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Key Performance Indicators

Establishing the Metrics that Guide Success

technologies

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Executive Summary

Tracking performance is a vital way for service providers to ensure their businesses are moving in the right direction. To measure and improve performance, leadership needs to track the right key performance indicators (KPIs). This paper offers service provider executives an overview of KPIs, describing the main categories of these measurements and providing a detailed look at a number of specific metrics that organizations can use to track their progress.

Introduction to KPIs: One Does Not Fit All

As service providers seek to institute the optimizations, initiatives, programs and services that improve the fortunes of their business, a critical question arises: How do you know if the changes and investments made are yielding the dividends desired?

Ongoing measurement and analysis of the right key performance indicators (KPIs) is a critical way to gain an objective understanding of what's happening in the business and how to improve performance. However, identifying the right KPIs for your organization isn't that straightforward. The reality is that there isn't one single metric that a business can look at to measure success. Further, there are a lot of measures to consider, and no single metric or set of metrics is going to be right for every service provider.

Choosing the right KPIs requires a good understanding of what is important to the organization and its customers. This latter component is key because most KPIs are tied to service delivery, and what's important to internal teams may not matter to the customer. To be effective, managers need to assess the alternatives available and pick the metrics that make the most sense for their business. Toward that end, this paper offers an overview of some of the most important metrics service providers can use to track performance. The metrics covered fall into several key areas: service delivery, financial, sales and customer satisfaction. The following sections offer a description of some of the most important KPIs within each of these categories.

Key Considerations for Managing KPIs

Tactics for tracking KPIs will vary substantially according to the metrics being assessed and the specifics of the business. However, following are some key strategic considerations that cut across all organizations and KPIs:

- **Consistency**. On a consistent basis, whether daily, weekly, monthly or quarterly depending on the metric, service providers need to be gathering performance data and continue to do so over time. It is only by gathering this multi-interval data that managers can start to spot trends and truly understand the trajectory of the business.

- **Communication**. The best KPI tracking is meaningless unless it is communicated to the right audiences. Both with customers and among internal teams, KPI reporting needs to be useful, relevant, consistent and timely.
- **Actionable**. KPIs need to help identify problems and strengths and inform actions that can improve performance.

Service Delivery KPIs

In tracking service delivery KPIs, a good rule of thumb is to use metrics that meet the Information Technology Infrastructure Library (ITIL) definition of "SMART" that is specific, measurable, achievable, relevant and timely. Often, optimal service delivery KPIs will be based on the service level targets set in your service level agreements (SLAs), which helps ensure you're looking at a measure that's relevant to you and customers. These KPIs are instrumental in helping your service delivery team ensure they're delivering effective services, and provide a solid basis for communicating their performance to customers.

Infrastructure Capacity Utilization

A KPI that's often used by cloud vendors, this is a vital measure for any service provider that offers a hosted solution or service. By tracking utilization rates, service providers can manage the balance between incurring the expense of new infrastructure investments against the support of non-productive capacity. This measure is also vital to customers who use that hosted service.

Availability Rates

Availability rates are a very common and very useful KPI to track, and are typically tied to an SLA. These KPIs can apply to help desks, application management and hosted infrastructures. Examples can include committing to a phone system or server being available 99.9% of the time. A service provider that delivers a help desk may commit to answering 95% of incoming calls within 20 seconds. As management starts to look at their organization's cumulative performance across all the KPIs in effect with customers, they can get a very good picture of what's happening in the organization.

A Lesson in Tracking the Right Metric

At a networking event many years ago, a CEO of a large service provider spoke about her KPI. She explained how every Monday, she would call her bank (this was before online banking) and find out what the company's operating account balance was. This CEO felt that as long as the balance was above a certain amount, everything was ok. If it fell below that amount, her management team heard about it. In speaking with other members of her team, it became clear that the CEO was looking at the wrong metric. This metric did not reflect customer satisfaction, retention, team performance or any other business metric. Unless management starts with the right metric, with an understanding of its context and relevance to fundamental business performance, the data gathered may not mean much, and even lead to some significant misunderstandings of the performance of the business.

