

Service Performance Insight, LLC

The Impact of Digital Transformation on Independent Professional Services Organizations



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A Tale of Two Cities

Service Performance Insight's recently published 2021 PS Maturity™ benchmark portrays a tale of two cities - with the best run and best positioned independent professional services organizations surviving, even thriving through a year of pandemic-caused lock downs while the bottom 20% of firms experienced project cancellations, layoffs and losses. Based on survey input from 561 global professional services organizations a clear picture has emerged highlighting the very real benefits of digital transformation. In particular, the use and integration of Professional Services Automation solutions is a clear differentiator for top performing people and project-based organizations.

Figure 1 shows the maturity progression of 272 independent PSOs with the least mature, level 1 organizations, reporting abysmal results and significant losses. The PS Maturity™ model describes the least mature organizations as “heroic and reactive” because they do not have integrated business applications nor do they have standardized business processes or operational visibility. The level 1 “heroic” organizations are comprised of the lowest performing 73 independent firms. Because these reactive firms had anemic sales pipelines and almost no backlog when the pandemic hit in March, 2020 they were roiled by project cancellations and delays. Although they did their best to hold on to their valuable employees, without enough work, billable utilization and revenue per consultant and employee plummeted resulting in the largest annual loss ever reported in this benchmark. After the devastating year of 2020, the least mature independent firms are practically on life support. At the other end of the spectrum, the top 61 firms (Level 4 and 5 Maturity) reported excellent 2020 results with strong year over year revenue and headcount growth combined with superior billable utilization. These firms boast robust sales pipelines and consistent on-time project delivery leading to abundant work which produced high revenue yields and industry-leading profit.

Figure 1: PS Maturity™ Progression – 272 Independent Firms

	Level 1 Heroic	Level 2 Piloted	Level 3 Deployed	Level 4 Institutionalized	Level 5 Optimized
	73 Firms	65 Firms	73 Firms	50 Firms	11 Firms
Year-over-year change in PS revenue	8.4%	5.8%	4.3%	11.7%	16.9%
Year-over-year change in PS headcount	4.6%	2.0%	4.1%	9.9%	13.5%
Deal pipeline relative to qtr. bookings forecast	135%	164%	176%	205%	253%
Bid-to-win ratio (per 10 bids)	3.99	4.49	5.25	6.19	6.47
Employee billable utilization	54.6%	62.9%	76.9%	83.8%	85.7%
Projects delivered on-time	42.2%	75.5%	84.7%	92.2%	94.4%
Annual revenue per billable consultant (k)	\$50	\$135	\$214	\$277	\$289
Annual revenue per employee (k)	\$50	\$108	\$168	\$239	\$255
Profit (EBITDA)	-10.1%	3.0%	13.9%	16.8%	30.2%

Source: SPI Research, April 2021

What is most surprising about the 2020 results for independent firms is the fact that the bottom 20% are quite large firms, averaging 952 PS employees with annual PS revenues of \$135 million. The top 20% are much smaller, averaging 434 employees and annual PS revenues of \$67 million but they are far more productive with per consultant annual revenue yields of \$242K compared to only \$90K for the bottom 20%. With low billable utilization and low revenue per consultant, poor performers are not generating enough revenue to cover employee costs, let alone make a profit.

Trends

For this analysis, we focus on 272 independent IT and Management Consultancies and Marketing and Advertising firms. On average, these organizations employ 480 PS employees. 79% are headquartered in North America, 13% are headquartered in Europe and 8% are headquartered in Asia Pacific.

Table 1 shows key trends for independent firms over the past three years. Given the turbulent social, economic and political environment which characterized 2020, most independent consultancies performed quite well. Overall revenue and headcount growth were suppressed but still quite strong given the circumstances.

