are managed services?

Managed services, or managed operations, are the practice of day-to-day technology being managed by third parties on behalf of the customer. There could be a number of reasons to do this, including reduction of the total cost of ownership (TCO) of technology, the acceleration of the return on investment in next generation technology, loss of expertise or an unwillingness to invest in building expertise in non-core technology.

Operational drivers include the reduction of operational risk, desire for continuous improvement of operations and the optimisation of resourcing allocation.

Figure 1: Operational drivers for managed services



Within managed services there are five main areas of activity:

- **Monitoring notification**: A managed services provider assists customers to operate their own technology. They do this by keeping a proactive eye on the performance of the applications in the infrastructure and notify the customer when the technology is not performing optimally or there is a serious degradation in performance. This is a typical entry-level agreement for managed services.
- **Operations**: In this scenario, a services company manages the technology operations on behalf of the customer. The managed services provider will undertake incident, problem, change and configuration management for the client. Along with monitoring notification, these two areas have for the past eight years been the main managed services activities.
- **Optimisation**: These services used to be offered via professional services teams. This activity recognises that IT infrastructures are constantly changing, are software centric and there is considerable interdependency; the performance of one area of the network could affect the performance of applications elsewhere on the network. There is a need to constantly optimise the environments in a holistic way. Managed services providers will monitor networks on a real-time basis and optimise IT performance when they identify any problems.
- **Transformation**: Managed services providers can also transform environments in order to enable their clients to move to the next generation of technology. The provider will transform the environment, and then manage it for the client. This is a high growth area for managed services.
- **Managed everything as a service (XaaS)**. A cloud computing term, XaaS refers to services that are delivered over the internet, rather than provided locally or onsite. Common examples include software as a service (SaaS), infrastructure as a service (IaaS) and platform as a service (PaaS). A conventional XaaS implementation involves a client subscribing to particular services but maintaining the responsibility for operations, system changes etc. Under the managed XaaS model, however, the provider takes over responsibility. Technology companies, for example, will bundle product with services such as implementation, integration and the day-to-day management of the solution. This is usually provided on a-per unit, per month basis.

The providers' perspective: data reveals take-up trends

The uptake of managed services has risen rapidly as companies deal with increasingly complex IT operations at the same time as delivering on demanding business objectives. Managed services eliminate onerous tasks that provide little business value and free-up IT operations to play a more integrated role in core business activities.

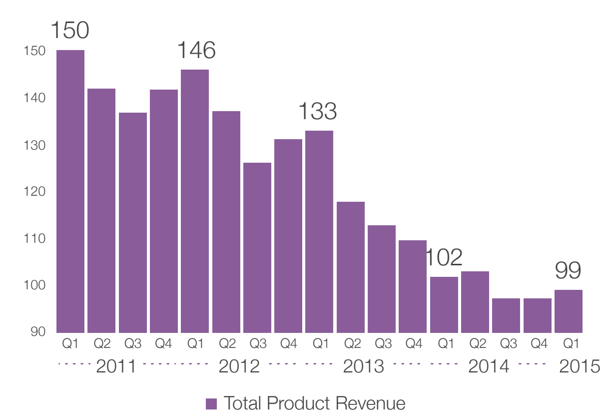
This shift towards a different model of IT operations is clearly demonstrated by figures from the Technology Services Industry Association (TSIA) that plot the rise in services revenues versus the drop in product sales. TSIA is an industry body that collects detailed operational and financial data from hundreds of technology services organisations. One of their studies compares the performance of 50 of the top technology companies, publishing the results in the TSIA Service 50. Since 2011 there has been a loss of more than $118bn of product revenue from the technology industry, while conversely there has been substantial growth in services revenues[1]. By the end of 2014, all services revenues (which grew by 2% that year) were greater than product revenues. Of those, managed services revenues grew by 39% on average. Managed services revenues have been growing almost 20 times faster than the services market as a whole. Of those, managed XaaS revenues grew 120% from 2013-2014.

ITIL IS A SET OF PRACTICES FOR IT SERVICE MANAGEMENT THAT FOCUSES ON ALIGNING IT SERVICES NEEDS WITH THE NEEDS OF BUSINESS. IT DESCRIBES THE PROCESSES, PROCEDURES, TASKS AND CHECKLISTS FOR ESTABLISHING INTEGRATION OF IT WITH AN ORGANISATION'S BUSINESS STRATEGY.

