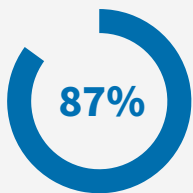




# Ctrl+Alt+Compete: Rebooting IT Services

As the demand for IT services continues to grow, so does the number of opportunities for investors. While this has created winners, volatile market conditions have also heightened risks, leading some companies into distress. With the tech race showing no signs of slowing, we examine the key themes and issues in the market, alongside the factors critical for sponsors and lenders to consider for managing exposures and maximising value.



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increase in M&A activity seen in the IT sector.

Demand for IT services is expected to continue to show strong growth of around 6.1% CAGR by 2029,<sup>1</sup> fuelled by a shift from both corporates and their sponsors looking to improve the way they embrace technology and bring efficiency to the workplace — most recently through the use of cloud computing, cybersecurity and artificial intelligence (“AI”).<sup>2</sup>

In our recent report, [AI Takes Center-Stage for Value Creation in Private Equity Firms](#), 75% of private equity funds are leveraging AI for value creation in their portfolio companies or plan to in the next 12 months, with 87% already seeing its benefits or expecting to in the next 18 months.

The changing landscape has provided numerous opportunities, with increased M&A activity seen in the IT sector, reaching 17.2% of all deals globally in 2024.<sup>3</sup> This activity includes a number of consolidators looking to bring together owner-founder businesses across Europe, while corporates look to inorganic growth as a means to fix their IT resource deficits and beat the competition.

Whilst this creates winners, there have also been a number of losers, with market turbulence and rapid growth creating an environment of increased risk, forcing some in the IT sector into distress.

What are some of the key themes and issues seen in the market, with both high-performing and underperforming businesses? These factors are critical for sponsors, lenders and wider stakeholders operating in this sector to consider — for making lending and investment decisions and for managing exposures and maximising recoveries.

## Current Market Themes

**The COVID-19 pandemic** accelerated the demand for digitalisation and the use of digital technologies and IT services, with virtual working and online services skyrocketing in use overnight. In today's post-pandemic market, the dominant themes have been AI, cloud computing and cybersecurity, with the generative AI market expected to grow by around 52% through 2030. The development and growth of these technologies is not a given though and will require ongoing investment in order for companies to remain relevant and competitive.<sup>4</sup>

One of the biggest inhibitors of growth remains **challenges in attracting and retaining talent**, with 54% of global tech organisations experiencing skills shortages. The demand for skilled IT professionals, particularly in emerging technologies like AI, machine learning and cybersecurity, is vastly outpacing supply. Investment in professional development and education across the market will be key to bridging this gap.<sup>5</sup>

We're seeing a growing number of companies using M&A to solve this skills shortage, with larger IT companies acquiring smaller players to expand their capabilities through plug-and-play and talent acquisition strategies. Whilst positive for the bigger players, it can lead to fewer options for clients, a more challenging environment for smaller players and potentially hinder innovation overall.

**Regulatory challenges**, including tightening data privacy laws and evolving compliance requirements, are adding complexity and cost to IT service delivery.<sup>6</sup> Service providers are required by law to constantly adapt to these changes to avoid penalties and ensure their clients' data is protected. The cost of failing to keep up shouldn't be underestimated; in 2024 we saw an aggregate total of €1.2 billion in fines issued across Europe.<sup>7</sup> These challenges only increase for global businesses operating across multiple geographies, with a need to navigate jurisdictional differences whilst still delivering growth.

In today's market, **customer expectations** are at the forefront of growth strategies, with clients now expecting faster, more personalised and increasingly innovative IT solutions. The rapid pace of technology evolution means companies must continuously innovate

or risk losing clients to more agile competitors. This is often seen by many organisations increasing the pace of cloud-native strategies, meaning providers of some traditional IT services are becoming obsolete. Many businesses are moving away from on-premises solutions and opting for cloud-based platforms, changing the nature of the delivery of IT services, with roles evolving towards cloud architecture, security, automation and AI-driven IT management.

## Common Issues

As IT companies navigate these tumultuous market conditions, they need to be aware of a number of common challenges which could hamper their success.