Table 1: Three-Year Trend - Independent Firms

Key Performance Indicator (KPI)	2018	2019	2020
Firms	269	239	272
Year-over-year change in PS revenue	10.9%	10.9%	7.8%
Year-over-year change in PS headcount	8.8%	9.3%	5.4%
New Logo Client % of Revenue	28.8%	28.2%	25.3%
Quarterly revenue target in backlog	43.8%	44.8%	42.2%
Employee Attrition	14.2%	14.1%	11.8%
Onsite service delivery	52.0%	48.5%	45.6%
Days sales outstanding (DSO)	40.4	42.9	40.4
Profit (EBITDA %)	16.1%	12.4%	13.3%

Source: SPI Research, April 2021

Although most key measures of performance were down in 2020, average net profit (EBITDA) increased year over year because firms reaped tremendous cost savings from no travel, no meetings, no meals and entertainment and lower facility costs. As the economy starts to recover in 2021, firms must reevaluate their previous lavish discretionary spending to determine whether it is really warranted in “the new normal” which will certainly be a much more virtual work environment. PS organizations need to guard against slipping back to their old spendthrift ways, particularly if their discretionary spending does not measurably improve client results or employee engagement.

Business Model Convergence

The lines between Marketing and Advertising, IT and Management Consultancies have been converging for quite some time. Classically, Management Consultancies, led by legendary firms like McKinsey, Bain and Boston Consulting Group, focused on strategy and innovation for the world’s leading companies. But clients started demanding that their management consultants help them translate strategy into execution. This led to a convergence of Management Consulting and Marketing and Advertising to

ensure new strategies were embodied in the brand and cemented in the culture. Now in the era of Digital Transformation, Management and IT Consulting are also converging because any focus on streamlining business processes, eliminating inefficiencies, cutting costs, building brand, culture or innovation must manifest in rationalizing and integrating legacy business applications.

Table 2: IT, Management Consultancies and Marketing and Advertising Cross Paths

PS Revenue Source	IT	Mgmt.	Marcom
Business / management consulting	10.1%	77.5%	47.7%
Technology or IT consulting	63.9%	9.6%	2.8%
Subscription Services	4.5%	2.9%	16.3%
Managed services	9.2%	3.8%	15.0%
Staff augmentation	7.1%	3.9%	5.5%
Hardware/software and other resale	4.0%	0.4%	1.8%
Other	1.2%	2.1%	10.8%

Source: SPI Research, April 2021

The overlap in professional service disciplines has also been a catalyst for mergers and acquisitions. Across the Professional Services industry thousands of mergers and acquisitions occur each year. Serial acquirers like Deloitte, IBM and Accenture have been joined in the acquisition frenzy by leading Indian consultancies including Cognizant, Tata and Infosys. As soon as an independent firm reaches 100 consultants, they become an acquisition target with price multiples almost on par with the crazy valuations of tech firms.

Blended service models that wrap software, service and advisory services together enjoy recurring revenues and facilitate profitable revenue growth. If you are a service provider, there is nothing better than starting a new year with 50% of forecasted revenues already “in the bag” via multiyear managed and subscription service contracts.

The War for Talent and the new wave of Digital Transformation have only accelerated convergence. There simply is not enough skilled talent to fuel the insatiable demand to move applications to the cloud and to support a virtual work environment. Initially pandemic fueled, a “new normal” hybrid virtual work environment will become the norm. Very few knowledge workers will be willing to return to employers who demand a daily into-the-office or to-the-customer-site commute.

The “Haves” and “Have Nots” - Business Applications Make the Difference

2020 was a tough year for all businesses and sectors. Unfortunately the [K-shaped recovery](#) which is widening the gap between the have and have nots in society is also at play in the Professional Services sector with the best-positioned firms (focused on the hottest growth areas of the cloud and analytics) garnering near record levels of growth and profit while the bottom 20% saw revenues and profits plummet. When we look at the juxtaposition of the top performing independent firms compared to the bottom performers, a stark “going out of business” picture emerges.

Table 3 compares the 54 top performing independent firms to the 54 bottom performing firms (20%). By all measures the gulf between top and bottom performers has widened, threatening to obliterate the bottom performers. Throughout 2020 they gallantly trudged on without enough pipeline or

backlog to sustain them. Per project, per consultant and per employee revenues nosedived resulting in layoffs, job losses and almost no profits.

