

OUTSOURCING APPLICATIONS MANAGEMENT

EUROPE

1992 - 1997

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**Outsourcing Information Services
Programme—Europe
(OEOSP)**

***Outsourcing Applications Management—
Europe, 1992-1997***

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Abstract

The scope of the outsourcing market in Europe is continuing to expand rapidly with services such as outsourced network management and desktop services now complementing traditional services such as systems operations.

Another emerging opportunity is the market for applications management where users outsource the development or maintenance of a range of applications. In recent years, this market has been targeted largely by specialist vendors such as FI Group. However, some of the leading European outsourcing vendors such as Cap Gemini Sogeti/Hoskyns are now positioning themselves more aggressively within this market, posing a challenge to the former specialists.

This report analyses the European market for applications management. In particular, it provides market forecasts by country and subsector, analyses of users' reasons for adopting application management and contract profiles, and details of leading vendors' offerings and strategies.



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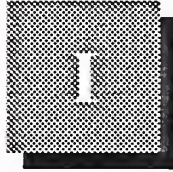
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Introduction

A

Purpose

The scope of the outsourcing market in Europe is continuing to expand rapidly with services such as outsourced network management and desktop services now complementing traditional service such as systems operations.

Another emerging opportunity is the market for applications management where users outsource the development or maintenance of a range of applications. In recent years, this market has been targeted largely by specialist vendors such as FI Group. However, some of the leading European outsourcing vendors such as Cap Gemini Sogeti/Hoskyns are now positioning themselves more aggressively within this market, posing a challenge to the former specialists.

This report analyses the European market for applications management. In particular, it provides:

- Market forecasts by country and subsector
- An analysis of users' reasons for adopting applications management
- An analysis of the nature of typical applications management contracts
- Details of users' future buying intentions
- Details of the offerings and strategies of five leading vendors

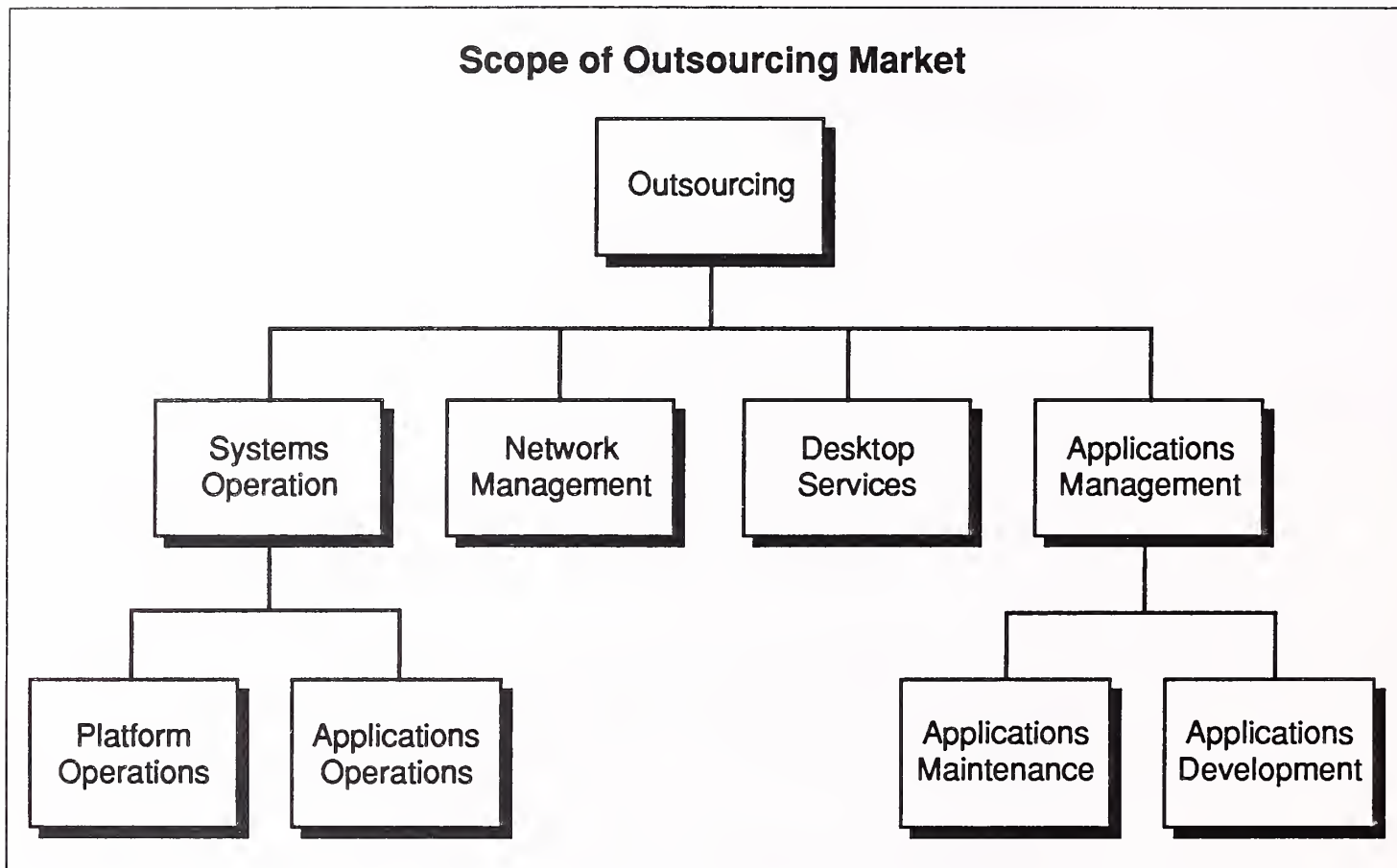
B

Scope and Methodology

This report is based on interviews with fifteen users of outsourcing services, 14 of whom use applications management services, and interviews with fifteen outsourcing vendors.

The scope of the outsourcing market is shown in Exhibit I-1.

EXHIBIT I-1



Each of these elements is defined as follows:

- Outsourcing - Contracting for all or a major portion of an information system function or process to a vendor on a long-term basis.
- Systems Operations - Contracting out, to a vendor, the information systems operations in either of two ways:
 - Platform Systems Operations - The vendor is responsible for managing the computer systems and their associated networks.
 - Applications Systems Operations - The vendor is responsible for developing and/or maintaining a client's applications software as well as operating and managing the computer systems and their associated networks.

- **Network Management** - Contracting to a vendor for the operation and management of the computer-related telecommunications network, transmitting data, voice, image, text, local- and wide-area networks. Voice-only network operations are not part of information systems outsourcing.
- **Desktop Services** - Contracting out to a vendor for the deployment, maintenance, support and connectivity of the firm's PC/workstation inventory. The service may also include performing the help desk function.
- **Applications Management** - The vendor is responsible for the development and maintenance of all the applications systems a client uses to support a business operation.
 - **Applications Development** - Contracting out for the design, development, and long-term maintenance and enhancement of new applications software associated with a business operation.
 - **Applications Maintenance** - Contracting out only for the maintenance of the existing applications software associated with a business operation.

Outsourced applications development management is typically associated with platform systems operations in comprehensive outsourcing contracts. In these instances, the revenues are included within the applications operations subsector rather than the applications management subsector.

C

Report Contents

Chapter II is the Executive Overview and contains a summary of the key findings of the report.

Chapter III provides market forecasts for the applications management market over the period 1992 to 1997. These forecasts are broken down by country and by subsector. The market shares of the leading vendors are also identified.

Chapter IV provides an analysis of organisations' use of applications management, concentrating on applications maintenance management which makes up the largest part of the European applications management market. In particular, the following issues are addressed:

- Users' reasons for adopting applications management
- The range of applications typically outsourced

- The nature of applications management contracts
- Users' future outsourcing intentions

Chapter V provides profiles of five vendors active in the applications management market. These profiles focus on vendors' service offerings and strategies and provide examples of applications management contracts.

Appendix A provides two applications management user case studies which were first published by INPUT in 1991.

D

Related Reports

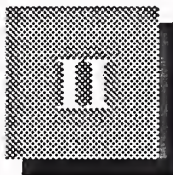
Information Systems Outsourcing Market Opportunities, Europe, 1992-1997.

Outsourcing Systems Operations, Europe 1992-1997.

Outsourcing Network Management and Operations, Europe, 1992-1997.

Outsourcing Desktop Services, Europe, 1992-1997.

Information Systems Outsourcing Competitive Analysis, Europe, 1992.



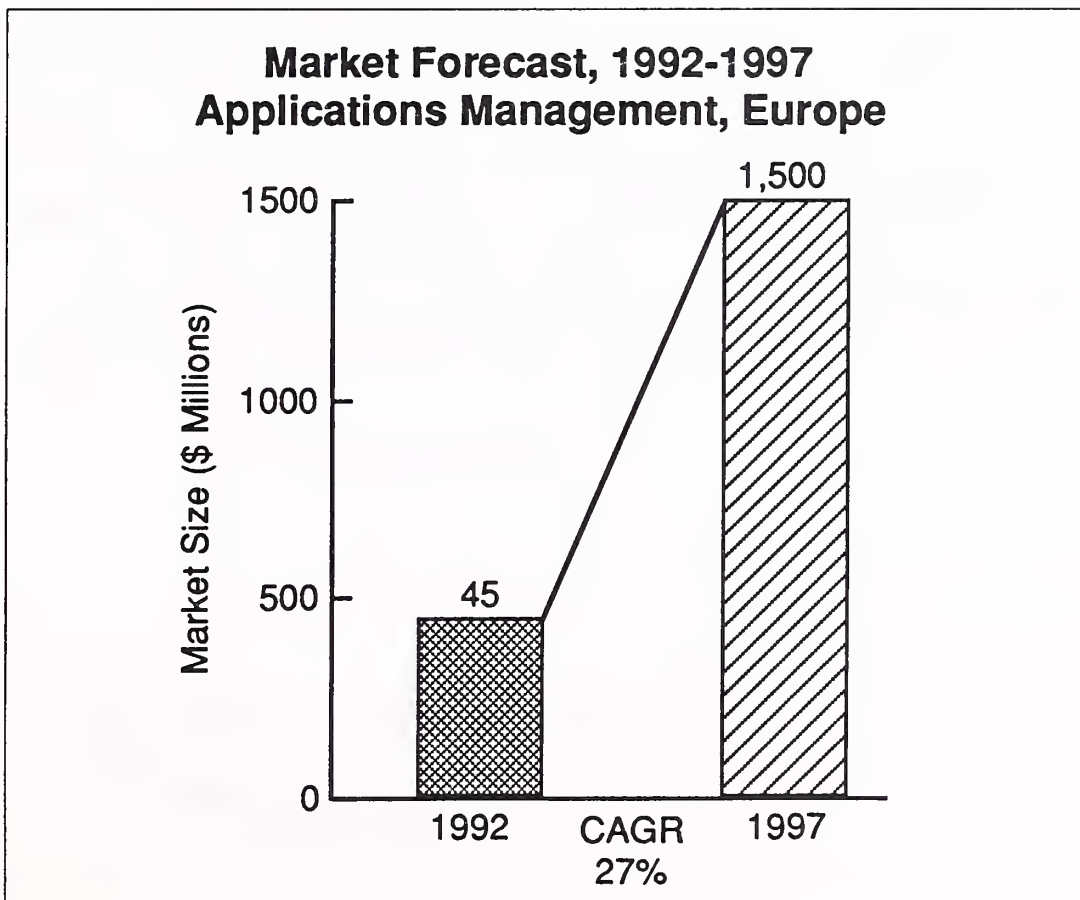
Executive Overview

A

Applications Management—Driven by Transition Outsourcing

Exhibit II-1 shows INPUT’s forecast for the European applications management market over the period 1992 to 1997.

EXHIBIT II-1



This market is forecast to show considerable growth over the next five years driven by the growth in applications maintenance management.

