



FAO MARKET REVIEW, AS OF OCTOBER 2005

Year 2005 has been particularly active in terms of business process outsourcing market growth, especially as related to demand for Finance & Accounting Outsourcing services. According to FAO Research, Inc.:

- Demand for Finance & Accounting Outsourcing (FAO) services as of October 2005 is up over the first half of the year. There has been increased interest in and implementation of FAO engagements as the year has progressed.
- Large corporations have comprised the largest share of interested FAO buyers, with medium-sized businesses and the public sector/government showing greater interest also.
- The most widely considered and outsourced enterprise-wide FAO functions have been transactional types of services, although there has been increased buyer interest in more strategic types of FAO services as of late, like asset management and product development support.
- Financial Services companies dominate FAO market interest and demand, while firms in the consumer products, retail and manufacturing sectors also show greater demand.
- The United States exhibited the greatest geographic FAO growth most recently, while the United Kingdom market continued to explode and, in some cases, surpass the pace of U.S. demand in terms of market interest and acceptance of FAO.
- Most enterprise-wide FAO contracts are valued at greater than \$500 million, with terms greater than five years in length. FAO deals with smaller scopes range from 3 years to 5 years, with values of less than \$100 million.
- Active FAO service providers recently have been ACS, Accenture, EDS, IBM and Infosys.
- The two most important attributes sought by buyers from FAO service providers have been “process expertise and quality” and “price and overall economic proposition.”

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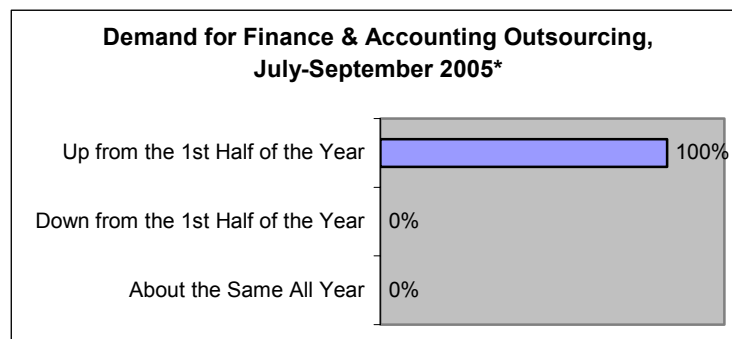
ABOUT “FAO MARKET REVIEW”

FAO Market Review, As of October 2005 discusses FAO market demand, contract scope, service provider activity and market trends, with particular emphasis on the past three months – July, August and September 2005 – to illustrate how this market has grown so far this year. This report results, in part, from our collaboration with highly-respected outsourcing lawyers, consultants, service providers and industry influencers who presented us with their “feet-on-the-street” perspectives of FAO market activity. They hold positions such as solutions architects, attorneys, customer advisors, consultants and FAO service providers. They are based in the United States and Europe and have global responsibilities.

MARKET DEMAND FOR FAO SERVICES

Buyer demand for FAO services was up this past quarter compared to the first two quarters of the year (see Figure 1). Every market-facing advisor with whom we spoke indicated that a greater number of companies considered and/or implemented the outsourcing of multiple F&A business functions on an enterprise-wide basis. **Affiliated Computer Services, Inc.** (www.acs-inc.com), a major supplier of FAO and other types of business process and information technology outsourcing solutions, also indicated a strong increase in FAO interest during July, August and September 2005. Demand came from a myriad of industries, types of companies, government entities and geographies.

Figure 1, Demand for Finance & Accounting Outsourcing, July-September 2005



* Represents the views and experiences only of FAO Research, Inc. and market advisors contributing to “FAO Market Review.”