When we look under the covers to discover the differences between the “haves” and “have nots” in the service sector (Table 4), business application use and integration is a major differentiator. The Digital Transformation picture that emerges shows a deep and wide chasm between top and bottom performers when it comes to their own use and adoption of cloud business applications. Understandably, the lowest performing firms are dissatisfied with their business applications

and are far less likely to have integrated CRM and PSA nor are either of these primary applications integrated with the core financial

system. Poor performers rely on a hodge podge of silo’ed legacy business applications necessitating the use of disconnected and error prone spreadsheets. The greatest differential in business application use is in Professional Services Automation. Poor performers do not have visibility into their sales pipeline nor is the pipeline integrated with PSA to enable proactive capacity and resource planning. Without integration and visibility, poor performers were not able to

anticipate or adjust to project delays and cancellations. Top performers on the other hand, replanned and continually adjusted throughout the year to keep pace with changing conditions.

Table 3: The “Haves” and “Have Nots” – Independent Firms

Key Performance Indicator (KPI)	Haves Top 20%	Have Nots Bottom 20%	▲
Size of PS organization (employees)	434	952	-54%
Total professional services revenue (mm)	\$65.6	\$135.3	-51%
Year-over-year change in PS revenue	11.9%	9.8%	22%
Year-over-year change in PS headcount	11.0%	5.2%	111%
% of employees billable or chargeable	79.1%	71.4%	11%
Deal pipeline vs qtr. bookings forecast	212%	114%	86%
Employee billable utilization	81.5%	53.1%	53%
Annual fully loaded cost per consultant (k)	\$142	\$99	-44%
Revenue per project (k)	\$259	\$27	875%
Annual revenue per billable consultant (k)	\$242	\$90	169%
Annual revenue per employee (k)	\$205	\$80	156%
Quarterly revenue target in backlog	51.4%	17.5%	194%
Profit (EBITDA %)	16.1%	4.8%	234%

Source: SPI Research, April 2021

Table 4: Business Application Use Comparison Between Top and Bottom Performers

Key Performance Indicator (KPI)	Top	Bottom	▲
Use a commercial Financial solution (CFM)	94.4%	92.5%	2%
Satisfaction with Financial solution	4.21	3.86	9%
Use a commercial CRM solution	86.5%	90.6%	-5%
Satisfaction with CRM solution	4.04	4.03	0%
CRM is integrated with CFM	41.1%	45.3%	-9%
Use a commercial PSA solution	87.0%	71.1%	22%
Satisfaction with PSA solution	4.10	3.93	4%
PSA is integrated with CFM	67.9%	55.0%	23%
Level of CRM and PSA integration	50.9%	34.6%	47%

Source: SPI Research, April 2021

Professional Services Automation (PSA) Improves Performance

Of the 272 independent firms in this analysis, 198 use a commercial PSA and 71 do not. FinancialForce PSA is the most adopted with 47 firms using it. The PSA results are very compelling with significantly higher growth and larger and more profitable projects resulting in superior per consultant and per employee revenue yields. Throughout the chaos of 2020, independent firms were able to rely on their PSA applications to reforecast and replan resource requirements. Underutilized consultants could be moved to other billable projects or down time could be used to improve skills and certifications or develop infrastructure.

PSA provides the necessary visibility to efficiently manage projects with fewer overhead resources, resulting in better resource management and profit. PSOs can manage the business with less administrative overhead and deliver more projects on time, driving better financial performance. The bottom line is that organizations that use a PSA solution grow faster, are much more profitable, and simply operate far more efficiently.

