



## Forecast Analysis

# North American IT Staff Augmentation Projections: 2000-2005

**Abstract:** *The North American IT staff augmentation market is expected to climb from \$23.4 billion in 2000 to \$24.3 billion in 2005. This year the market is expected to drop 0.8 percent to \$20.7 billion.*

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### Strategic Planning Assumptions

By 2005, 40 percent of North America-based IT staff augmentation vendors will have offshore capabilities either through their own facilities or through partnerships with offshore vendors (0.7 probability).

By 2005, 20 percent of the Fortune 1000 will outsource their IT staff augmentation procurement processes to a third-party vendor management system operator (0.6 probability).

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## Is the Worst Behind Us?

As was the case with virtually every sector of the IT market, the North American IT staff augmentation market was hit hard by the unexpected reduction in demand for e-business services and the economic recession that engulfed the United States in 2001. This reduction in IT spending resulted in many IT staff augmentation vendors realizing at least a 10 percent decrease in revenue in 2001 — one of the worst years in the history of the IT staff augmentation market. With 2001 past, one question remains: Was 2001 an aberration or is more bad news on the horizon for this market segment? IT appears as though the worst is over; however, growth for the remainder of 2002 and 2003 will likely remain anemic. By the end of 2004, this market is expected to post a healthy rebound growing 6.2 percent. Even so, the growth is well below the double-digit rates experienced before 2001.

## IT Staff Augmentation Defined

To avoid confusion between the meaning of IT staff augmentation and IT services, Gartner Dataquest's definition that differentiates staff augmentation from IT services is as follows:

- Staff augmentation provides technical workers in a support capacity to IS organizations or end-user business units on a time and expenses basis. Typically, the client, not the supplemental staffing vendor, manages these people. Therefore, the staff augmentation company is not responsible for any pre-defined service deliverables. A vendor responsible for delivery of pre-defined IT services does not provide staff augmentation services.

There are two major classes of IT staff augmentation services. One class is equivalent to what Gartner Dataquest traditionally defines as IT professional services (IT consulting, application development, systems integration, education and training, and outsourcing). The second class is what Gartner Dataquest traditionally defines as product support services (hardware and software maintenance and support). The combination of IT professional services and product support services is referred to as IT services. This report provides projections for each major service segment as they relate to the IT staff augmentation market. Definitions of each major service line are as follows:

**Consulting Services** — Consulting services are advisory services to help companies analyze and improve the effectiveness of business operations and technology strategies. Consulting services include the following two subsegments:

- Business consulting services are advisory services that influence the adoption of information technology. Business consulting activities include corporate strategy planning, business plan review, business process analysis or re-engineering and business requirements analysis, as well as change management and organizational consulting pertaining to the adoption of IT solutions.

- IT consulting services are advisory services that help clients assess different technology strategies and align their technology strategy with their business or process strategy. These services support customers' IT initiatives by providing strategic, architectural, operational and implementation planning.
- Development and integration services — Development and integration services customize or develop IT solutions, assets and processes, and then integrate these solutions, assets and processes with established infrastructure and processes. Development and integration services implement designs conceived by consultants. Development and integration services include the following subsegments:
  - Application development services create new functionality for custom-developed or packaged applications. Application development frequently serves to integrate or link internal or external business processes. These services may include conversion applications to run on different platforms or architectures.
  - Integration services are detailed design, implementation and management services to link applications (custom or prepackaged) to each other or with the established or planned IT infrastructure. Specific activities may include project planning, project management, detailed design or implementation of application programming interfaces.
  - Deployment services support the implementation and rollout of new applications or infrastructure. Activities may include hardware or software procurement, configuration, tuning, staging, installation and interoperability testing.
- IT management services — Management services provide day-to-day management and operation of IT assets and processes. As such, they represent the core value components of IT outsourcing. Management services include the following subsegments:
  - Operational services transfer all or part of the daily system management responsibility for a customer's IT infrastructure (host/data center, client/desktop or connectivity/network), and in some cases the transfer of ownership of the technology or personnel assets to an outside vendor.
  - Applications management services provide a wide variety of services, processes and methodologies for maintaining, enhancing, and managing custom and packaged software applications.
  - Help desk management services provide centralized information and support management service to handle a company's internal queries and operational problems about IT-related processes, policies, systems and use. Services include hardware and software support, logging of problems, dispatch of service technicians or parts, training coordination, and other IT-related issues.
- Business process and transaction management (BPTM) services — BPTM services are a component of business process outsourcing (BPO).

BPTM includes transaction processing services that provide IT operational support for specific types of transactions, such as for credit/debit cards, payroll, check/bank and healthcare. BPTM also includes business process management services that provide business transformation knowledge and expertise applied as a part of a BPO contract. Examples of business processes that are outsourced to an external service provider include logistics, procurement, human resources, finance/accounting, customer relationship management (CRM) or other administrative or customer-facing business functions.