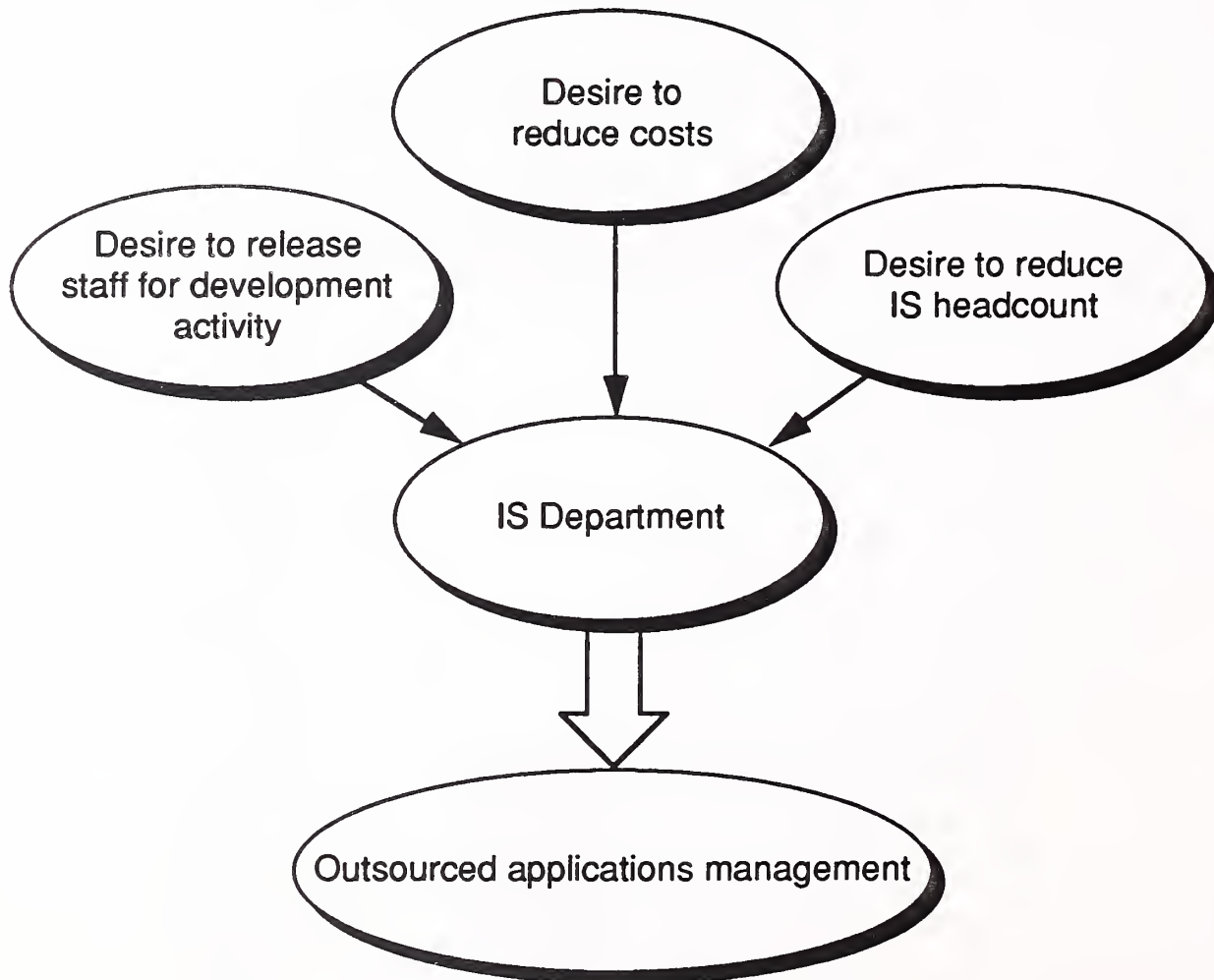
However, this growth will not arise from users' outsourcing of individual applications that are now proving troublesome to maintain.

Instead, users are expected to outsource the maintenance of all, or most of the applications running on particular equipment platforms.

The principal driving forces for this activity are shown in Exhibit II-2.

EXHIBIT II-2

Driving Forces Applications Management, Europe



The single most important influence is users undertaking transitions between equipment platforms, typically downsizing from mainframes to a more distributed architecture. In these instances, applications maintenance outsourcing is accompanied by outsourcing of the associated platforms.

In this context, users want to release in-house IS personnel who have been involved in maintaining the “old” systems, so that these personnel can contribute towards the development of the “new” systems to be implemented.

European IS departments are currently under considerable pressure to reduce their costs and to reduce their headcounts. Though it is important that vendors provide greater value for money than would be provided by an in-house service, the main cost savings to users accrue from replacing “old” in-house developed systems instead of marginally more efficient software maintenance.

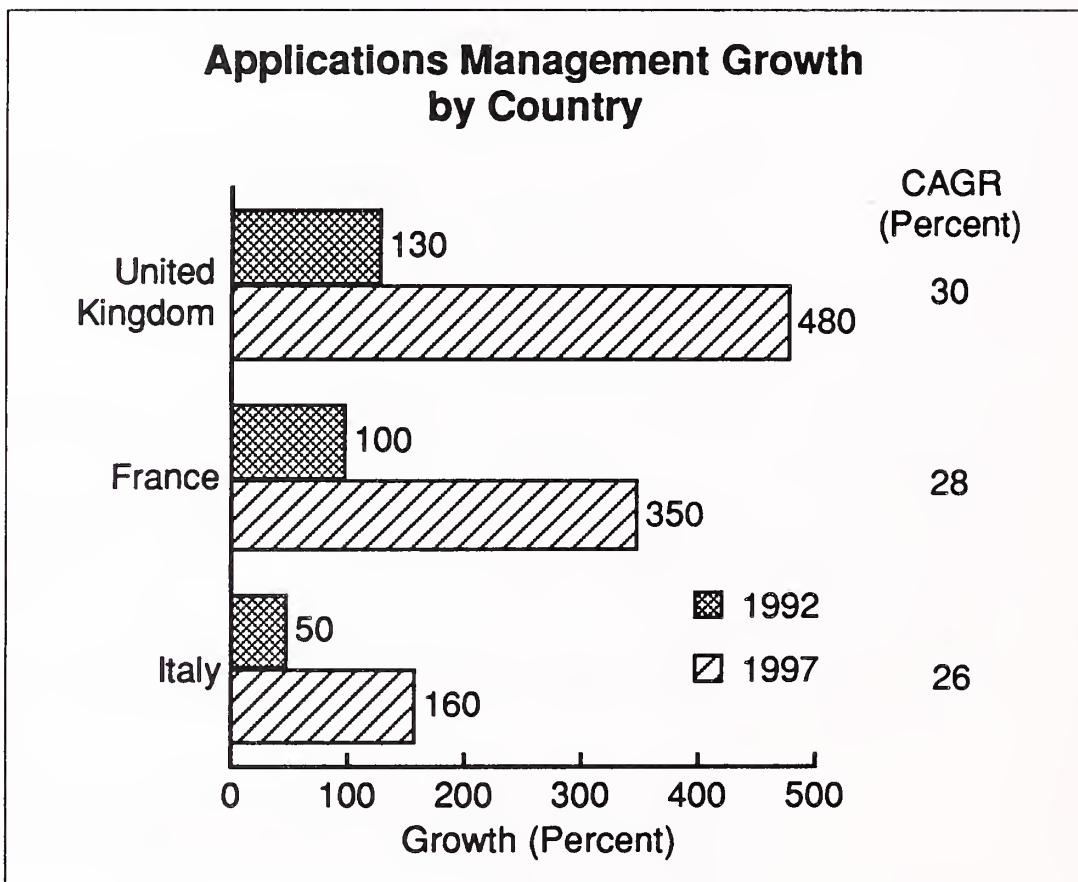
This pattern of outsourcing has the following implications:

- The market for applications maintenance management will be most developed in those countries with the most developed transition outsourcing markets.
- Users will tend to outsource a complete range of applications not individual applications in isolation.
- The principal outsourcing vendors such as Cap Gemini Sogeti and the Sema Group will present an increasingly serious challenge to the smaller specialist applications maintenance management vendors such as FI Group.

B
United Kingdom—The Most Developed Market

Exhibit II-3 provides the applications management growth forecast for the United Kingdom, France and Germany.

EXHIBIT II-3



The applications management market can be considered to consist of three main components:

- Applications maintenance management as a component of transition outsourcing services
- Applications maintenance management outside this context
- Applications development management

The proportion of the overall European applications management market accounted for by each of these elements in 1992 is estimated to be 71%, 18%, and 11% respectively. Although these proportions are forecast to change to 57%, 30%, and 13% by 1997, transition outsourcing will remain the major driving force behind applications maintenance management throughout this period.

Accordingly, the adoption of applications maintenance management by country will follow a similar pattern to the adoption of transition outsourcing. As a result, the United Kingdom and France are expected to remain the most significant country markets with Germany lagging some way behind.

C

Outsourcing a Generation of IS Systems

The profile of a typical applications maintenance management contract reflects this background of the replacement of a generation of systems as shown in Exhibit II-4.

EXHIBIT II-4

Profile of Typical Applications Management Contract

- Value \$2 million over three years
- Covers all commercial applications
- Cobol predominant language used
- Users highly satisfied

Typically, such a contract will cover all applications running on the platform or platforms to be replaced rather than individually chosen applications. Because these applications will typically be standard commercial applications covering accounting, payroll, and business administration, their predominant source language can be expected to be COBOL. At present, such contracts are typically expected to last for three years with average revenues of \$700,000 per annum. However, some vendors indicate that although years may represent the initial intention, the maintained applications can take significantly longer than this. The recipients of such services tend to be highly satisfied with the performance of the vendor used.

This has important implications for these organizations' future adoption of outsourcing. These implications are listed in Exhibit II-5.

EXHIBIT II-5

Future Outsourcing Intentions of Users

- Increases usage of outsourcing
- Principal services favoured:
 - Additional applications maintenance management
 - Network management
 - Desktop services

Firstly, the majority of the respondents stated that they would increase their usage of outsourcing in the future. This finding contrasts with earlier studies that have indicated that users of transition outsourcing would cease to use outsourcing services immediately after the transition period had ended. Transition outsourcing has always been the most popular outsourcing service with European IS Managers because it confined the outsourcing vendor to the chore systems leaving the chore system development activity in-house. This type of contract was especially popular because it was also envisaged as being comparatively short-lived.

European users are still reluctant to transfer new systems development activities to an outsourcing vendor. However, users of applications maintenance management services show a high level of propensity to outsource additional applications maintenance management. They also show high levels of propensity to outsource network management and desktop services. This may reflect their downsizing to distributed systems and then finding that their IS departments require additional assistance to manage the technically complex IS infrastructures on which their systems are now based.

D

Specialist Vendors Face Major Challenge

The leading vendors in the European applications management market are listed in Exhibit II-6.

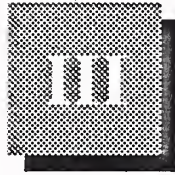
EXHIBIT II-6

Vendor	Revenues (\$ Millions)
Cap Gemini Sogeti	40
EDS	20
Sema Group	15
FI Group	15
Anderson Consulting	12

A significant share of the applications management market has historically been taken by specialist vendors such as FI Group who have not been positioned in the wider outsourcing market. As such, these vendors have been unable to offer platform operations services and have relied on their unique positioning as applications maintenance management specialists to capture elements of wider transition outsourcing contracts as well as standalone applications management deals.

However, the standing of these vendors is now threatened as the full service outsourcing vendors such as Cap Gemini Sogeti and Sema Group position themselves in this sector of the market. Once they have succeeded in achieving this and have demonstrated their own applications maintenance management capabilities, it will become more difficult for the specialist vendors since clients will frequently prefer to purchase all their outsourcing services from a single source.

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Outsourced Applications Management—Forecast to Grow at 27%

Exhibit III-1 shows INPUT's applications management market forecast for the period 1992 to 1997.

EXHIBIT III-1

Country	1992 Revenues \$ Millions	1997 Revenues \$ Millions	CAGR (%)
France	100	350	28
Germany	30	85	23
United Kingdom	130	480	30
Italy	50	160	26
Europe	450	1500	27

The major element of the market for applications management arises from organizations' use of transition outsourcing. Accordingly, the relative size of this market largely follows the overall systems operations market which is most developed in the United Kingdom and much less developed in Germany.

Nonetheless, with in-house IS organizations across Europe keen to adopt new generations of architecture yet facing steadily increasing pressure to reduce their costs and their headcounts, applications management is expected to show high levels of growth.

It is also a type of service which European IS Managers find less threatening than may other types of outsourcing service, and so has a comparatively high level of acceptability.

Exhibit III-2 provides a breakdown of the European applications management market by subsector.

EXHIBIT III-2

Applications Management by Subsector Europe, 1992-1997

Subsector	1992 Revenues \$m	1997 Revenues \$m	CAGR (%)
Applications Maintenance Management	400	1,300	27
- within Transition Outsourcing	320*	850*	22
- Standalone Contracts	80	450	40
Applications Development Management	50	200	32
Total Applications Management	450	1,500	27

Note: *Revenues included within systems operations market forecast.

The bulk of the applications management market in Europe arises from applications maintenance management. It remains comparatively rare for users to outsource applications development without also outsourcing the accompanying platform operations function. When both of these functions are outsourced simultaneously, INPUT classifies this type of service as applications operations not applications management.

One of the few known examples of applications development management is Hoskyns' contract with ICI Agrochemicals. In this case, ICI agrochemicals transferred its 57 system development staff to Hoskyns who gained preferred systems developer status in return. However, ICI Agrochemicals continues to use ICI's own data centers for delivery of services based around the applications developed.

The bulk of applications maintenance management revenues arise from transition outsourcing contracts in which a wider range of outsourcing services are used.

Where a wider range of outsourcing services is required, then this offers an advantage to full-service outsourcing vendors who can provide the client with one-stop shopping. In this survey approximately 60% of clients adopting transition outsourcing used the same vendor for both platform operations and applications maintenance management, and inability to offer the complete range of outsourcing services required was identified as one significant factor why vendors were not chosen for applications maintenance management.

However, this leaves 40% of cases where separate vendors were chosen for platform operations and applications maintenance management. In the United Kingdom, the FI Group has been particularly successful in positioning itself as a specialist in applications maintenance management and so separating the applications maintenance management contract from the platform operations contract within transition outsourcing requirements. However this may become more difficult in future as the leading outsourcing vendors recognize the potential of applications maintenance management and position themselves aggressively within this market.