Integrated PSA (with Financials) Does Even More

SPI's research has consistently measured the improvement in all facets of the business when PSA is deployed. Over the past 14 years we have seen increased PSA adoption resulting in dramatic advancements in service delivery. As Table 6 shows, when PSA is integrated with the core financial management application, results improve exponentially due to enhanced visibility and alignment across all elements of the business. Better visibility

facilitates faster, fact-based decision making. All members of the team have visibility to the same information which is constantly updated and accurate. One source of the truth helps foster

Table 5: PSA Adds to the "Bottom Line"

Key Performance Indicator (KPI)	Use PSA	Do Not	▲
Number of Independent Firms	198	71	
Year-over-year change in PS revenue	7.7%	7.1%	9%
Year-over-year change in PS headcount	6.3%	2.3%	175%
Use a standardized delivery methodology	66.0%	58.7%	12%
Onsite delivery	42.0%	57.7%	27%
Use a standardized delivery methodology	66.0%	58.7%	12%
Project duration (man-months)	24.3	17.7	37%
Project margin	38.6%	35.5%	9%
Annual revenue per billable consultant (k)	\$214	\$189	13%
Annual revenue per employee (k)	\$174	\$155	13%

Source: SPI Research, April 2021

Table 6: Integrated PSA Improves Performance Even Further

Key Performance Indicator (KPI)	Int. PSA	Non-Int.	▲
Number of projects delivered per year	222	111	101%
Revenue per project (k)	\$224	\$89	153%
Project staff size (people)	4.71	3.03	55%
Project duration (months)	5.90	4.29	38%
Profit (EBITDA)	14.7%	9.8%	50%

Source: SPI Research, April 2021

collaboration and knowledge sharing so all team members can provide accurate client updates, resulting in fewer project overruns and more timely change orders. Consultants have more control over their schedule and can bid on upcoming projects in line with their career goals and aspirations. Projects start and end on time resulting in improved client satisfaction. Revenues and costs can be kept in balance to ensure every project is delivered profitably. Invoices are accurate and timely, conforming to contract and purchase order guidelines, so clients are more likely to quickly pay, resulting in better cash management.

PSA Integrated with CRM Does Even More

SPI's research shows the pervasive use of CRM applications within the service industries, with Salesforce CRM commanding dominant market-share. However, the true power of a CRM for service organizations can only be realized when it is sharing critical information with the PSA solution, such as territory, account, opportunity and probability information. With the emergence of FinancialForce PSA, built on the Salesforce Platform, sales and service delivery no longer have to maintain separate systems. Out-of-the-box and seamless data sharing is assured because both applications are built on the same development platform and leverage the same data. Now the needs of both constituencies can be realized. Bidirectional, real-time data means sales has an up-to date view of resource availability and project status while service delivery can see the sales pipeline to anticipate, plan and staff upcoming projects appropriately.

Table 7 shows the powerful impact of integrated CRM and PSA. When the sales pipeline is synchronized with the resource plan, all aspects of service sales and delivery improve. Sales can sell projects which take advantage of available resources and service delivery can anticipate resource requirements. If required resources are not available, new requisitions can be opened. Optimizing the delicate balance between demand and supply is the way money is made in the Professional Services industry. During the pandemic, integration of CRM and PSA was even more important so organizations could replan and rebalance as seismic changes occurred in the business environment.

Table 7: Integrated PSA and CRM Improves Performance Even Further

Key Performance Indicator (KPI)	Int	Non-Int.	▲
Year-over-year change in PS headcount	6.5%	6.0%	10%
New client revenue as percent of total	26.4%	23.1%	14%
Sales cycle (days)	79	92	14%
Percentage of referenceable clients	77.5%	74.9%	3%
Employee billable utilization	75.0%	73.6%	2%
Number of projects delivered per year	166	117	42%
Revenue per project (k)	\$205	\$167	23%
Project staff size (people)	4.90	3.53	39%
Projects delivered on-time	84.9%	81.5%	4%
Project overrun	6.9%	8.6%	19%
Annual revenue per billable consultant (k)	\$226	\$219	3%
Annual revenue per employee (k)	\$186	\$176	6%
Executive real-time wide visibility	3.90	3.83	2%
Project margin	39.8%	38.6%	3%

Source: SPI Research, April 2021

Ideally, PSA is Integrated with Both CRM and CFM

The true power of integrated, cloud-based business applications is shown in Table 8. Top performers have integrated CRM, PSA and the core Financial application, providing visibility and management control across all aspects of the business. This real-time visibility provides a host of benefits including faster time to close the books, fewer errors and improved cash flow. Demand and supply are not only synchronized but projects can be staffed with the best available resources with an eye to maximizing project quality and profitability. With integrated