SLA and Service Level Target Attainment

For service providers, it's critical to always track the attainment of SLAs and associated service level targets. If your organization sets a service level target of 99.9% uptime for a Windows server, it's important to track that and report on it on a consistent basis. These metrics are instrumental in understanding the strengths and weaknesses of the service delivery organization. It can also be a key way to demonstrate value to clients, if, for example, your team can report that it bested its service level targets for 15 months running.

Days of Project Backlog

This KPI describes the number of days it will take for a team to complete a new project. This is calculated by totaling the number of hours estimated for the projects committed, divided by the potential hours of project team availability. This KPI is useful in gauging the capacity of a service provider's project delivery team. For example, if the business is continually running with a high project backlog, management may determine additional staff is needed.

Percent of Projects Delivered on Time

For many service providers, tracking the percentage of projects that are delivered on time is a vital way to assess project delivery team performance. There are two ways to gauge this metric. First, a service provider can track whether project revenues are delivered on time. This can be an effective way to gauge not only the delivery team, but whether associated billing mechanisms are effective. Second, a service provider can track the time of project completion vs. the initial committed delivery date.

When service providers are assessing project delivery against schedules, there are three potential scenarios:

- A project will be well designed and delivered on time.
- A well designed project will be completed behind schedule, whether because of scope creep or because of inadequate capabilities within the project delivery team.
- A project may be completed behind schedule due to it being poorly designed.

The timeliness of project delivery is a vital contributor to customer satisfaction. Further, this can be a significant contributor to team morale: If a project is scoped for eight hours and it ends up taking 40, it can be a great source of frustration for team members. Consequently, if projects aren't completed on schedule, managers have to figure out what's causing the delays.

Onboarding

This KPI tracks the time it takes to go from contract execution to when recurring services begin. This is an important metric for several reasons. First, getting new customers up and running is instrumental in the successful initiation of a new customer engagement. Further, because service providers can't start billing until they start delivering the service, this is inherently a measure of time to cash. Once invoices are submitted, many are payable on 30-day terms, so there can inherently be a significant gap between when a contract is signed and when payment is received. Consequently, by tracking and taking steps to identify any obstacles, service providers can speed the onboarding process, which can yield immediate financial benefits.

Financial KPIs

Monthly Recurring Revenue

Monthly recurring revenue represents one of the significant advantages of moving to a managed services model; with each new contract signed, the amount of predictable, ongoing revenue increases. This KPI is a measurement of the sum of managed services billings. Rather than billings contracted, this KPI should track the sum of revenues actually received.

Non-recurring Revenue

It is important to track non-recurring revenue. This represents non-contracted work and hourly billed projects, essentially anything done beyond existing managed services agreements. Early on especially, it is important not to be overloaded by KPIs, so initially managers can track the sum of non-recurring revenue. In more mature organizations, it is often a good idea to measure hourly billings and project billings separately, so managers can track how each of the two compare to contracted revenues on an ongoing basis. Over time, managers will often start to see some interesting ratios from managed services customers, assessing how much hourly billing they are generating depending on what contracts they had in place, how many projects they would generate depending on the size of the company and the frequency of those projects.

Revenue Mix

Figure A.

A representative sample of the revenue mix of a service provider.

Time	MRR	NRR	Product	Total
1	$125,000	$75,000	$300,000	$500,000
2	$150,000	$80,000	$310,000	$540,000
3	$180,000	$85,000	$320,000	$585,000
4	$216,000	$90,000	$330,000	$636,000
1	25.0%	15.0%	60.0%	100%
2	27.8%	14.8%	57.4%	100%
3	30.8%	14.5%	54.7%	100%
4	34.0%	14.2%	51.9%	100%

Ratio of Monthly Recurring Revenue to Non-recurring Revenue to Product Revenue

Within many service providers, executives have an objective of getting monthly recurring revenue to be a certain percentage of total revenue. Rather than setting a goal for monthly recurring revenue to be a specific dollar figure, it is often a worthwhile goal to establish a specific revenue mix. In fact, this can be a very important goal, given that, in the world of managed services, the revenue mix, and specifically how much of the company's revenues recur monthly, is one of the biggest factors in determining the company's valuation. That's why it's a good idea to put these measures in place and track this KPI.