Exhibit III-3 lists the leading vendors in applications management in Europe.

EXHIBIT III-3

<p style="text-align: center;">Leading Vendors 1992 Applications Management, Europe</p>		
Vendor	Revenues \$m	Market Share (%)
Cap Gemini Sogeti	40	9
EDS	20	4
Sema Group	15	3
FI Group	15	3
Andersen Consulting	12	3
Data Sciences	8	2
ITnet	8	2
IMI	8	2
Finsiel	5	1
K3	4	1
Total Listed	135	30
Total Market	450	10

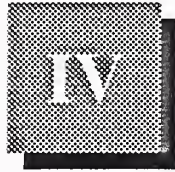
This list primarily reflects the vendors' success in targeting transition outsourcing in Europe. However, Cap Gemini Sogeti through Hoskyns has placed more emphasis on applications management as a separate service line in 1992, and the list contains several specialist applications management vendors, the most successful of which is ITnet.

The leading vendors in the United Kingdom are listed in Exhibit III-4.

EXHIBIT III-4

**Leading Vendors
1992 Applications Management, United Kingdom**

Vendor	Revenues \$m	Market Share (%)
Hoskyns	20	29
FI Group	8	11
Sema Group	7	10
Andersen Consulting	6	9
Data Sciences	4	6
ITnet	4	6
IMI	4	6
Total Listed	53	77
Total Market	70	100



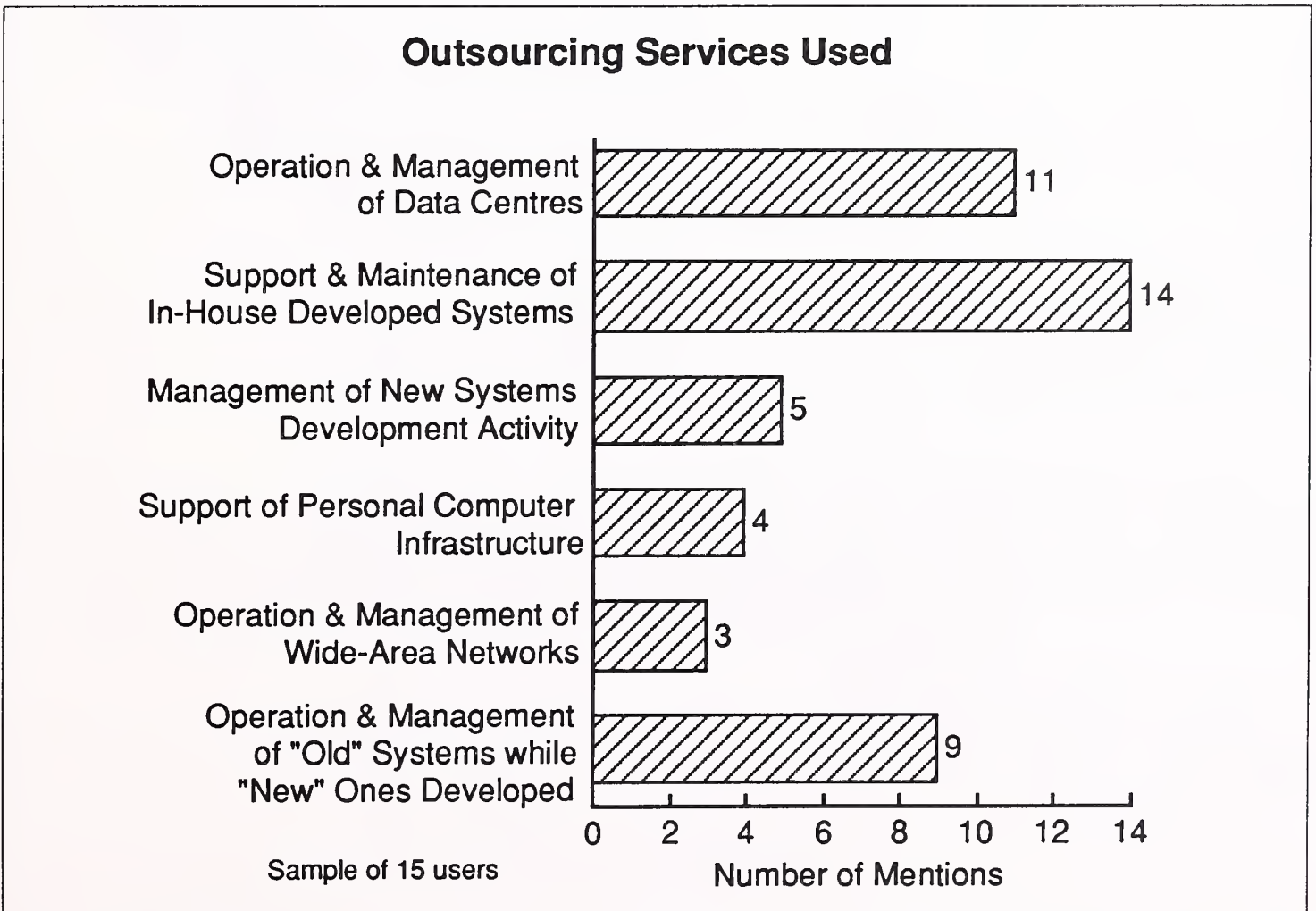
Transition Outsourcing Initiates Applications Maintenance Management

A

Users Outsource Maintenance Management to Release Staff for Development

Exhibit IV-1 identifies the mix of outsourcing services used by the sample of 15 outsourcing clients, whose activities are analyzed in the remainder of this chapter.

EXHIBIT IV-1



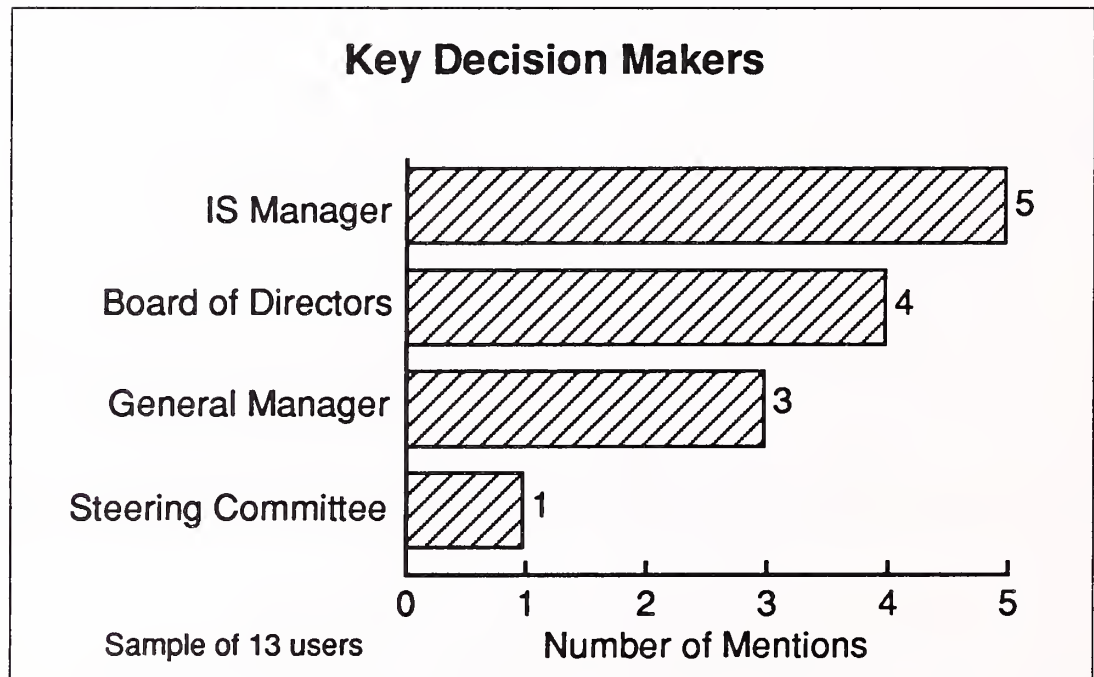
The sample was not random because it was specified that in order to qualify for the survey the respondent must be a user of either applications management or transition outsourcing services.

Nevertheless, the survey indicated that approximately 90% of transition outsourcing clients use applications maintenance management services. Indeed this element of applications maintenance management dominates the overall market for such services.

Hence, applications maintenance management is typically delivered in combination with other outsourcing services, in particular platform operations, rather than being delivered in isolation.

This has an impact on the buying process for applications maintenance management. If this service was sold as a standalone service, then IS management would be expected to be largely responsible for the purchasing decision. However, this is not the case as is shown in Exhibit IV-2.

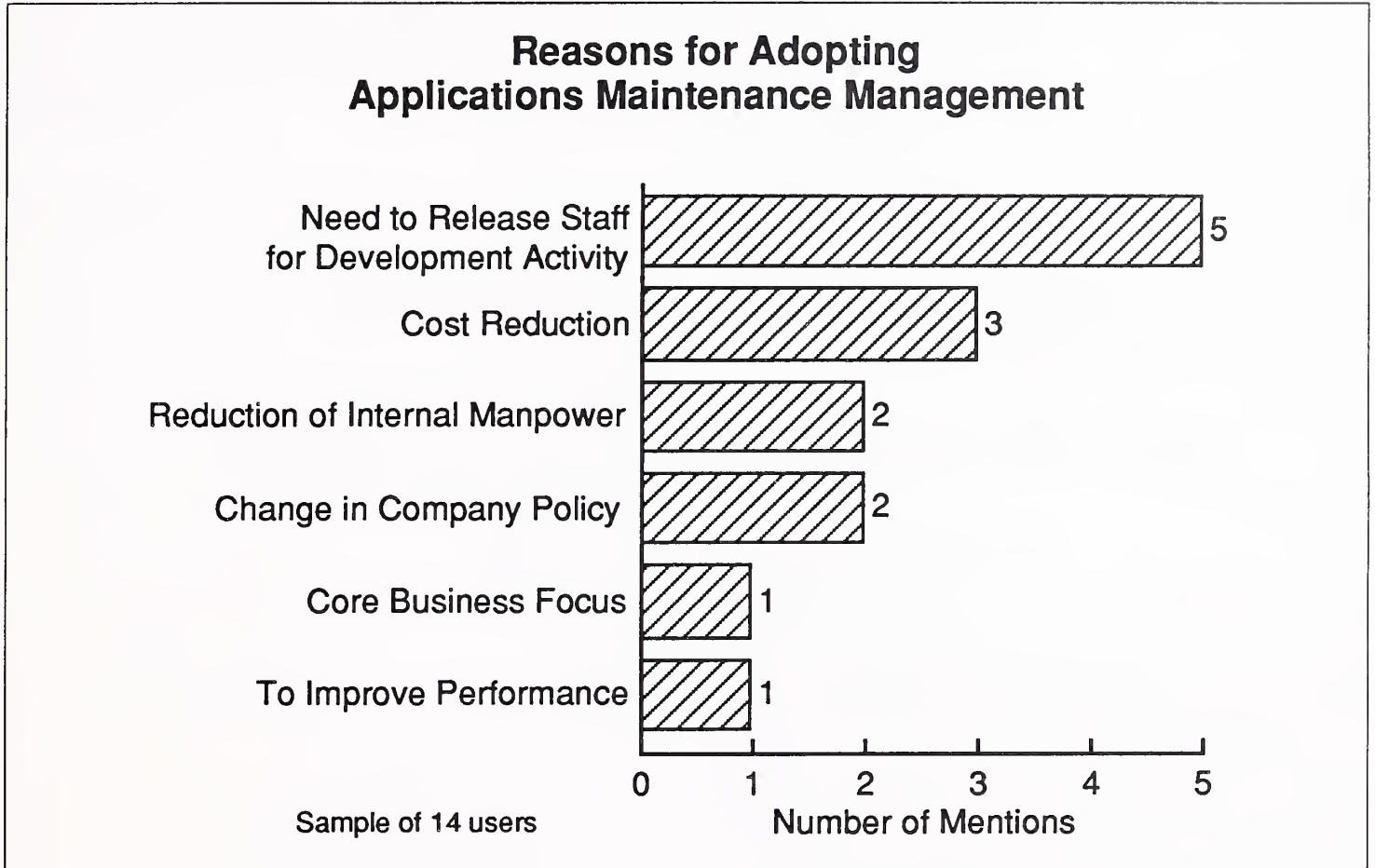
EXHIBIT IV-2



Here it can be seen that in 60% of instances the key decision makers were senior executives and not the organization's IS management. In those instances when only applications maintenance management services were supplied, then the key decision-maker in all cases was the organization's IS management.

The principal reasons for organizations adopting applications maintenance management are listed in Exhibit IV-3.

EXHIBIT IV-3



The main reason is to support the organization in the redevelopment of its IS systems by releasing staff from maintenance work to develop the organization's new generation of IS systems. It is estimated that between 50% and 80% of an organization's in-house IS manpower is devoted to the maintenance of existing applications.