We often see that **revenue recognition can mask underlying performance**. It's important to look for warning signs, such as a lack of understanding of accounting treatment, identification of volatile revenue numbers and confusing messaging explaining underlying trends. The precise nature of customer contracts will determine how revenue is recognised in accordance with IFRS 15, for example, upfront, spread over the life of the contract. This can often make it challenging for stakeholders to understand underlying financial performance, especially when profit and loss volatility is identified, as well as compare trends over time — resulting in detrimental decisions being taken without full clarity or total visibility of information.

**A limited understanding of contracts, products and service profitability** can also be a challenge.

Limited reporting and historical data — often due to rapid growth and a stretched finance function — has led to a lack of detailed profitability insights, hindering effective pricing decisions and strategic planning. This lack of detail is often caused by a shortage of resources, capacity, know-how or sophisticated systems. Effective business plan forecasting will require an understanding of key revenue and gross profit drivers, along with enabling improved management and understanding of the business. Investing the time and resources to ensure this area is not overlooked is critical, with this improved visibility creating an opportunity to generate long-term value and drive success.



Historically, **long-term contracts** are seen as the jackpot of client engagements, providing security and sustained profitability. Today, the fast-paced and dynamic nature of the industry may mean that whilst a customer agrees to a long-term contract, they may determine over time that the services no longer meet their requirements or the technology has become obsolete. Long-term contracts are open to increasing client payment risk, such as default or renegotiation, and, possible accounting adjustments.

In an attempt to tackle this shift, many are looking to **pricing strategies** as a solution. However, under or overpricing of services is common among businesses not undertaking regular pricing reviews, which should be completed annually at a minimum. If the business underprices services, they may not be able to sustain profitability, and on the other hand, overpricing can lead to losing potential clients to more affordable competitors and damaging reputations. Striking the right balance is crucial.

When it comes to securing these contracts, **misalignment between sales team incentivisation and liquidity** can be problematic. Sales teams may be incentivised based on the size of new contracts secured, regardless of the estimated cash receipt profile or risk profile of the customer. This can be particularly detrimental if a business is having to closely manage liquidity headroom. Reviewing — and if needs be, resetting — the incentivisation policy to consider cash flow rather than just contract size and revenue is vital.

Finally, **with M&A on the rise within the sector, this can backfire if the acquired businesses are integrated too slowly**. Acquisitions often take time to be fully integrated, and there are numerous examples where reporting processes/information of the enlarged group is not sufficient for management or stakeholders, there are cultural challenges with entrepreneurial businesses becoming part of larger organisations, and parts of the business operate in silos rather than as a joined-up group.

## What Next?

The tech race shows no signs of slowing. The speed at which change occurs in the industry means businesses can go from growth to distress in a flash.

Strong governance and robust financial reporting and processes will assist stakeholders in managing the business, investments and exposures; identify trends; and enable effective decision-making to maximise value. Getting this wrong can see value diminish and companies fall into restructuring scenarios where stakeholders may be forced to re-evaluate.



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<sup>1</sup> Statista, "IT Services: market data & analysis" (August 2024) <https://www.statista.com/study/108044/it-services-report> (page 8)

<sup>2</sup> Statista, "IT Services – Worldwide" <https://www.statista.com/outlook/tmo/it-services/worldwide> (page 9)

<sup>3</sup> Pitchbook, "Global M&A Report" (January, 2025) <https://pitchbook.com/news/reports/2024-annual-global-ma-report> (page 36)

<sup>4</sup> Statista, "IT Services – Worldwide" <https://www.statista.com/outlook/tmo/it-services/worldwide> (page 42)

<sup>5</sup> Statista, "IT Services – Worldwide" <https://www.statista.com/outlook/tmo/it-services/worldwide> (page 23)

<sup>6</sup> UK Government Policy Paper "New approach to ensure regulators and regulation supports growth" (March 2025) <https://www.gov.uk/government/publications/a-new-approach-to-ensure-regulators-and-regulation-support-growth/new-approach-to-ensure-regulators-and-regulation-support-growth-html>

<sup>7</sup> DLA Piper, "GDPR Fines and Data Breach Survey" (January 2025) <https://www.dlapiper.com/en-gb/insights/publications/2025/01/dla-piper-gdpr-fines-and-data-breach-survey-january-2025>