Source: FAO Research, Inc., October 2005

Attorney John K. Halvey who heads the international outsourcing practice of law firm **Milbank, Tweed, Hadley & McCloy LLP** (www.milbank.com) noted that FAO demand grew noticeably over the past three months. “More importantly,” he said, “the FAO product is starting to expand into other F&A classifications, like asset management services for hedge funds and mutual funds, complex financial product development and roll out and tax compliance-based services.” He added that governmental entities also requested third-party assistance with FAO functions this past quarter, stating that government entities in the United States are beginning to follow the trail blazed by similar entities in other countries and are expanding their use of outsourcing solutions.



One advisor indicated that F&A is more difficult to outsource than other types of business processes, since these functions are closely tied to internal corporate cultures; however, most advisors believe that buyers experience the same level of ease/difficulty when outsourcing F&A versus other types of business processes. According to attorney Robert Zahler, Senior Partner at **Pillsbury Global Sourcing (PGS)**, a practice group of global law firm **Pillsbury Winthrop Shaw Pittman LLP** (www.pillsburylaw.com), the key to buyer demand and ease of enlisting third-party FAO assistance depends on the maturity of the process, both of the customer and by the provider. Buyers with prior outsourcing experience and those more familiar with the process and resulting challenges/benefits are more apt to have smoother transactions than are newer outsourcing buyers. In addition, buyers with deep process knowledge of their F&A functions also have smoother transitions.

WHAT TYPES OF BUYERS ARE OUTSOURCING?

Large corporations comprised the majority of interested FAO buyers this past quarter. Companies with multiple divisions across numerous geographies with a myriad of offerings serving thousands of customers make the most compelling business case to outsource F&A functions at many levels. Over the past three months, major companies investigated and engaged in enterprise-wide FAO, although many of these companies chose not to disclose publicly the details of their new FAO arrangements.

Medium-sized businesses also exhibited interest in FAO during July, August and September 2005, according to the “feet on the street” people with whom we spoke. Competitive dynamics, regulatory conditions and operational initiatives drove companies of this size to seek more efficient ways to conduct business. They considered numerous F&A business functions as potential candidates for outsourcing.

Governments and governmental agencies also explored third-party assistance with FAO functions this past quarter. According to Simon Tennant, a consultant/advisor with global **PA Consulting Group** (www.paconsulting.com), an increasing trend towards service modernization, which is evident across the public sector, is driving organizations to look at F&A and Human Resources transactional outsourcing as well as the more conventional outsourcing of contact centers, information technology (IT) and property management outsourcing arrangements. He added, “We are consequently seeing all types of Public Sector clients – from Health Care to Broadcasting – who are seeking objective advice in selecting the right outsourced service suppliers for F&A and other areas to best meet their needs.”

WHAT ARE THEY OUTSOURCING?

The types of F&A functions evaluated for outsourcing depend on a variety of factors specific to each company, including opportunities to reduce cost, streamline business processes and standardize the underlying IT systems. According to attorney William Peters of global law firm **O’Melveny & Myers LLP** (www.omm.com), a company will see the most immediate benefit from outsourcing those F&A functions that are transactional in nature or those that can be leveraged across the entire company. He said, “Companies looking for longer-term benefits may also turn to F&A business process outsourcing as a means for transforming the overall environment. In some cases, this is accomplished by migrating a company to a common set of systems and business processes across all of its operating units.”