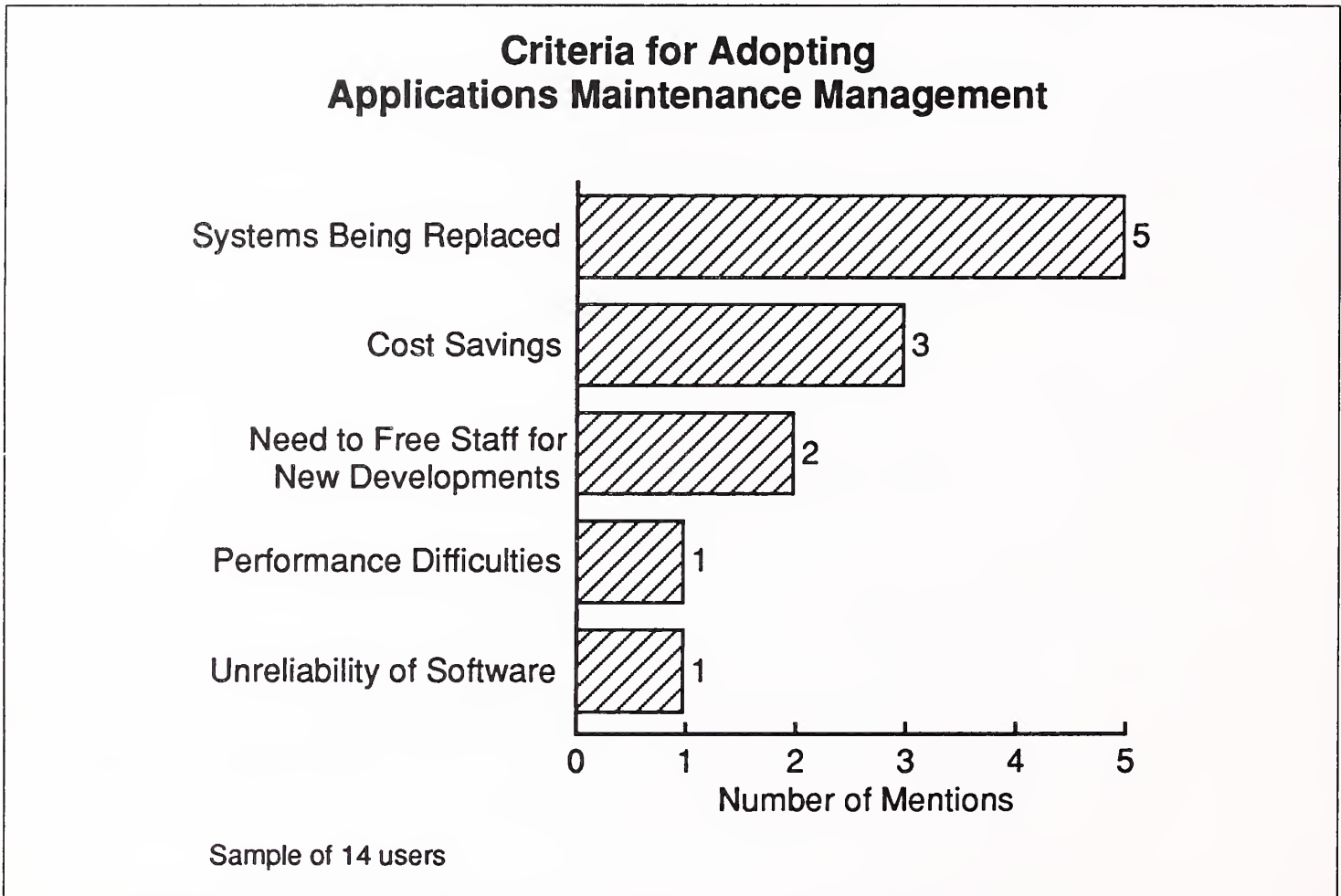
Downsizing is often characterized as reducing spending by replacing expensive equipment with lower cost equipment. However, downsizing also offers the potential for the organisation to escape costly maintenance of in-house developed applications software, and to move to a less maintenance-intensive environment.

Many in-house IS organizations are under pressure to avoid increases in their headcount, or increasingly to reduce their headcounts, and this is another significant driving force in organizations' adoption of applications maintenance management. In extreme cases, a number of organizations are now adopting a "core business focus" and endeavouring to avoid employing in-house IS professionals.

Surprisingly, poor performance by in-house developed software and maintenance difficulties received a low number of mentions.

Users were also requested to rate on a scale of one to five the importance of a number of factors in their decision to adopt applications maintenance management. A score of 5 indicated “very important” and a score of 1 “not at all important”. The number of times each criterion received a score of 5 is shown in Exhibit IV-4.

EXHIBIT IV-4



This again supports the view that the planned replacement of systems and the need to free staff to work on their successors are currently the major driving forces behind the outsourcing of applications maintenance management.

B**Applications Used On Average for Further Three Years**

Exhibit IV-5 indicates the profile of expenditure on applications maintenance management of the users surveyed.

EXHIBIT IV-5

Expenditure on Application Maintenance Management

Spend per annum	Number of companies
≤ \$100K	3
\$100 < \$500K	5
≥ \$500K	4
Average	700K

Sample of 12 users

The variation in spending is considerable because applications maintenance management encompasses situations where the user outsources the maintenance of a single application alongside situations when an organization is downsizing from a number of mainframes and wishes to outsource the applications maintenance management of all the applications resident on this equipment during the transition phase.

On average, organizations adopting transition outsourcing incur 30% of their outsourcing expenditure on applications maintenance management services.

It is commonly assumed that only applications which have been in use for periods of ten or twenty years are candidates for applications maintenance management outsourcing. However, this is not the case as indicated by Exhibit IV-6.

EXHIBIT IV-6

Age of Applications	
Age	Number of users
Wide range (1-20 years)	7
< 5	3
≥ 10	4
Average	7 years

Sample of 14 users

When applications maintenance management is being used to support a major transition such as downsizing, then applications tend to be outsourced regardless of their age. This leads to the outsourcing of applications with a wide spread of ages, typically from 1 to 10 years.

Overall, the age of applications does not appear to be a major factor behind the decision to outsource their maintenance, except that it is obviously an important contributor to the decision to replace them.

It appears that the decision to replace a group of applications, or a policy decision by senior management to reduce the organisation's IS headcount, are more important determinants of outsourcing than an application's age.

On average, organizations expect to continue to use applications that are the subject of applications maintenance management contracts for a further three years (see Exhibit IV-7).

EXHIBIT IV-7

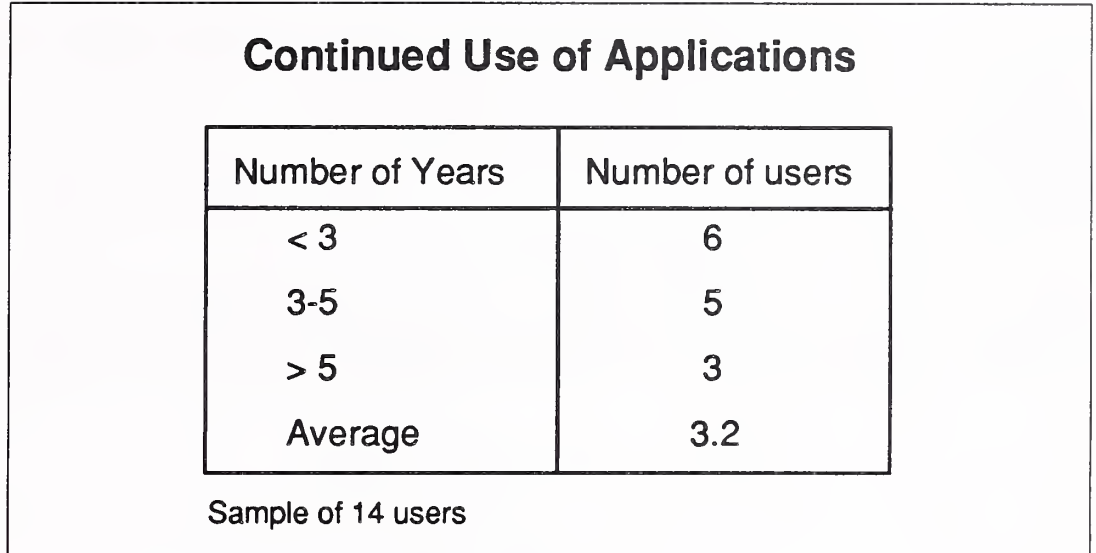
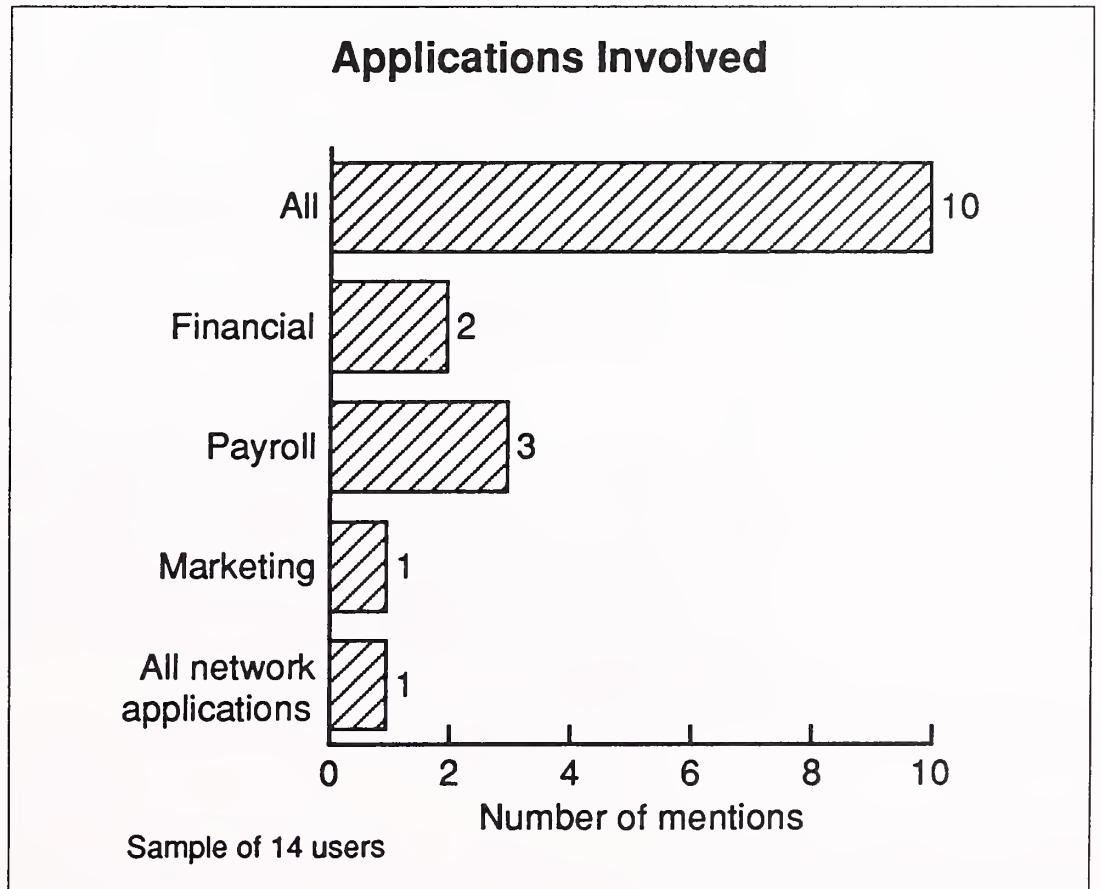


Exhibit IV-8 shows the types of applications being outsourced by the respondents.

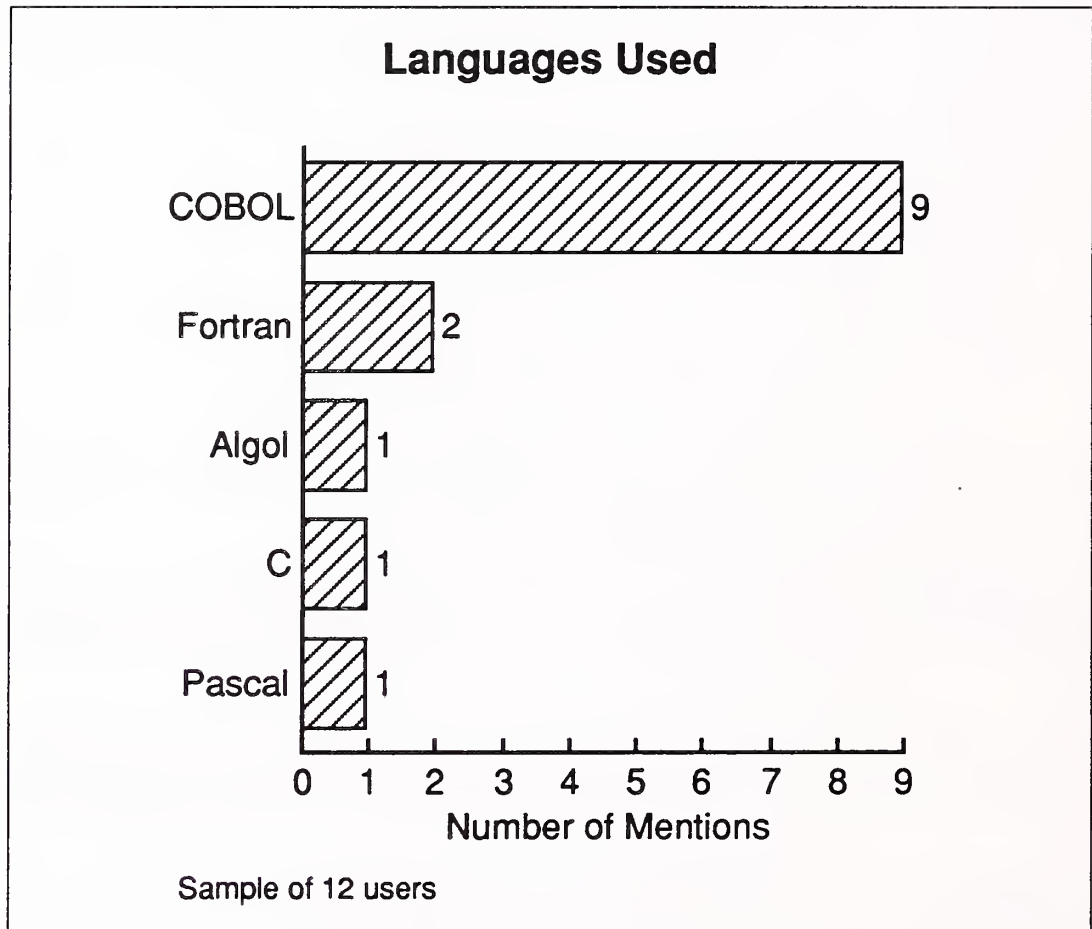
EXHIBIT IV-8



In 70% of cases, users were outsourcing all their applications maintenance on selected equipment. The remaining respondents tended to outsource a range of administrative applications, typically financial in nature.