Many well-run service providers have the following revenue mix: 50% recurring monthly, 30% non-recurring and 20% from products. For those organizations looking to establish a successful managed services business, this can be a great revenue mix to establish as a long-term goal.

Figure A provides a breakdown of a partner's revenues. This organization is predominantly a product-centric sales organization, but is looking to increase its monthly recurring revenue almost 40% over a few quarters, which can provide a significant boost in the company's valuation.

Cost of Goods and Services Sold

For just about every service provider, it is imperative to track the cost of goods and services sold. To calculate this KPI, managers need to tally all the costs incurred in running a business and delivering a service, including the following expenses:

- Infrastructure build out and maintenance
- Network operations systems staffing
- Professional services expenses
- Travel
- Training
- Software expenses
- Utilities
- Staff salaries

Management needs to understand and track all of this, and ultimately determine with certainty that every one of the services provided is either breaking even or profitable. It is important to realize that not every service a service provider goes to market with is going to be highly profitable; some will be marginally profitable, but nevertheless necessary to provide customers with a good range of offerings.

Gross Profitability

Gross profitability is a KPI that should be tracked at all times. This KPI is calculated by taking monthly recurring revenues and subtracting the cost of goods sold. The resulting figure illustrates the profitability of the business before accounting for general overhead, administration and taxes. Fundamentally, this is important to track because service businesses should strive to ensure that recurring revenues always exceed the cost of goods sold. Across the industry, the average gross profit for an IT services business is greater than 60%[1].

1 Channelnomics, "Managed Services Tops Profitable Models", Larry Walsh, May 28th, 2013, http://channelnomics.com/2013/05/28/managed-services-tops-profitable-models/

Average Revenue per User

Average revenue per user (ARPU) is a great indicator of how much money the service provider is making in aggregate. In many scenarios, this can be a difficult metric to track because it may be hard to know precisely how many individuals are utilizing the services being sold. However, for those businesses that can track this statistic, this KPI can be very useful to follow.

For example, if your business offers tiered pricing models, ARPU can provide an insightful view into similarities that may exist across customers and tiers. This metric is also a very good measure of the effectiveness of the sales team in penetrating accounts.

Often, the customers with the highest ARPU figure are the ones that have been customers the longest; as the service provider increases its presence as a trusted advisor in the account, the customer continues to sign up for more services.

Customer Density

This KPI tracks the amount of revenue that a specific percentage of accounts is responsible for. It often is best to measure across a few percentages, for example 10%, 20% and 30% of accounts, and see what percentage of revenue they generate for the company.

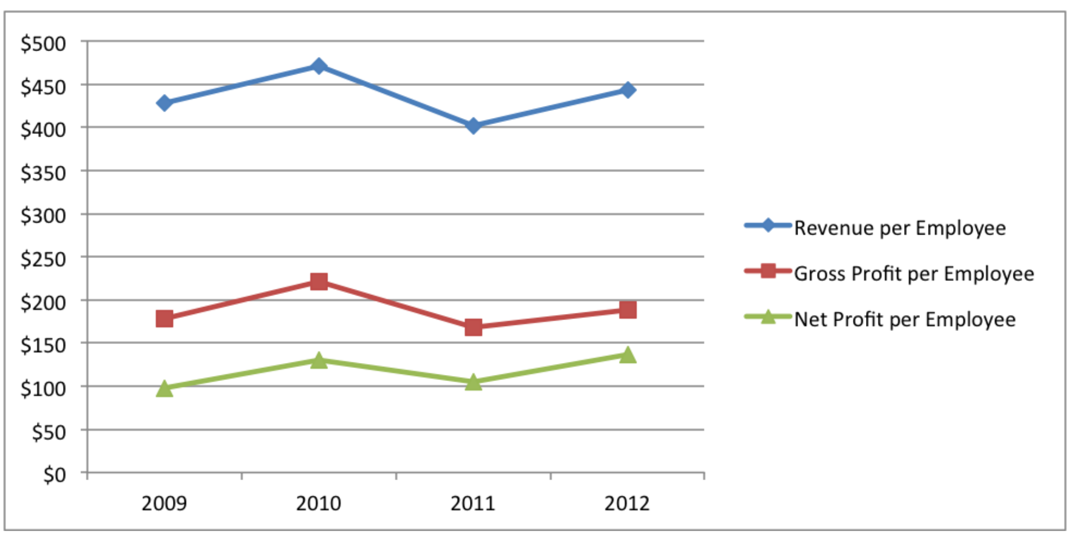
Ideally, when tracking this KPI, you want the revenue percentage to be close to the account percentage. For example, you want the top 10% of accounts to represent close to 10% of the company's revenues. If a small number of accounts dominate your revenue picture, your business can be in a tenuous position. If one of your large customers experiences a downturn, whether due to internal issues or problems across a region or industry, your business could be susceptible to a big revenue hit due to circumstances over which it has no control.