Financials, PSA and CRM, firms keep revenues and costs in balance. They have visibility to time tracking, utilization, expense, billing, and invoicing with reports and dashboards for profit and loss by project, cost center and job level. New hire requisitions can be tied to backlog and pipeline to ensure there is enough work to justify opening a new requisition. Integrated systems eliminate manual processes and painful, time consuming resource discussions. Projects can be staffed quickly, improving cash flow and increasing billable utilization while enhancing client satisfaction.

In Conclusion

2020 was a wake-up call for the Professional Services industry, accelerating Digital transformation and a move to virtual, cloud-powered operations for all businesses. Just as we have seen in the larger economy, the pandemic-induced recession produced PS winners and losers. The rich got richer and the poor are on the brink of going out of business. This report shows a very uneven K-shaped recovery for independent firms. Clearly some aspects of 2020 performance were outside of management control, particularly for firms focused on the travel, leisure and hospitality sector which was severely battered. But many independent PS firms not only survived but thrived. Top performing firms were able to quickly and easily move to virtual operations. They were able to plan and replan the business to keep their employees productive and engaged. When projects were delayed or cancelled, their integrated business applications enabled them to anticipate and react, to reassign resources and ramp new projects. Many firms saw a big uptick in business as their clients accelerated their own digital transformation efforts. One key fact is apparent. Top performing firms are more resilient and agile because they rely on integrated, cloud-based business applications. These investments pay for themselves with improved transparency and visibility across all aspects of the business.

Table 8: CRM, PSA and CFM Integration Helps Optimize Performance

Key Performance Indicator (KPI)	Int.	Not Int.	▲
Number of Independent Firms	145	68	
Year-over-year change in PS revenue	8.1%	5.8%	38%
Year-over-year change in PS headcount	6.1%	3.1%	95%
Bid-to-win ratio (per 10 bids)	5.31	4.84	10%
Deal pipeline / qtr. bookings forecast	193%	160%	20%
Sales cycle (days)	85	91	7%
Employee billable utilization	73.7%	71.4%	3%
Revenue per project (k)	\$180	\$144	25%
Project duration (man-months)	24.3	19.8	22%
Onsite delivery	42.8%	51.5%	17%
Project margin	38.3%	37.2%	3%

Source: SPI Research, April 2021

About Service Performance Insight



R. David Hofferberth, PE, Service Performance Insight founder, managing director and licensed professional engineer has served as an industry analyst, market consultant and product director. He is focused on the services economy, especially productivity and technologies that help organizations perform at their highest capacity.

Dave's background includes application and analytical tool development to support business decision-making processes. He has more than 35 years of domestic and international information technology experience with firms including the Aberdeen Group and Oracle. Contact Hofferberth at david.hofferberth@spiresearch.com or 239.207.7773.



Jeanne Urich, Service Performance Insight Managing Director, is a management consultant specializing in organizational improvement and transformation for small to large service and project-oriented organizations. She has been a corporate officer and leader of the Worldwide Service Organizations of Clarify, Blue Martini and Vignette, responsible for leading the growth of their Professional Services, Education, Account Management and Alliances organizations from 50 to over 1,000 consultants. She earned a BA in Math and Computer Science (Phi Beta Kappa and Magna Cum Laude) from Vanderbilt University.

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Service Performance Insight (SPI Research) is a global research, consulting and training organization dedicated to helping professional service organizations (PSOs) make quantum improvements in productivity and profit. In 2007, SPI developed the PS Maturity Model™ as a strategic planning and management framework. It is now the industry-leading performance improvement tool used by over 35,000 service and project-oriented organizations to chart their course to service excellence.

SPI provides a unique depth of operating experience combined with unsurpassed analytic capability. We not only diagnose areas for improvement but also provide the business value of change. We then work collaboratively with our clients to create new management processes to transform and ignite performance. Visit www.SPiresearch.com for more information on Service Performance Insight, LLC.