The languages in which these applications were initially written tend to reflect their administrative background. COBOL is the principal language used as shown in Exhibit IV-9.

EXHIBIT IV-9



The emergence of the languages C and Pascal in this list offers encouragement to those vendors seeking to support users "new" systems, not their "old" ones. However, so far this is not a widespread trend. The respondent who indicated that these "new systems" would be maintained by an external vendor was a local authority in the United Kingdom, recognizing the political pressure from central government to adopt outsourcing of all its IS activities.

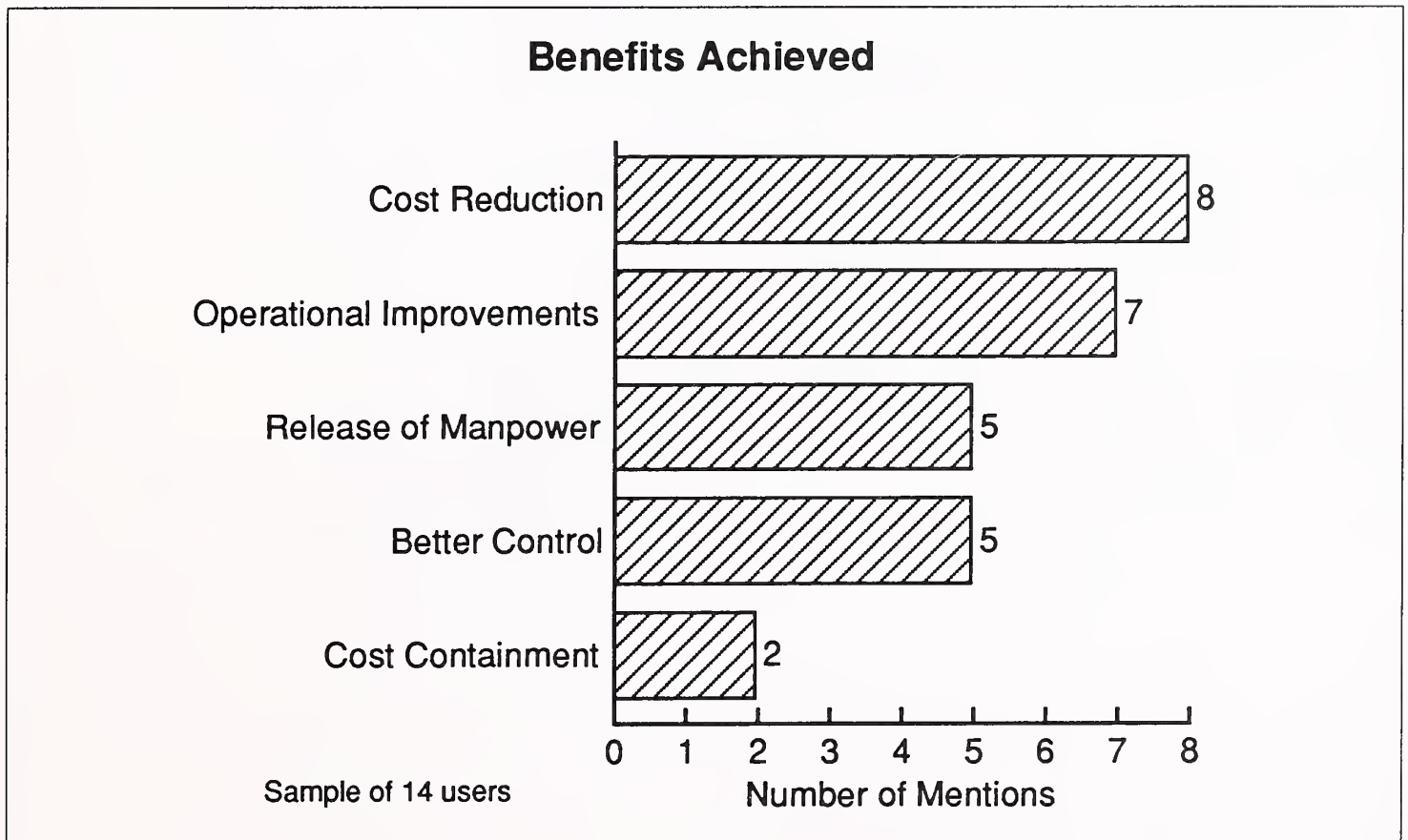
C

Users Impressed by Vendor Capabilities

INPUT asked the respondents to rate their satisfaction with the service received on a scale of one to five, where 1 represented “not at all satisfied” and 5 represented “very satisfied”. Users typically showed a high level of satisfaction with the outsourcing services they had received. The average vendor score was 4.1, and no vendor received a score of less than three.

Exhibit IV-10 lists the benefits that users felt had been achieved from outsourcing. Because the majority of respondents had undertaken a wider level of outsourcing than just applications maintenance management, it is difficult to identify the benefits accruing solely from this type of service.

EXHIBIT IV-10



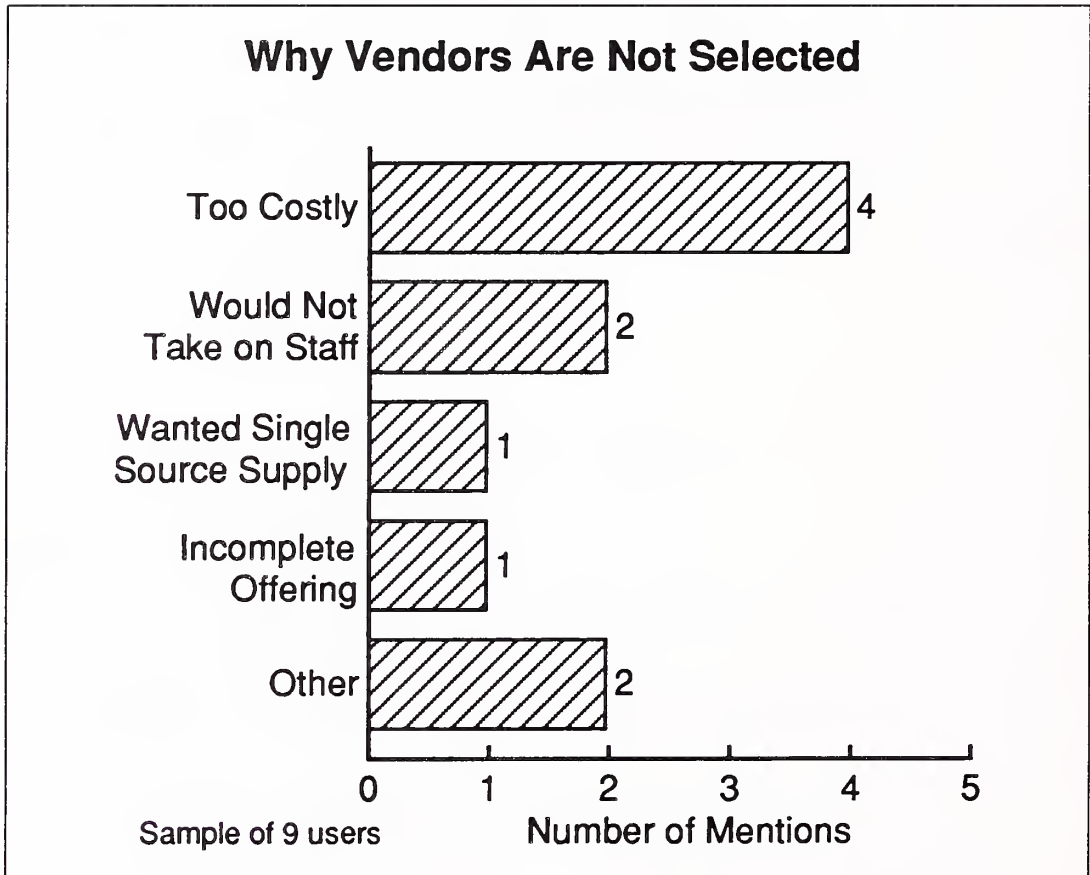
However, there is no reason to believe that the benefits achieved from applications maintenance management differ widely from these shown in this list.

“Cost reduction” and “release of manpower” were benefits cited as important by those respondents who were solely using applications maintenance management services and not a wider range of outsourcing services.

A possible handicap for vendors offering solely applications maintenance management services is that most of this activity takes place within the wider transition outsourcing context and some users will require a single source of supply for both platform operations and applications maintenance management services.

These reasons for rejecting vendors are evident in Exhibit IV-11 that lists the reasons why vendors were not chosen for outsourced applications maintenance management.

EXHIBIT IV-11



However, it is also apparent that many users are prepared to place contracts with separate vendors for platform operations and applications maintenance management services. In this survey approximately 40% of users requiring a wider transition outsourcing service awarded the applications maintenance management contract to a different vendor from the one supplying their platform operations services.

Users' future buying intentions are also encouraging for vendors. Exhibit IV-12 list the future outsourcing intentions of respondents, and shows that approximately 75% of these users will increase their usage of outsourcing over the next few years.