Other companies have also attempted to quantify the growth of the managed services market. New York-based technology research and advisory company, 451 Research, estimated the managed cloud market at $17 billion in 2014 and set to grow to $43 billion in 2018, a CAGR of 25.6% . Managed cloud services will account for 36.3% of the total cloud market revenue in 2018. The company also found that managed services revenue was growing 60% faster than infrastructure-only revenue.

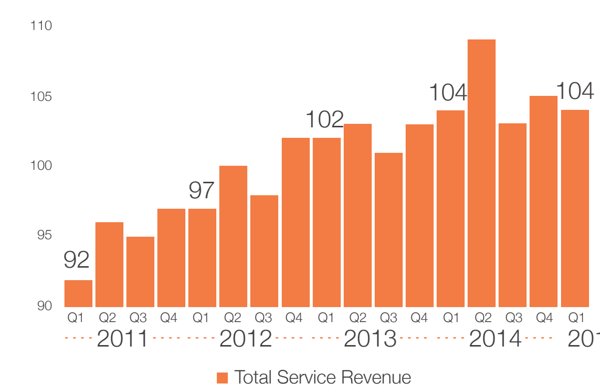
One of the main trends in managed services is a move towards greater standardisation. Historically, managed services have been highly customised, with the scope of work defined for individual clients. This is now changing. The TSIA has found that providers are increasingly aligning the Information Technology Infrastructure Library (ITIL) with a standard service catalogue. At the beginning of 2014, only 22% of the managed services members at TSIA had implemented a standard service catalogue for their managed services offers; by early 2015, 39% had a standard offer catalogue.

Figure 2: S50 Product versus Services Revenue Q1 20111-Q1 2015



2011=$517B 2014=$399B

S50 Services Rev Q1 2011 – Q1 2015



2011=$388B 2014=$421B

SOURCE: TSIA

[1] *Market Monitor: Cloud Computing – Worldwide managed services, 2014-2018, 451 Research, March 2015*

Greater standardisation may make it easier for clients to change providers, however, with renewal rates of 91-92% in the industry; it seems clients are happy with their providers and the predictability of IT costs that they offer.

The other significant trend in managed services is the rapid growth of the managed XaaS model. According to the TSIA, the managed XaaS model now represents 34% of the managed services revenue of more than 40 different providers. The same data also show customised, on-site revenues eroding as a percentage of all managed services revenues.

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Drivers of managed services adoption

The rapid growth of managed services has been driven by the confluence of a variety of trends. The continuing rise in the technical complexity of technology solutions, the network dependency of applications and infrastructures, and the mobile workforce environment have all combined to create significant challenges for IT departments.

Figure 3: Challenges faced by companies

As a result, for many organisations, operating expenses have got "out of control" and gaining funding for IT requirements, such as training and bringing in new talent, is extremely difficult, says George Humphrey, senior director of managed services research at TSIA. Indeed, he says the converse is happening, with IT budgets slashed and resources downsized. As technology solutions become more complex, organisations need better tools and applications to monitor performance and integration levels, automate event correlation, undertake remediation and filter the multiple events feeding into the infrastructure. "We are seeing a massive rise in complexity as budget dollars are being taken away that are needed to deal with this complexity," says Mr Humphrey. "Many firms are out of options, which is one of the reasons they are turning to managed services providers."

By turning to managed services providers, organisations can build more predictability into their IT budgets and into the reduction of operational risk. And by enabling customers to shift their resources to focus on their core business, customers are better placed to take advantage of new technologies as they appear on the market.

TSIA figures demonstrate that customers are voting with their wallet when it comes to procuring technology. Within the membership of the TSIA, data shows that some of the younger managed services businesses are experiencing revenue growth of 150-200%. Average growth rates are 30-40% per year.

Humphrey describes managed services as "the way of the future", with many organisations no longer able to carry the risk of operational complexity on their own shoulders. Instead, organisations want to enjoy the benefits of what new technologies can offer but transfer the risk of operating such systems on to the manufacturer, system integrator or global services company.

Managed services in the financial services industry

The acceptance of managed services as a way to manage IT infrastructures has not happened overnight. Outsourcing in the financial services industry has slowly evolved, with initial reluctance on the part of firms to hand over responsibility for any activity to a third party. Initial outsourcing offerings tended to focus on outsourcing the entire IT operations, which was worrying for many financial services companies.