Return on New Investments

The concept of tracking return on investment has been a prevalent measure for a range of organizations for years. For services providers, a vital KPI is to assess is the return on new investments.

Figure B.

A service provider's report charting revenue, gross profit and net profit per employee over a four-year period.



Successful service providers are often looking to add new services to their portfolio, which helps provide additional opportunities for sales to do horizontal selling within existing accounts and ultimately to increase ARPU. It is always advisable to track every new service launch individually to make sure your business is getting a return on new services its bringing to market. After calculating the cost of the build out of the new services, based on the popularity of a new service, you can calculate how long it will take for the investment to pay for itself. For example, one month, you may see that a service will take 42 months to pay off. The following month, after an uptick in adoption, you may be looking at a 38-month pay off.

Earnings Before Interest, Taxes, Depreciation and Amortization

Earnings before interest, taxes, depreciation and amortization (EBITDA) is one of the most relevant financial KPIs. For many service providers, the ultimate exit strategy is an acquisition by a larger company, and EBITDA is the most significant factor an acquirer will look at in determining the value of the target organization. Likewise, if you approach banks to get a loan to expand your business, EBITDA will be one of the key metrics they'll look at.

To establish an EBITDA calculation for your business, it is highly advisable to work with a seasoned accountant or financial planner. These financial experts can provide critical guidance in terms of deciding what to include in the calculation in order to come up with an accurate picture of the company's value. Once a formula for your business has been established, start tracking the figure on a consistent and sustained basis.

Revenue, Gross Profit and Net Profit per Employee

Relatively easy to calculate, these KPIs are important, representing a good measure for assessing the progress of the business. These measures give management a clear picture of business status and opportunities for growth. For example, executives may assess the numbers and find that it makes sense to bring on additional sales resources, who can help with generating additional top-line revenue.

Accounts Receivable (Comparative)

Tracking accounts receivable is fundamentally about understanding and managing cash, and it is imperative to track this metric over time. In addition to monitoring absolute dollar amounts, executives can ultimately get a lot of vital insights by tracking relative percentages. This entails tracking the percentage of accounts at 30, 60, 90, 120 and greater than 120 days past due.

It is important to identify significant aberrations in these numbers. For example, if the percentage of payments received within 30 days only fluctuates by a couple percentage points over a few months, there shouldn't be any alarms raised, but if that figure drops by greater than five percent over a month, it is important to identify the reason and make sure this isn't the result of a significant issue that could lead to ongoing payment delays.

Accounts Receivable

Figure C.

A sample chart depicting a service provider's percentage breakdown of accounts receivable.

	30 Days	60 Days	90 Days	120 Days	>120 Days
April	78%	8%	7%	5%	2%
May	82%	7%	6%	5%	0%
June	80%	5%	10%	3%	2%

Sales KPIs

Sales Activity

In the service provider industry, profitability is predicated on the continual and increasing flow of revenue coming from new sales. To ensure your business is doing what it takes to increase new sales, it is important to track sales activity, including the number of sales leads, meetings and deals closed on a monthly and quarterly basis. While it isn't a trivial effort to track this activity, this can be a fruitful effort in identifying what's working and what isn't within the sales organization, and ultimately altering approaches and behavior in order to boost productivity in the future.