- **Hardware maintenance and support services** — Hardware maintenance and support services are preventive and remedial services that physically repair or optimize hardware, including basic installation, contract maintenance, and per-incident repair on-site or at a centralized repair depot. Hardware support also includes telephone technical troubleshooting and assistance for setup and all fee-based hardware warranty upgrades. Exclusive of parts bundled into maintenance contracts, sales of all parts used to repair high-tech equipment in carry-in, mail-in, or per-incident on-site delivery modes, or purchased by internal staff to perform the repair, are included. This segment includes only external customer spending on these services.
- **Software maintenance and support services definitions** — Software maintenance and support services include revenue derived from long-term and pay-as-you-go support contracts. Technical support contracts include telephone and online troubleshooting, installation assistance and basic usability assistance. Software maintenance includes delivery of product updates and enhancements excluding software maintenance provided under support contracts, custom software updates and major upgrades sold through nonservice channels. Software products and technologies covered under this category include operating systems; application software; and systems and network management software, tools and utilities.

The market forecast model used to produce these projections is available in "U.S. IT Staff Augmentation Market," PSEM-WW-DP-0101.

## Forecast Scenario

Table 1 contains North American IT staff augmentation services projections from 2000 through 2005. The services include IT consulting, application development, systems integration, education and training, hardware and software maintenance and support, and discrete outsourcing (management services, as well as business process and transaction management). Discrete outsourcing is defined as project-specific contractual arrangements with a predetermined scope of work to be completed within a given time period. Discrete projects may last a few weeks or several years, depending on the project. Business strategy consulting services are not included because staff augmentation vendors rarely provide them.

**Table 1**  
**Total North American IT Staff Augmentation Projections for 2000-2005**

	2000	2001	2002	2003	2004	2005
Consulting	5,485	4,837	4,940	5,298	5,613	5,997
Development and Integration	14,520	12,998	12,738	13,274	13,827	15,062
Education and Training	888	777	771	794	850	932
Management Services	815	818	746	777	889	847
Business Process and Transaction Management	653	704	630	498	678	509
Hardware Maintenance and Support	604	448	570	442	544	621
Software Maintenance and Support	457	239	264	269	277	291
<b>Total</b>	<b>23,421</b>	<b>20,821</b>	<b>20,659</b>	<b>21,352</b>	<b>22,679</b>	<b>24,259</b>

Source: Gartner Dataquest (September 2002)

## Dominant Market Accelerators

The following are dominant accelerators supporting growth in the North American IT staff augmentation market:

- **Optimization vs. transformation** — The economic slowdown in North America, combined with a need to demonstrate rapid return on investment (ROI) has created a wholesale shift in market requirements. Propelled by the disruptive nature of e-business, enterprises embraced the notion of competitive advantage through business transformation. With no disruptive technologies on the horizon, enterprises are beginning to take stock of their IT investments by looking to capitalize on past IT purchases. This includes fine-tuning and upgrading past investments.
- **Reduction in project size** — As the North American economy began to sour in 2000 and early 2001 and as costly e-business IT purchases often did not deliver the anticipated ROI, enterprises across all industries adopted a bread-and-butter strategy regarding IT purchases. Instead of purchasing large, all inclusive IT solutions, companies are purchasing small pieces of a larger solution and awaiting positive ROI before moving on to additional phases of the project.
- **Solutions for the small and midsize business (SMB)** — Enterprise resource planning (ERP) and CRM application suites are maturing, which provides demonstrable business benefit to those that have effectively implemented them (predominantly large enterprises). CRM and ERP success is tied to an appreciation of the required business process changes. For IT services providers, the opportunity lies in applying knowledge of lessons learned and best practices. This was not always the case, which helps explain why midsize enterprises were reluctant to embrace ERP and CRM. Typically, risk-averse SMBs lack the funds to experiment with new technologies and wait until a given technology is mainstream, and best practices have been identified and adapted to its industry before investing. They opt to wait patiently for larger enterprises to purchase, fine-tune, and derive business benefit from the technology before they enter a new market. Given the maturation of ERP and CRM technologies and associated

implementation methodologies, midsize enterprises represent another new class of buyers, which, in many cases has prompted larger ERP vendors to create applications specifically for this class of buyer. Other solution sets this segment is purchasing include security, networking, Web site design and development, e-commerce and data warehousing. Many also anticipate the need for additional hardware and software upgrades.