In financial services, technology performs tasks that are critical to performance; system outages or data breaches can result in serious damage to a firm's reputation. Financial institutions have to take into account questions of security and regulatory compliance when mulling over a move to managed services.

As outsourcing evolved into managed services, providers have become more intimately engaged with clients and therefore have gained a better understanding of the individual business lines that are served by the technology infrastructure. The moves towards standardisation of service level agreements and documentation have helped to give confidence to financial services firms when deciding to opt for managed services.

"One of the initial reasons financial institutions were reluctant to move to managed services and outsourcing was that many felt no one else could manage their technology infrastructures better than they could," says Mr Humphrey. "Moving any aspect of operations to a third party was deemed to be a risky prospect. However, as many financial institutions have had data compromises they now realise that securing and protecting customer data is increasingly complex and that they need help."

The security issue is being addressed by specialist managed services providers that take on risk, designing, implementing and managing solutions that secure financial services businesses. An important aspect of this is that these providers also take on the financial risk in the case of a security breach.

In addition to ensuring security, financial institutions also have to ensure maximum uptime and performance from their technology infrastructure. Billions of dollars can be on the line if systems fail. Mr Humphrey paints a vivid picture of the cost of system failure: "One of the top internet services providers had a 32 second outage during one Christmas. This cost the firm $32 million – that's $1 million per second."

A view from Asia

For many years in Asia, particularly in China, financial institutions were able to employ large numbers of IT staff because their revenues were growing rapidly and the cost of labour was relatively low. However, labour costs are now rising and banks are facing more challenges in terms of driving revenues. At the same time, says Zennon Kapron, co-founder and director at research and consulting firm Kapronasia Shanghai, managed services offerings in the region have matured and bank attitudes have changed.

A former CIO for Citigroup Portugal, Mr Kapron has more than 20 years' experience in the finance and technology sectors and has lived in China for the past 10 years. While at Citi, during 1998-2005, he was involved in outsourcing projects. Banks' uncertainty about outsourcing has not changed much since that time, he says. "During the five years I was at the bank, global network connectivity was outsourced, then insourced, then outsourced again. This was fairly typical and was very costly."

While attitudes towards outsourcing may not have changed, technology has – and the ability to leverage cloud computing in technology and operations is a game changer, Mr Kapron says. Managed Services offer a level of security, predictability and efficiency that previous approaches did not provide.

"A decade ago, if a financial institution wanted to have its network or services managed by an external provider, it would have to clearly define what it required, in terms of computing power and resources, from the very beginning," he says. "Now there is the possibility of leveraging cloud computing platforms that can scale with the business, whether institutions use the platforms directly or via a managed services provider." Mr Kapron also says there has been a "natural evolution" as financial institutions become more comfortable with a new approach to managing their products and services. "Managed services offerings are more secure, more sophisticated and the providers are more stable in the market."

This growing confidence means that decisions about what to keep in-house and what to let others manage – typically characterised by questions about what is 'core' or 'non-core' to a financial institutions' operations – are changing. An illustration of this growing confidence in cloud and managed services, says Mr Kapron, is Chinese private bank Mybank, a part of Ant Financial, the online payment service spun out of China's Alibaba in 2011. Ant Financial built MYbank on its existing infrastructure, using open source systems. The banking system was then put on Aliyun, Alibaba's cloud, and offered as a service to other banks, says Kapron. "There is no concept here of core or non-core, pretty much everything is available as a service. It demonstrates a different mentality when it comes to managed services."

The future for managed services

Many believe that managed XaaS will be a 'megatrend' for the foreseeable future. The providers that do the best will be those that combine unique product capabilities with unique services capabilities that are focused on specific business outcomes for their clients.

In addition, TSIA's Humphrey expects to see more advances made in the area of standard services catalogues. This will ensure that clients understand what they are getting when they sign up to managed services. Alongside a standard services offering, customisation will also occur; for example, onsite service desk resources should be delivered in the native language of the country in which the client is based.

He also believes that service automation and a machine-to-machine intelligence platform for managed services providers will emerge. This will enable event correlation and remediation to be automated, monitoring security and removing as much of the human factor (and therefore errors) as possible.

Managed services have been described as a "locomotive that has left the station and cannot be turned around". There are many different flavours of Managed Services, but one thing is clear, they are on the increase. Determining what the right balance of managed services is for a business is a complex, but critical, question.