When managing a sales team, it's important to get reports showing sales representative activity, ideally by drawing a report from the sales force automation platform. If you see that there are low sales contact numbers and closing rates are going down, either representatives aren't being active enough in contacting prospects or they're not logging activities as required. If the former, these trends can ultimately lead your business to encounter expense-to-revenue issues. It's important to track this activity and assess it over time, so you can spot, and act to address, troubling trends.

Customer Retention and Renewal Ratios

One of the key advantages of the managed services model is the predictability of recurring revenue. Within this context, maximizing customer retention is a critical predictor and determinant of long-term success.

Customer retention and renewal ratios are an important KPI for tracking retention on an ongoing basis. This KPI is a percentage based on the number of accounts with contracts expiring during a given period and the number of accounts lost. For example, if during a given time period, 50 accounts had expiring contracts and 5 accounts were lost, the retention rate would be 90%. Over time, well-run service providers should sustain high retention rates, typically 90% or higher.

Customer Satisfaction

Customer satisfaction is critical for any business, and is a vital KPI for the service provider to track. Unlike a lot of other KPIs, which are more objective in nature, when it comes to customer satisfaction, the only thing that matters is the customer's perception of your business and its services. Consequently, it's critical to do surveys on a consistent basis to track how customers feel about your company.

Tracking perceptions of customers is critical in identifying potential problems—before you lose the customer. If you're only tracking churn rates, you're only finding out about problems when it's too late; once the customer leaves, there's not much you can do to get them back. If customer surveys indicate there is a potential issue with a customer, you can find out about it and take the steps needed to get them back to being a satisfied customer.

In many service provider businesses, customer satisfaction issues are often the result of misperceptions rather than significant issues. By following up when customer satisfaction scores drop, your business can often work through these misperceptions and address them before they have any lasting impact on the customer account.

There are many approaches for measuring customer satisfaction. It is best to do the research required to make a strong selection for your business, and once you've picked an approach, to stick with it as long as possible. If you change methodologies, you won't be able to track how satisfaction metrics change over time, which is essential to spotting problematic trends.

Following are some other tips for tracking customer satisfaction:

- Leverage ongoing quarterly business reviews as opportunities to gauge the satisfaction of clients.
- After each incident is closed, follow up by sending a survey to the user.
- On an annual basis, send surveys to all of the end users within client organizations, and send surveys more frequently to the client's leadership team.
- Don't conduct surveys anonymously, but rather track specifics of who submitted the survey. Gathering individual names and companies of respondents can make survey data more actionable.

When it comes to tracking customer satisfaction, the Net Promoter Score is a common and useful methodology, one that CA Technologies has recently adopted. Net Promoter Score is measured by asking customers one question: How likely is it that you would recommend us to a friend or colleague?

One of the key benefits of this approach is its simplicity. Given it's only one question, it's simple to administer and it's easy for customers to respond to. Further, given its broad adoption, there are many published metrics, which makes it practical for companies to establish a baseline across their industry and understand how their company compares. (For more information about Net Promoter Scores, visit **http://www.satmetrix.com/**.)

Conclusion

Taking the time to identify an organization's most important KPIs, and tracking those KPIs consistently, is a critical success factor for every service provider. Important KPIs fall into a range of areas, including service delivery, financial, sales and customer satisfaction. While some metrics, such as system availability or infrastructure utilization, will only be relevant to specific types of service providers, other metrics, particularly cost of goods sold, gross profitability and EBITDA will be relevant to all businesses.

About This Document: Developed by the CA Service Provider Center of Excellence

This document has been written by the CA Service Provider Center of Excellence team and is intended to provide our service provider partners with the guidance they need to address some of their most pressing challenges. Our team has rich expertise in service provider businesses, strategic consulting, technical deployments, sales and marketing. Our documents are informed by the Center of Excellence team's extensive experience over the past ten years in helping build successful service provider businesses and by interviews with some of our most successful service provider partners. This document is provided for informational purposes only and on an as-is basis. The guidance and results described herein are based on the unique experiences of our staff and partners, and may not be applicable to all organizations.

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