EXHIBIT IV-12

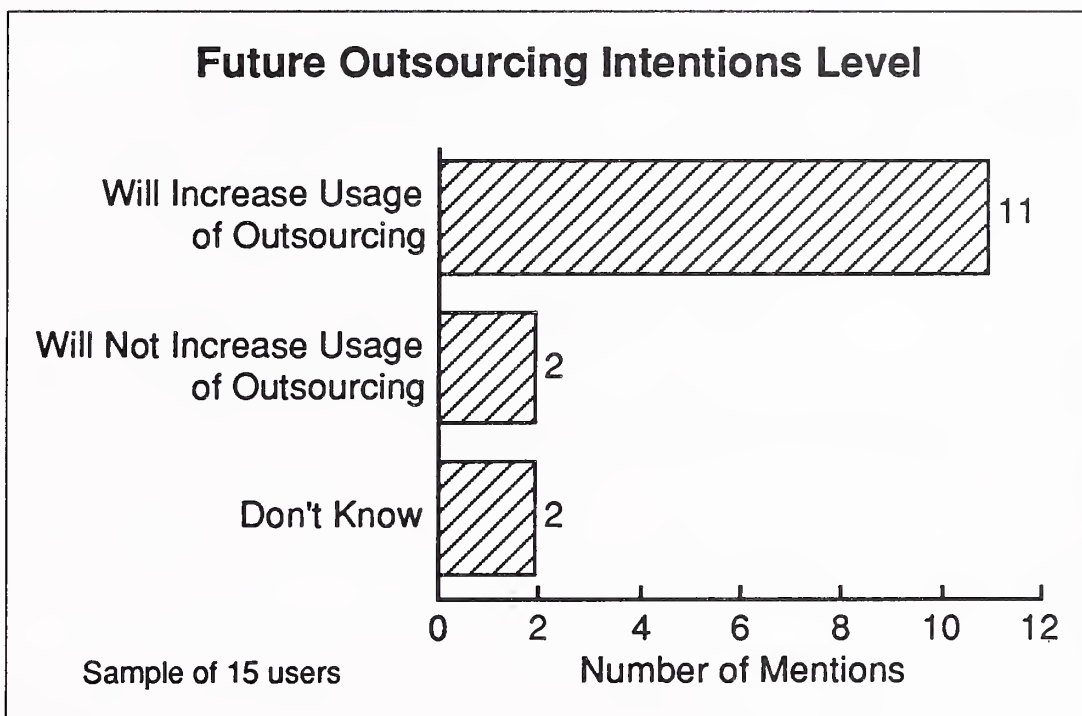
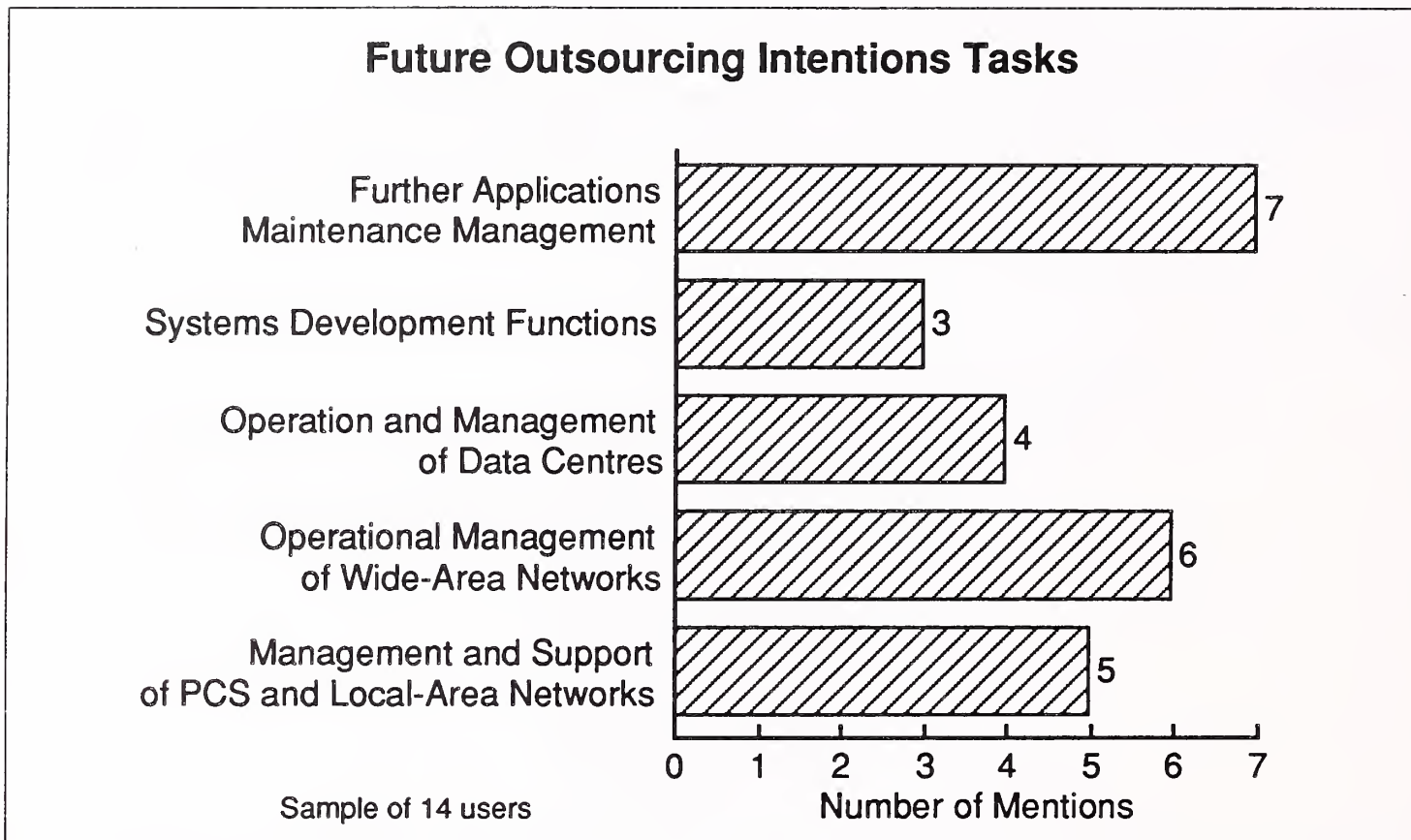


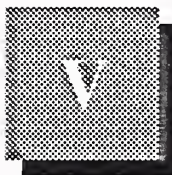
Exhibit IV-13 provides a more detailed breakdown of users' future outsourcing intentions.

EXHIBIT IV-13



Although this survey contains an element of bias in that it selected users with prior experience of applications maintenance management, Exhibit IV-13 shows the pattern which would be expected in Europe.

It is particularly encouraging for vendors of applications maintenance management that existing users of these services show a high level of enthusiasm for extending their usage of them over the next few years.



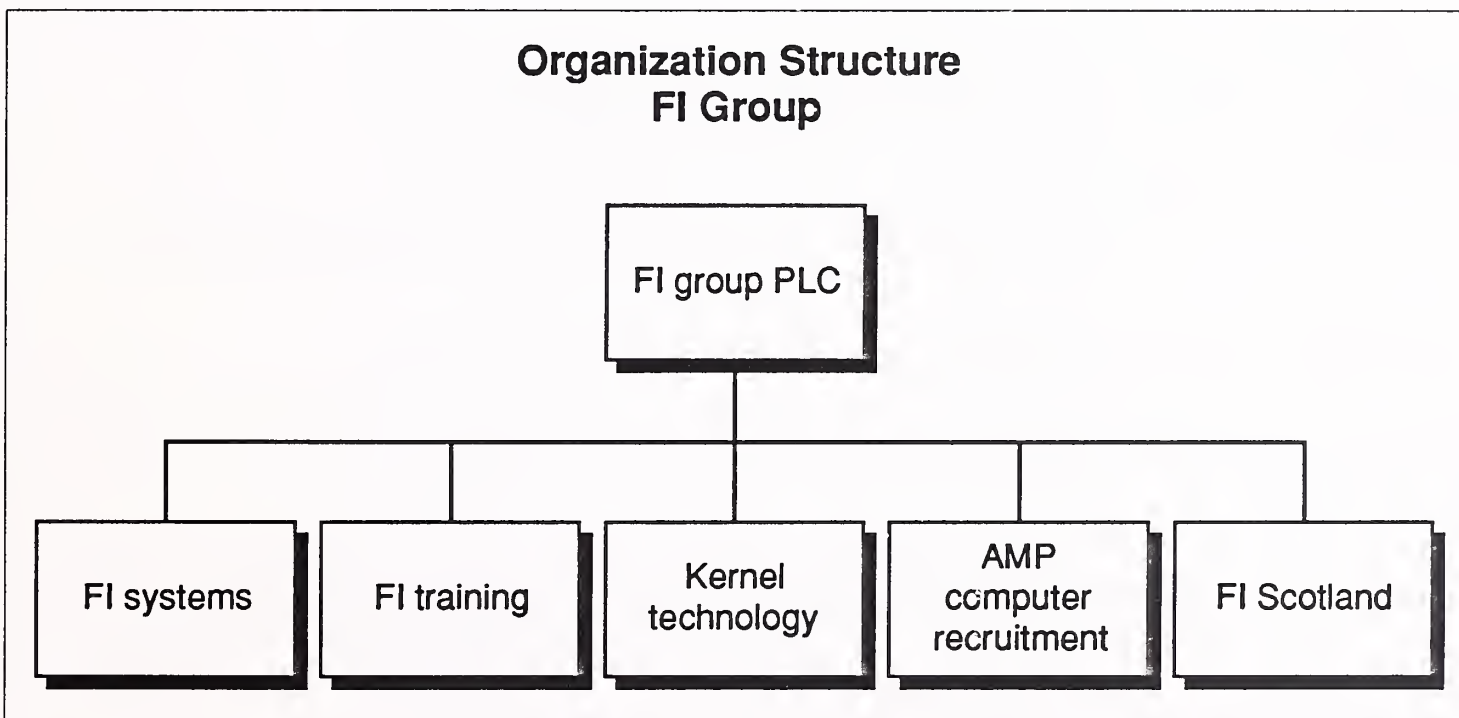
Specialist Vendors Face Increasing Challenge

A

FI Group—Over 30% of Revenues Derived from Applications Maintenance Management

FI Group is organized into the subsidiaries shown in Exhibit V-1.

EXHIBIT V-1



The group has recently acquired the Kernel Group, consisting of Kernel Training and Kernel Technology—a company specializing in open systems development, and AMP Computer Recruitment. As a result the FI Group now considers itself to be a rounded computing service group with business in systems, training, and recruitment.

However, much of the company's success can be attributed to MAIN-STAY—FI Group's applications support and maintenance service. For the financial year ended April 1992 the FI Group achieved revenues of \$47 million. At the present time, FI Group has approximately 25 applications maintenance management contracts contributing annual revenues of \$15 million. These contracts also give rise to professional services activity for Kernel Systems worth an additional \$3 million.

1. Management Process More Important than Technology

FI Group defines applications management outsourcing as "taking responsibility for part or all of the maintenance work for one or more of a client's systems". Maintenance is seen as everything after the first live operation of a system and the key issue is that of responsibility. The whole of the applications management service is provided under the title of "MAIN-STAY" and this comprises the following activities:

- The support of user communities and IT service groups, for example, operations staff
- The fixing of faults
- Answering user queries through a help desk
- Enhancements, that is agreed changes
- Preventive maintenance, that is to improve the quality of maintenance work
- Migration, that is conversion work
- Provision of support and maintenance methods such as change management and testing

FI Group has specialist consultants who concentrate on assessing the risk elements of projects and are very important in the project definition and startup process. The startup is defined as a systematic yet pragmatic method of defining the service delivery approach and the handover process. The first steps include:

- Defining service level requirements
- Assessing the quality of the systems
- Assessing current service provisions, strengths, weaknesses and risks to the business
- Establishing resource levels required

- Establishing procedures and working practices and a plan for handover

FI provides two key deliverables:

- The Approach Document, describing the requirement and how it will be met and implemented
- The Support Procedures Manual, describing the practical, day-to-day procedures for user interfaces, problem and change management, testing, handover, security, QA and service reporting.

A key success factor is in having a structured, practical and proven approach to applications management.

FI Group believes that technologies such as navigation tools, impact analysis, testing changes through compiler tools, data dictionary and code analysers do play a part in applications management, but only a small part. Much more emphasis is placed on tried and tested management techniques and effective procedures to ensure the success of the service.

In order to maintain the quality of the delivery a team of anything from 4 to 40 is dedicated to a customer or for small systems there may be one team for several customers. Subsequently a Service Manager ensures the meeting of the Service Level Requirements and the specialist team members are trained to gain a professional qualification such as the SSEB/BCS Certificate of Proficiency in Infrastructure Service Management.

2. Cost Reduction is the Principal Driving Force

FI believes that there are several major driving forces behind this market:

- The push to outsource from the public sector, as evidenced by the approach of compulsory competitive tendering, in other words, political pressure
- The recession and consequent business restructuring with a view to cost containment
- Specific skills shortages, for example, in the support of aging ICL systems, the requirement for rare skills such as that of PLAN programming
- The cost of hardware and software now available, for example, the wish to downsize, rightsize or to use object-oriented programming techniques

However, such factors as the general downturn in the economy and the consequent cancellation of projects, the use of client's own staff given the expense of redundancies, do provide some inhibition to the growth of the market for applications management.

The key benefits of applications management to users are:

- To gain a cost advantage over the comparable in-house support cost
- To enhance the performance and provide a better service to the user communities.

In addition, the vendor takes the day-to-day problems away from the IS or Financial Directors and sometimes provides the benefit of "added value" through being agents of cultural change, through instilling a more formal, commercial approach to system changes and through bringing to bear the wider range of additional skills of a specialist organization.

Overall FI Group believes that applications maintenance management should either:

- Provide a cost reduction for the same level of service
- Provide a higher level of service for the same cost.

3. Successful in the Financial Services Sector

FI Systems is organised into eight divisions:

- Time Top 500 private sector organisations
- Public Services (Central and local government and Health)
- Two Financial Services Divisions for Banks and Insurance and Investment organisations
- Commercial—Retail
- Commercial—The remainder
- Utilities including water
- Energy including gas and electricity

There are divisional managers and sales staff based in five offices (Hemel Hempstead, Altrincham, Basingstoke, Solihull and Edinburgh) which act as work centres and work is also carried out at customer sites.

FI Group has approximately 25 applications maintenance management contracts and appears to have achieved a high level of success in the financial services sector.

Example contracts include the following:

Ministry of Agriculture, Fisheries and Food. This has been a one-year renewable contract since 1989 where FI provides total support for the agricultural census system and a range of other applications systems.

Britannia Life. The provision of MAINSTAY service to support and maintain sixteen of Britannia Life's systems on a range of IBM, HP and PC systems. Its value over a one-year contract is \$660,000.

Property Holdings. Formerly a part of the PSA of central government, this three-year contract provides MAINSTAY services on ICL mainframe systems.

Midland Montagu. MAINSTAY support for a foreign exchange dealing system on DEC VAX and PCs using Windows. The contract was worth \$1,500,000 in its first year.

Barclays Bank. The maintenance and support of the MasterCard, Gateway and Interchange clearing system which started in 1990 and is worth \$470,000 per year but may reach up to \$4 million over a five-year period from its initial one-year contract period.

Some 60% of applications supported by FI Group are 20 years old, others are only just post live operation: the ratio is approximately 60:40 old: new. Typically the contracts are seen as a long-term measure by the client which is usually the IS department itself. Both FI and the IS department perceive the service provided to be better than the standard in-house service due to improved focus, and having teams trained to seek improvements using tried and tested methods. Contract lengths vary between one and five years but the most common is the year contract with a fairly automatic renewal.