The growing popularity of this option will be further driven by the desire of financial institutions to refocus on their core business activities and to move to a model of predictable costs and scalable resources. In doing so, they will be able to reap the benefits of the increasingly complex IT environment without shouldering the burden of that complexity in their operations teams.

Managed services in practise: the SWIFT environment

The evolution of managed services has not only offered new IT sourcing alternatives (in addition to in-house IT and cloud options), it has also broadened the number of financial institutions willing to consider whether having certain functions managed by external providers and has triggered a more serious examination at individual banks of what is core and non-core to their operations. And in the risk-averse financial industry, the monetary aspects are sometimes only secondary when compared to questions of minimising operational risk or data privacy. For example, although some financial institutions are technically ready to move towards cloud solutions, they sometimes are not willing to take this direction due to constraints imposed either by local regulation or their own IT and security policy, which mandates that data be stored locally on their premises.

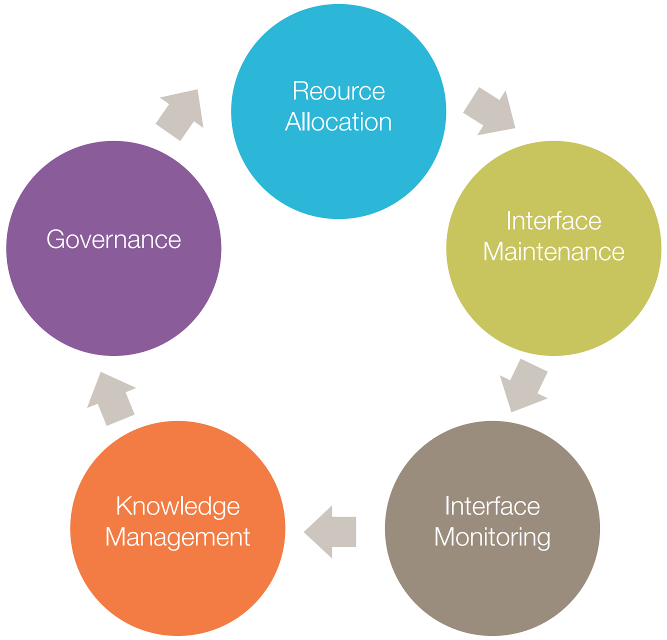
This is where Managed Services can offer financial institutions the right balance between complying with data privacy regulations and decreasing operational risk all the while relieving them of non-core activities.

These challenges faced by financial institutions were the main driver for SWIFT to investigate the possibility of providing Managed Services towards its customers. The result is SWIFT's first Managed Services offering, Alliance Managed Operations, whereby SWIFT customers are already opting for managed services as a way to manage their SWIFT environments in an increasingly resources constrained environment.

SWIFT CUSTOMERS THAT HAVE TAKEN UP (OR ARE CURRENTLY LOOKING INTO) SWIFT'S MANAGED SERVICE OFFERING, ALLIANCE MANAGED OPERATIONS (AMO), ARE TYPICALLY BENEFITTING FROM A 22-38% REDUCTION IN YEARLY TCO, EVEN AFTER FACTORING IN THE COST OF THE AMO SERVICE. WITH REGARDS TO THE ONE-TIME COST REQUIRED FOR SETTING UP THE SERVICE, CASH BREAK-EVEN IS TYPICALLY ACHIEVED WITHIN ONE YEAR.

The uptake of AMO is driven by a number of challenges, mainly faced by small to medium sized financial institutions, in managing their SWIFT environments with their existing IT team (i.e. SWIFT interfaces being added to their countless non-SWIFT IT responsibilities). These are:

Figure 4: What is driving uptake of AMO?