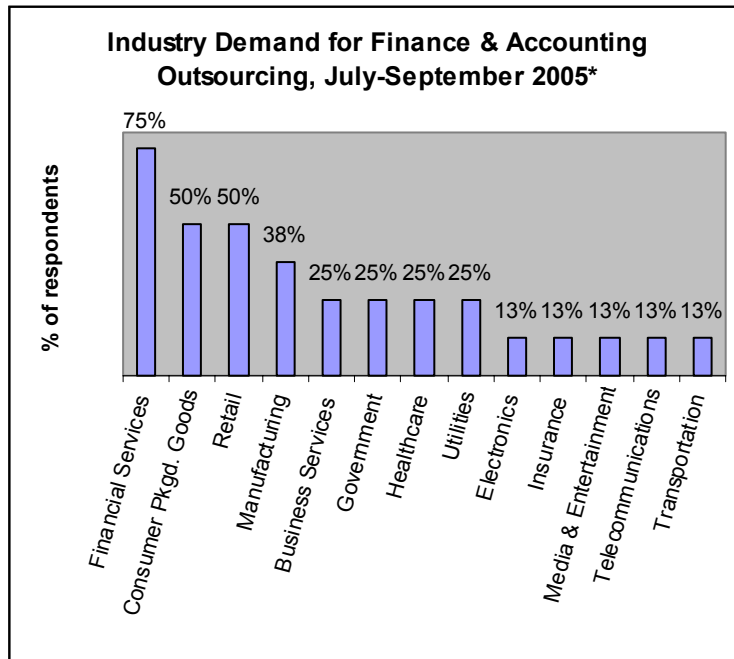
Many other advisors also found that recently-outsourcing F&A functions included transactional processes, like: Accounts Payable; Accounts Receivable; General Accounting; Revenue Accounting; Purchasing Payables; and Payroll (often considered a Human Resources function).

One advisor expects that strategic functions under heavy scrutiny, like audit control, will be areas in which buyers increasingly will reach for help. Denise Underwood of **Agilita Consulting** (www.agilita-consulting.com) and former leader of the global sourcing practice of Gartner, Inc. said, "If I can reduce my number of external audits from 100 to 5, that is a significant impact." She stressed that the organization of data and adherence to process standards are essential for FAO buyers.

WHICH INDUSTRIES ARE THE MOST ACTIVE?

Companies in the Financial Services sector dominated the FAO market during July, August and September in terms of requesting third-party assistance company wide (see Figure 2). According to 75% of advisors with whom we spoke, the Financial Services industry exhibited the most interest in FAO primarily due to the overall economic proposition and process expertise that FAO provides. Brad Peterson, attorney/customer advisor at global law firm **Mayer, Brown, Rowe & Maw LLP** (www.mayerbrownrowe.com), indicated that other highly-active industries showing interest in FAO services this past quarter included consumer packaged goods, retail and manufacturing.

Figure 2, Industry Demand for Finance & Accounting Outsourcing, July-September 2005



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WHICH GEOGRAPHIES HAVE THE MOST DEMAND?

The United States was the most active region worldwide this past quarter with regard to demand for FAO services. The United States also is the most mature region worldwide of third-party assistance with all types of business process improvement. According to the advisors with whom we spoke:

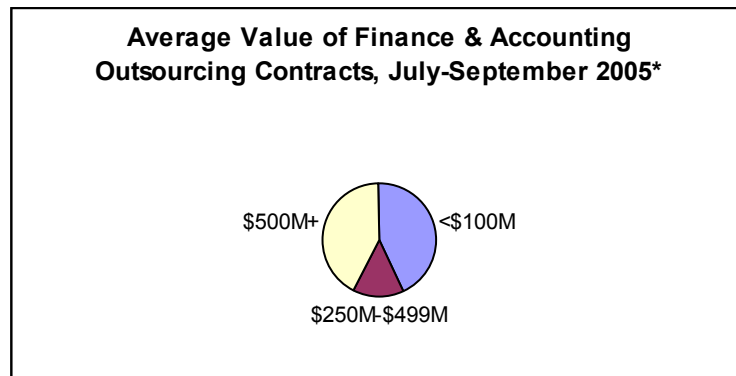
- 88% of buyer advisors mentioned the United States as having the highest FAO demand.
- 63% of advisors listed the United Kingdom as having strong recent growth.
- 13% cited Canada and the Asia-Pacific region as areas with higher FAO interest.

The United Kingdom is poised for explosive growth in the coming months and already exhibited strong interest in the outsourcing of FAO between July and September. Simon Tennant who is based in the U.K. office of **PA Consulting Group** has seen that UK-based local and central government bodies are now either considering the feasibility of FAO or already are embarking upon outsourcing in this area. He mentioned that particular F&A focus areas are front- and back-office transactional activities associated with Revenue collection (e.g. Council Taxes), Payments (including social security benefits) and Payroll.