B

Andersen Consulting—Applications Maintenance & Support Is a New Service Line

In the United Kingdom, Andersen Consulting is organised along the lines shown in Exhibits V-2 and V-3.

EXHIBIT V-2

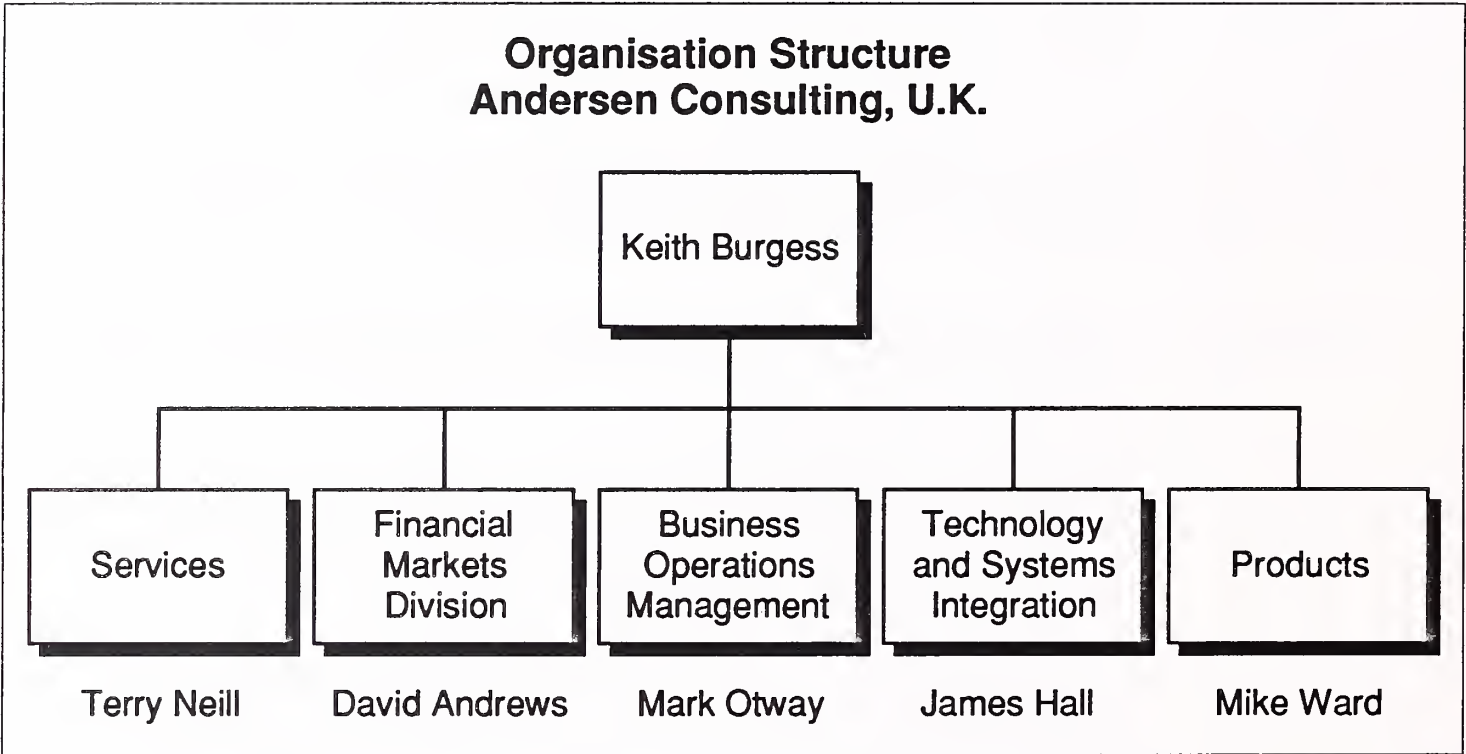
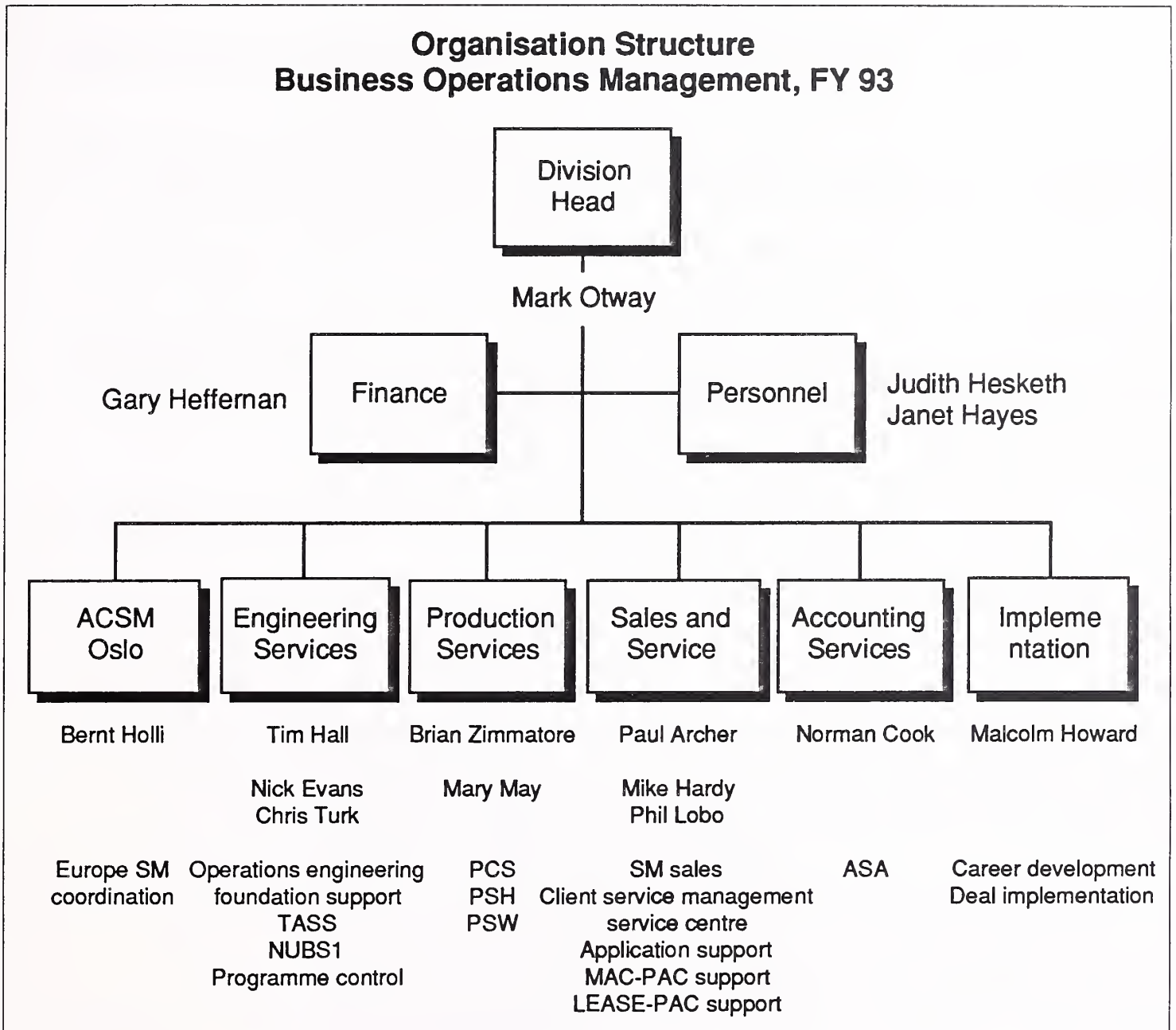


EXHIBIT V-3



The activities shown in Exhibit V-3 are as follows:

- ACSM Oslo—Andersen Corporate Systems Manager responsible for the coordination of the world-wide systems management methods and techniques called “Method/SM”.
- Engineering Services providing Operations Engineering services, consultancy within Business Operations Management (BOM), Foundation (a CASE tool), Programme Control (overall programme control of all projects within each client, thus involving staff control, re-engineering and the rationalisation of hardware) and some government projects.

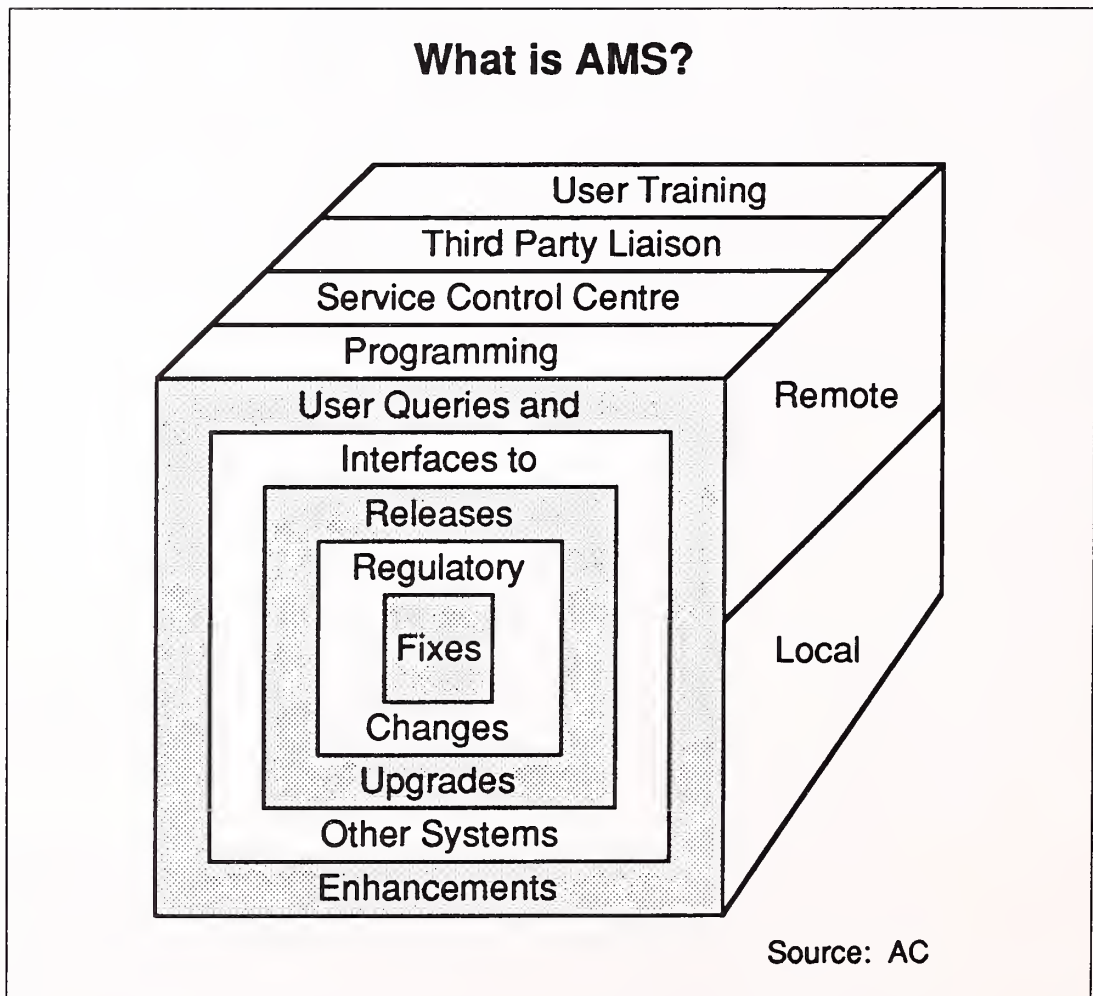
- Production services providing data centres in Bristol, Harrogate and London (the most recent).
- Sales & Service being primarily Applications Management and Support (AMS).
- Accounting Services being primarily the outsourced accounting activity of BP Exploration of Scotland, but new clients are being added.
- Implementation including the management of systems, particularly human resource issues.

The overall turnover of the Business Operations Management division in the United Kingdom is approximately \$110 million of which applications management accounts for \$12 million.

1. Method/SM—The Key to Success

Andersen illustrates their AMS definition and offerings through the use of a cube, shown in Exhibit V-4.

EXHIBIT V-4



The three faces or aspects to the business are:

- Mainstream maintenance comprising fixes to system or program errors, regulatory changes such as those in VAT and pay, upgrades or new releases to operating systems software, facilitating links to other software systems and user queries and enhancements.
- Additional related services such as programming, maintaining a Service Control Centre, liaising with third parties or suppliers and developing and delivering user training.
- The delivery of the above services either on on-site with the client or remotely through telephone/communications lines.