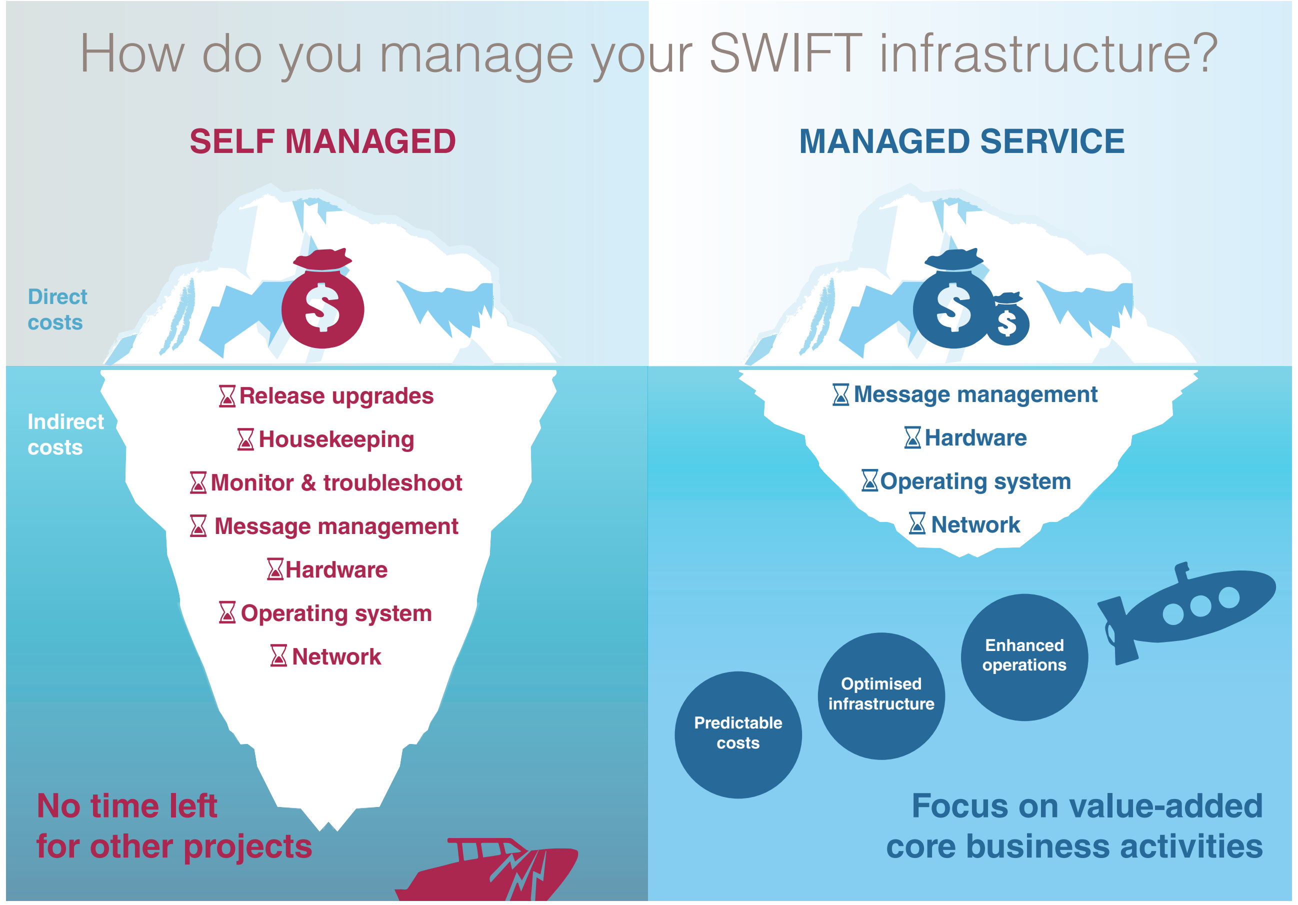


- **Resource Allocation**: IT budgets have declined and staff are already stretched with maintenance of other core-business applications
- **Interface Maintenance**: with time and IT resources stretched, delays in housekeeping operations and change management become more frequent, representing higher operational risks
- **Interface Monitoring**: The SWIFT environment comprises many components and critical flows that require adequate monitoring and follow-up
- **Knowledge Management**: The management of interfaces requires in-depth technical knowledge and many IT teams do not enough resources to allocate time for keeping up-to-date with the changes in external applications
- **Governance**: Supporting complex infrastructure environments across multiple business lines means that roles and responsibilities are often not clear cut and accountability is shared across numerous teams. This can create oversight gaps and lead to operational risk.

When banks employ managed services, this does not necessarily mean wash their hands of all operational activities. SWIFT research has identified a number of areas over which customers want to retain control or influence: business impact analysis; knowledge of the Alliance suite; relationship between the business lines and IT department; awareness of processes; and internal flexibility.

But within the overall SWIFT environment, there are many activities that can be handed over to a remote SWIFT team, covering all the operations and infrastructure, monitoring, troubleshooting, maintaining, patch/releases installations etc that apply to the SWIFT environment. This greatly reduces the burden on IT departments, freeing them up to focus on their core business and on areas that may generate competitive advantage while benefitting from predictable costs, an optimised infrastructure, and enhanced operations.