WHAT'S THE VALUE OF RECENT CONTRACTS?

The average value of enterprise FAO contracts this past quarter ranged from greater than \$500 million each to less than \$100 million (*see Figure 3*). Contracts on the high end included a myriad of outsourced services, while the lower-priced deals included more transactional services with smaller scopes. We expect the average value of FAO contracts to rise over the next few quarters, as companies become more comfortable with the concept of third-party assistance for F&A functions and outsource larger pieces of their operations.

Figure 3, Average Value of Finance & Accounting Outsourcing Contracts, July-September 2005



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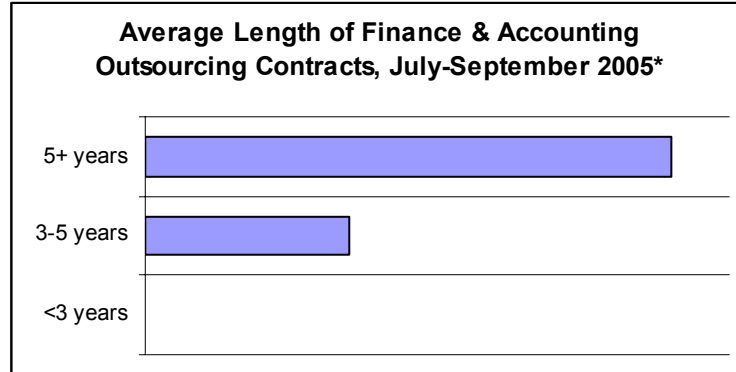
HOW LONG ARE CONTRACT TERMS?

The majority of recent enterprise FAO contracts span greater than five years in length (*see Figure 4*). The breadth and depth of scope within major F&A deals is so vast that buyers and suppliers forge long-term (5+ year) commitments for the success of these engagements. FAO buyers seek long-term solutions rather



than quick fixes, so even though some contracts span 3-5 years, the operational and cost improvements inherent in enterprise FAO arrangements are more apparent over longer periods of time.

Figure 4, Average Length of Finance & Accounting Outsourcing Contracts, July-September 2005

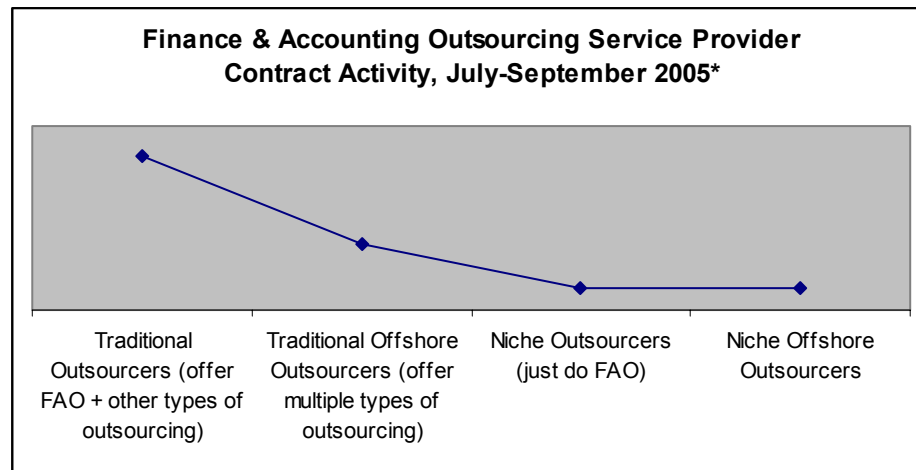


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FAO SERVICE PROVIDER ACTIVITY

Multiple types of service providers have been considered for and awarded FAO contracts over the past three months, with traditional outsourcers – those offering FAO as well as other types of outsourcing services – dominating the market for new enterprise-wide engagements (see Figure 5). Traditional offshore outsourcers – those offering multiple types of outsourcing services from offshore locations, mostly from India – also played dominant roles in new FAO arrangements. Suppliers that solely offer FAO services (niche providers) – both onshore and offshore – also won a fair share of market interest.