- **Build in-house** — The weaker economy has released into the market a wave of highly talented IT workers who frequently find employment in the internal IT departments of enterprises. As a result, many enterprises are deciding to use in-house resources for virtually all IT projects and supplement their resources with external contractors when needed. In other words, they are using more staff augmentation and less project-based services.
- **End-user demand** — According to Gartner Dataquest's annual User Wants and Needs survey of 59 enterprises published in early September of 2002 ("Consulting and Systems Integration Market in North America," ITES-WW-UW-0110), 51 percent stated that they are using staff augmentation services. The use of staff augmentation services was ranked second just behind application development services (58 percent) and ahead of packaged application implementation services (41 percent) offered by vendors specializing in project-based engagements.
- **Vendor on premises/vendor management systems** — Many IT staff augmentation vendors realize a new line of revenue by placing one or more of their employees on-site with a client to manage all of the client's IT staff augmentation needs. These needs include requirements gathering, contractor identification, interview scheduling and consolidated invoicing. Often the staff augmentation vendor also uses proprietary vendor management software designed to make the business process of identifying, qualifying and selecting a contractor more efficient. This is a form of BPO.

## Dominant Market Inhibitors

The following dominant inhibitors are hampering growth in the North American IT staff augmentation market:

- **Economically restrained budgets** — By far the largest inhibitor to growth in the North American IT staff augmentation market is the overall reduction in IT spending, particularly for IT consulting, application development and systems integration.
- **Offshore application development** — There continues to be a growing trend toward the use of offshore developers in countries such as China, India, Ireland, Israel and the Philippines. As the communications infrastructure in these countries improves, more application development will be outsourced because of cost advantages. Also, offshore service providers are taking advantage of their North American success and establishing onshore facilities to offer services that compete with North American staff augmentation vendors, often at lower prices.

- Other competition — Traditional project-based IT professional services providers as well as large enterprise software vendors increasingly are looking to increase their use rates by hiring out their idle resources to staff augmentation projects.
- Charge rates — The weaker economy has forced the hand of enterprises to seek rate cuts from their preferred staff augmentation vendors. Therefore, although the volume of staff augmentation work may be steady, the margins realized from delivering this work have been eroded which financially impacts a vendor's ability to launch sales initiatives, marketing campaigns and innovative R&D programs, or to hire needed talent.
- Buildup of internal staff — Given the flood of IT talent that is still circulating in the market, internal IT departments continue to build up their in-house talent pool. This in turn reduces their reliance on external service providers.
- Absence of technological innovation — No new disruptive technologies are on the horizon that will prompt a massive surge in the purchase of IT services. In the past, disruptive technologies, such as client/server, ERP and e-business, catalyzed sharp increases in services spending, largely to transform the manner in which companies conducted business. With no transformation technologies approaching quickly (Web services and mobile computing are still maturing), enterprises are focusing on how they can optimize their business processes.
- Lack of specialization — Professional service vendors are slowly catching on to the fact that enterprises of all sizes want service providers with proven capabilities in their industry. The ability to demonstrate vertical market expertise and business process knowledge is key to winning clients. Very few staff augmentation vendors have developed brand recognition for having expertise in a core set of business processes for one or more vertical markets.

## **Gartner Dataquest Perspective**

The North American IT staff augmentation market is emerging from one of its worst years in recent history, and it would appear as though this particular market may be entering a period of radical change. This change is fueled by the fact that major market inhibitors are anticipated to outweigh major drivers during the next 15 months. Barring any unforeseen sharp pickup in the U.S. economy, the IT staff augmentation space will most likely enter a period of consolidation to bring demand more in line with supply.

## **Gartner Dataquest Recommendations**

For established IT staff augmentation vendors looking to weather this storm, the following strategies must be taken into consideration to achieve future growth:

- **Offshore capabilities** — Aside from constrained budgets, the growth of the offshore services market, particularly in India, is perhaps the largest threat to North American based IT staff augmentation vendors. As such, Gartner Dataquest recommends that these vendors look to develop their own offshore facilities or partnerships with offshore services providers to meet clients needs. The use of offshore services providers is expected to continue to grow as more and more countries develop the skills and infrastructure to support these services.
- **Market specialists** — It is clear that end users across North America expect service providers to have a solid understanding of their industry and business processes. It is incumbent on the IT staff augmentation vendor to differentiate its capabilities through the creation and marketing of vertical market specific IT services. Past strategies of offering a broad set of horizontal IT capabilities to the market are being undercut by offshore providers offering identical services.
- **Vendor management systems (VMS)** — Most enterprises in North America do not have a formal strategy for identifying, qualifying, selecting and managing IT staff augmentation contractors. As a result, these companies spend excess money supporting a mosaic of fragmented business IT procurement processes. There is a need for VMS, and it is likely that more IT staff augmentation vendors will slowly have the entire IT staff procurement process outsourced to them as companies realize the savings from doing so. Vendors that have VMS, strategies will be in the best position to capitalize on this opportunity that is beginning to emerge in earnest in North America.

#### Key Issue

What is the market size and forecast for the IT services market?

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