Figure 5: Hidden costs of in-house IT



SWIFT has carried out detailed cost-benefit analysis of managed services among its customers, comparing the total cost of ownership (TCO) for customers managing the full SWIFT environment themselves with or without the Alliance Remote Gateway (ARG)[2], and with or without the AMO service. The most impressive results were gained by customers that moved to AMO with ARG. Indeed, the AMO + ARG model enables customers to transfer daily monitoring operational tasks to SWIFT, reduce the number of components to be monitored and enables more time for project management and

coordination. At the same time, customers still benefit from peace of mind, knowing that SWIFT experts will address any issues as they arise. As well as optimising infrastructure and processes, SWIFT undertakes change management and monitoring, greatly freeing up customers' IT resources.

The extent of the operations that can be performed by SWIFT on behalf of the customer in an ARG + AMO scenario means that the resources historically allocated to managing the SWIFT environment could be freed-up – sometimes up to a full time equivalent (FTE) reduction from 4 to 1.75 – and allocated instead to managing core-business projects. In the end, AMO is not just about having SWIFT perform operations on behalf of the IT team, it's also about allowing the IT team to provide more added-value to the business without needing to hire additional staff; a welcome benefit for customers in these tumultuous and resource-constrained times.

[2] ARG is a hosted service operated by SWIFT, which allows customers to connect Alliance Access/Entry directly to the SWIFT network without the need for the customer to manage its own Alliance Gateway, SWIFTNet Link and Hardware Security Modules (HSMs).

AMO in action: Aktia

In 2012, Finnish bank Aktia opted for managed services when it experienced a significant increase in its SWIFT payments volumes, following the establishment of the Single Euro Payments Area (SEPA). The bank had only one SWIFT expert on its payments team and when the expert left the bank, it needed to find a replacement. Analysis by the bank's payments and IT teams identified a number of challenges: insecurity about the operational health of their SWIFT infrastructure, lack of detailed SWIFT knowledge and resources in-house, low management awareness of the criticality of SWIFT systems, no on-going adoption of best practices related to SWIFT systems, and unclear roles and responsibilities between payments and IT departments. The teams worked together to identify not only the short-term lack of SWIFT expertise, but to address a longer-term strategy for managing the operations of the SWIFT systems.

Aktia asked SWIFT to perform a detailed review of its SWIFT architecture model, as well as related processes, costs, skills and effort required. SWIFT was charged with providing a comparison of in-house and outsourcing options based on criteria including staffing, cost, impact on business operations integration and Service Level Agreements (SLAs). The study also included a high-level assessment of the infrastructure and identified areas for improvement.

"We chose SWIFT Services because we knew we'd be dealing with SWIFT experts, not generalists who lacked detailed SWIFT knowledge," says Niklas Lemberg, head of payments at the bank. "We appreciated the fact that SWIFT experts took the time to understand our needs and provided a detailed analysis with concrete and objective recommendations."

Aktia opted for Alliance Managed Operations and SWIFT now performs continuous, real-time monitoring of the bank's SWIFT environment. As part of a systematic and long term engagement with the customer, SWIFT experts automatically start investigating any problems which may arise and manage Aktia's Alliance interfaces through regular housekeeping activities and installation of mandatory patches. "Alliance Managed Operations is definitely the right solution for our needs," says Mr Lemberg. "It has enabled us to maintain control over our infrastructure and focus on core business activities while handing over day-to-day management of our Alliance interfaces to the experts at SWIFT."

As a result of AMO, Aktia has been able to save the equivalent of one FTE. "We are so pleased with AMO that we now plan to also implement ARG during 2016, as this will help to further reduce TCO," says Mr Lemberg.

Being at the heart of the financial industry, we understand your business challenges and opportunities to grow. A changing landscape, adhering to regulation, reducing costs, streamlining and ensuring your operations, improving your customer's experience or developing your staff to the level you need. These are challenges SWIFT has been supporting you with since 40 years. Building on that experience, SWIFT has today a wide team of experts at your service to offer you the highest quality of training, consulting and operational services, tailored to your needs. SWIFT Services experts keep you going, resolve your issues and propose improvements where seen. SWIFT Services – expertise from the source, tailored to your needs.

For more information please contact your SWIFT account manager or visit www.swift.com/services

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