Figure 5, Finance & Accounting Outsourcing Service Provider Contract Activity, July-September 2005



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The most active service providers in the FAO realm during July, August and September 2005 were, according to the market-facing advisors with whom we spoke:

- Accenture
- ACS
- EDS
- IBM
- Infosys

All of these service providers offer full-scale FAO services on a global basis and have a strong heritage of providing outsourcing services. These suppliers, among others, will be profiled in an upcoming FAO Research, Inc. report to be published in November 2005 that highlights activity in the FAO arena and in-depth analyses of the most significant FAO service providers worldwide.

SELECTION CRITERIA FOR FAO SUPPLIERS

Service provider “process expertise and quality” is the most important attribute that buyers seek in an FAO provider, according to the advisors we interviewed (*see Table 1*). The advisors indicated that, different from applications outsourcing, payroll outsourcing and other types of outsourcing which are based often on price, FAO requires a unique set of skills and experience to manage highly detail-oriented data within specific parameters and guidelines among multiple business units...necessitating a strong focus on FAO expertise. Although price and overall economic value is of tremendous importance to those considering FAO, buyers seek service providers with a deep understanding of how to better manage their critical business functions.

The following table lists attributes that buyers seek most frequently when choosing an FAO service provider, with the % values indicating the number of polled advisors mentioning each attribute:

Table 1, Most Important Attributes for Finance & Accounting Outsourcing Service Providers*

FAO Service Delivery Attribute	% of Advisors Indicating Its Importance
Service provider process expertise and quality	86%
Price and overall economic proposition	71%
Service provider reputation	57%
Service provider stability and commitment to FAO	57%
Cultural fit	57%
Service provider's technology platform	43%
Past experiences	43%
Breadth of global/geographic delivery options	29%
Strength of management team and processes	29%
Service provider innovation and creativity	29%
Speed to achieve objectives	29%
Company specific knowledge and/or experience	29%
Proximity to company locations	29%
Ability to support ERP implementation alongside FAO	29%



Contractual commitments to deliverables (e.g., gain sharing, value based pricing)	14%
Flexibility to accommodate change	14%
Capabilities beyond FAO including end-to-end processes and other functions	14%
Company industry knowledge	14%

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NOTE:

The information and data presented in **FAO Market Review** is intended solely for informational purposes. This report should not be used as a tool when making FAO-related decisions. Individual responses presented in this report represent the views and experiences only of FAO Research, Inc. and those with whom we have collaborated. Any feedback or comments should be directed to us by phone, toll free, at #888-498-FAOR or by email at info@faoresearch.com.

ABOUT FAO RESEARCH, INC.

Who We Are

FAO Research, Inc. (www.faoresearch.com) is the only market research/consulting firm that offers an exclusive focus on providing Finance & Accounting Outsourcing (FAO) market and competitive intelligence to outsourcers worldwide. We help FAO service providers be the best at understanding their markets, competitors and customers. We help them improve their go-to-market strategies, better meet their prospects' needs and refine their business development and operational initiatives.

What We Do

FAO Research, Inc. publishes Research Reports on topics of interest to FAO service providers; all reports contain actionable recommendations for outsourcers to become more competitive in their markets. We offer Custom Consulting Services that are tailored to address FAO service providers' individual needs. We perform Multiclient Studies for multiple service providers on topics of specific interest to them. We provide direct support from our analysts to outsourcers that have questions for our experts. We offer webcasts and conferences to keep FAO suppliers informed of our research findings and the best suggestions for market success.

To Contact Us

We welcome your questions and suggestions and would be happy to avail ourselves to discuss our annual subscription packages (of reports, custom consulting services and analyst support) and upcoming research schedule.

- Regularly check our website, www.faoresearch.com, for new research findings and events.
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