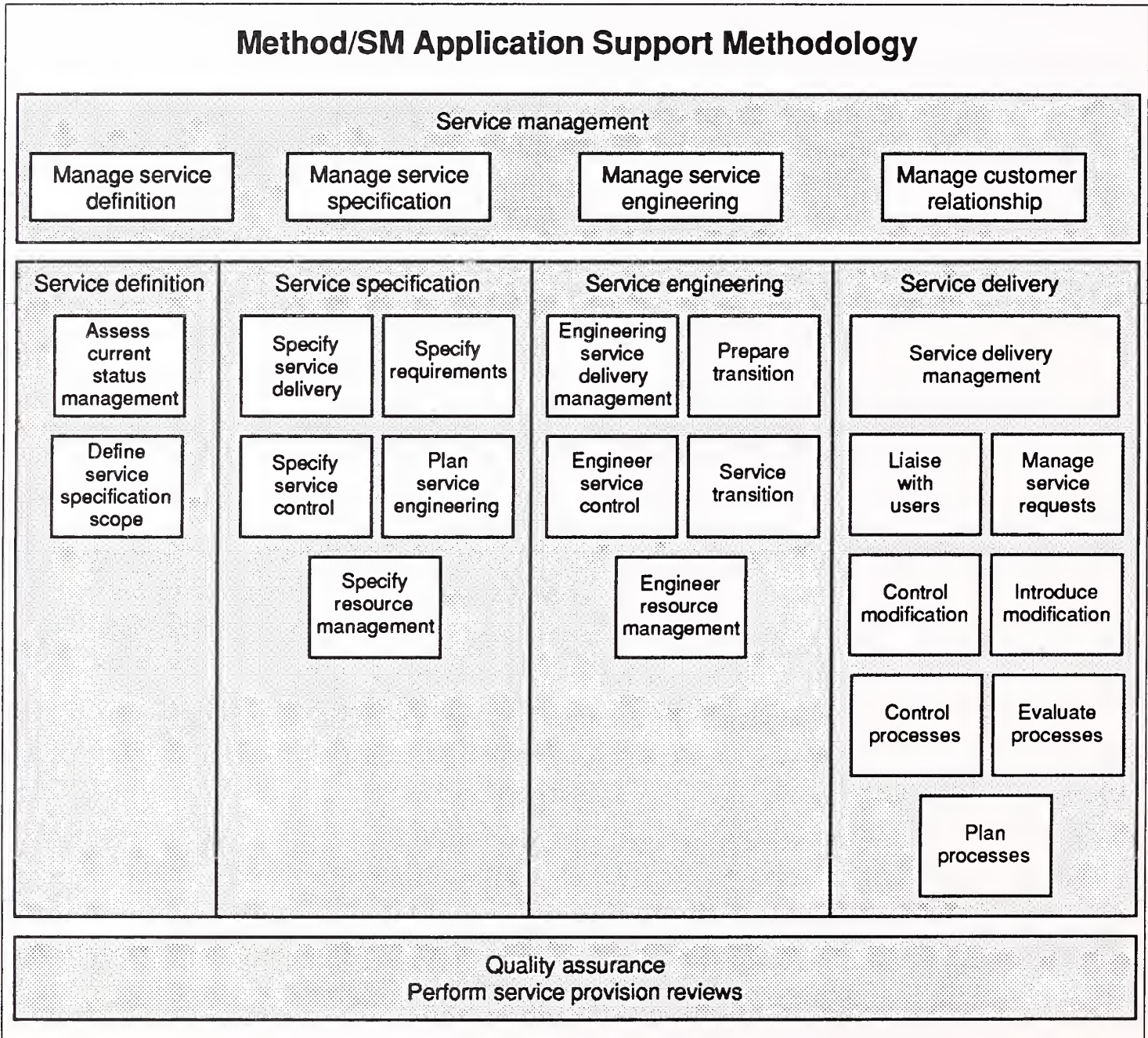
The Andersen approach comprises a number of key elements geared to meet the challenges of applications management, in particular the reliability and responsiveness of the system, control and focus (particularly cost control), appropriate management involvement and staff motivation. The key elements are:

- Service Level Agreement which is similar to that which they use for systems management contracts, defines the included and excluded services, target response and resolution times, the escalation process and sets the users' expectations.
- Personnel—the provision of dedicated managed resources, the use of Andersen consultants who are trained in their methods and tools, have a fast track career development and who are motivated and responsive to problems; staff are process-orientated rather than project-based thus providing a reliable, continuous service.
- A managed process providing problem and order management with logged problems, assigned priorities and completion, change control with appropriate authorization and thus minimised disruption and Service Review meetings to ensure regular liaison with key client personnel and formal reporting.
- Reliability—the assurance of delivery of services on time and to budget gained through the continuity provided by an external vendor.
- Reporting: a thorough approach providing reports at appropriate frequencies at differing levels:
 - Monthly Executive reports covering performance, utilisation, trends and strategic plans
 - Weekly management reports with performance, backlog and tactical plans

- User reports either hourly or daily dealing with problem status and closing.

Andersen Consulting's application support methodology is shown in Exhibit V-5

EXHIBIT V-5



Andersen Consulting believes that technologies such as FOUNDATION and code surveyors have their place but the real key to success with a client's applications management lies in the project management and methods and procedures, that is METHOD/SM, tailored to suit the client's

needs. Within their service provision, there is a corporate service methodology and tool set/work bench which provides facilities for account management, problem management and service level details on line and monitors customer agreements.

Through the formal service definition the particular services required by a client are specified and this is then passed to service engineers who organise the transition to Andersen management; the final phase is to provide continued service delivery to the client.

2. Demonstrate Accountability and Cost Control

Andersen plans to develop its position in the market place in the same way as they have developed in other areas—namely through direct contacts at a senior level in their clients and target market and through convincing senior executives of the credibility and practicality of their formal methods, in particular Method/SM for ASM activity.

AMS is a relatively new service line and Andersen is actively seeking further business through total system management deals and specific, AMS-only contracts. It is not setting limits on whether the service is provided remotely, locally or as a combination or whether the system was built by Andersen or by the client.

Andersen believes that the critical success factors in the AMS market place lie in the relationship with the client. It believes that seeking a growth in percentage market share would most likely damage its relationships with clients and would therefore prefer to grow its business through success with existing clients and through using their Method/SM as a differentiator. The main benefits to clients are seen as:

- Accountability and cost control through using an external commercial resource
- The protection of the investment of systems development and prolonging the life of a system through a more responsive and pro-active approach.

The typical age of applications is up to 15 years old and contracts are seen as long-term measures except in the case of systems running down, for example DRG. Contract lengths range from 3 to 7 years but 5 years is the most common. Clients tend to be IS managers in the main and the service is better than an in-house department can provide due to the differentiating factors of their formal methodology and the skills-orientated trained staff who are service rather than project-based.

C

Hoskyns—Leveraging its Transition Outsourcing Expertise

Hoskyns' European outsourcing revenues fell from \$128 million in 1990 to \$100 million in 1991. The company's revenues in 1991 were adversely affected by two factors:

- The conclusion of two contracts, together worth \$20 million per annum, with Plessey and the London Residuary Body.
- The fierce price competition in particular from new market entrants, for platform operations contracts.

In order to provide the company's outsourcing revenue growth in 1992 and take advantage of new market trends, Hoskyns has re-organised its outsourcing product lines into those shown below.

- Mid-range
- Mainframe
- Applications Management
- Desktop Services

These services can be delivered to clients either individually or in combination and will enable the company to take advantage of three new trends in the market, namely:

- The growth of outsourcing on mid-range equipment
- The need for IS management to outsource the maintenance and enhancement of existing applications
- The growth in the market for desktop services

Hoskyns currently has 43 applications management clients generating revenues of approximately \$40 million.

The contracts can be split into two types:

- Those solely involving the support of existing systems
- Those including both support and applications development

The bulk of users' in-house manpower resources continues to be committed to the support—both maintenance and enhancement—of existing systems. IS managers now need to release some of this resource to enable new developments to take place. Cost pressures in the current recessionary economic climate typically prevent IS organisations from increasing

their headcount to tackle this challenge. Accordingly this is creating an opportunity for vendors such as Hoskyns to take-over the management of the existing applications base for clients. Examples of this type of contract are those with PowerGen and Prudential Holborn.

However, some companies are taking a still more radical approach to the problem of varying IS manpower requirements. For example, ICI Agrochemicals has outsourced both the support of existing applications and its system development activities to Hoskyns. This enables ICI Agrochemicals to transfer its fixed IS manpower costs to a variable cost which can be increased or decreased according to the company's systems development needs.

Hoskyns also benefits from its traditional strength in transition outsourcing.

The two pressures of wishing to reduce the costs, particularly of maintenance which has been estimated to be up to 80% of the costs in a mature installation, and the continued wish to move to newer technologies are the key factors in AM development.

Hoskyns is very confident in the growth of this area of business, even if in the short term it may be at the expense of new project development work. It sees the chief benefits to be:

- Cost reduction or control of the heavy maintenance activity in mature installations
- The freeing up of internal resources to create new applications with new technology
- Extending the life of applications through smart enhancements such as the improvement of response times and graphical front ends thus maintaining or increasing the acceptability to the users

Hoskyns targets organisations which are effectively household names, since they have been involved with information systems for many years and typically are IBM or ICL mainframe users or large Digital users. Further, they are likely to have more than 20 staff dedicated to support functions. Hoskyns does not focus on particular industries or applications but are currently gaining approximately equal business from existing outsourcing clients and from completely new clients. Hoskyns believes that the critical success factor for the business is in actually delivering the main benefit of reduced costs. In the past savings on running a data centre were seen to be enough but now maintenance, or applications management, is seen by many clients to be of greater value, since it frees up the client's existing staff to work on new projects with new technology.

Concerning pricing and contracts, Hoskyns takes a typically simple, commercial and effective approach. Initially there is an agreement of the number and type of resources (staff) to form a core team and an agreed preferential rate for the use of additional or top-up resources. This may be determined through a short, low cost study if the client will bear it but increasingly Hoskyns appears to have been asked to provide quotations based purely on documentation from the client. Clearly the less study possible the higher the risk, but in times of recession it is important to bid and win as much business as possible.

Contract lengths range from one to five years but the most typical length is for three years. It would appear from Hoskyn's annual revenue of approximately \$20 million for applications management with 43 clients that the average contract value is about \$0.5 million. Example contracts include:

- ICI Agrochemicals—a three-year contract worth \$10 million supporting applications software, providing preventative maintenance and enhancement, particularly the front end of systems using graphical user interfaces
- Prudential Assurance—another three-year contract for application software maintenance
- Calor Gas—a three-year application software maintenance contract.

The applications supported on these contracts are about five years old on average, but some are only a year old, others were inherited from the original outsourcing contracts and may be well over ten years old. This support is both temporary and permanent—it is totally dependent on the client's perception—on some occasions a client may consider a five-year period to be temporary, others may consider six months to be temporary but the contract is then renewed many times. The issue here is simply the need to decide what period of time is strategic or long-term and what is not. Hoskyns believes the reasons for providing a better service than an in-house IS department are better utilisation of staff (for example, using a fraction of a person for one client's application in a work period, whereas the client cannot achieve this) and having a wider experience of certain technical areas and tools (for example, the use of the CGS tool for code analysis).

Whilst technology and tools are seen as essential ingredients of the offerings of a high tech supplier, their role in the provision of applications management is seen to be rather more cosmetic than real. It is difficult to find proof of the efficacy of such things as CASE re-engineering tools. Having said that, they are evidently keen to promote the use of CGS tools, to use quality standards, monthly metrics and of course their own project management tool PMW.

D**IMI Computing—Offering Risk-Free Outsourcing**

IMI Computing has annual revenues of approximately \$50 million. The company has 240 staff based in three centres: the head office at Birmingham, London and Edinburgh. The company has been targeting applications management for a number of years and has approximately 10 clients for its applications maintenance management services.

The company has four operating divisions:

- Applications services
- Contract services
- Installation services
- Offices services

The Applications Services Division supports every aspect of the application life cycle in four main areas:

- Business/computer system design
- Development & Implementation
- Maintenance & Enhancement
- Replacement & Re-engineering

IMI is very confident about its applications management activity and sees the chief benefits to clients as the following:

- Increasing productivity without a cost increase
- Reducing cost while maintaining productivity
- Freeing up valuable staff for development work
- Providing the benefits of outsourcing without the risk, i.e., a client can use a number of vendors for Applications Management contracts, whereas with outsourcing he became committed on both hardware and often all systems management.

With the continuing recession, IMI believes its customers are unable to increase their head counts within the computer systems department, but that this does not stop the users demanding greater functions and features, or more friendly systems, such as Windows and other graphical user interfaces. In addition, for many applications there is a distinct lack of packaged systems available and often a lack of specific skills in house. Despite the inhibiting factors of frozen budgets, the lack of commissioning of many large new systems or activities, IMI believes that it will succeed

through its approach of moving away from the standard systems operations for hardware and concentrating on applications management. The idea behind this is simply that the client keeps the core systems and IMI takes the chore systems.

In addition, they believe they are demonstrating creative and innovative approaches for their clients, particularly with respect to maintenance (for example, building a windows style front-end to an old VMS system to make the old system more acceptable to the users).

IMI believes that the key success factor from the clients' perspective is that the major changes in organisations are causing an increased drive towards reducing head counts and costs whilst either maintaining or increasing productivity. Success for IMI is critically dependent on an even more coherently integrated sales and support activity, with appropriate quality procedures in place.

IMI targets large IBM, AS400 or LAN client server computer installations. Its main clients are the IS departments in the insurance and manufacturing industries and the public utilities.

IMI plans to develop its presence in the market through further integration of this service offering within its portfolio. It sees a convergence in the market place of Business Re-engineering, Network Management and Applications Management. Through the continued provision of innovative services including management reviews twice a year, professional Help Desk function, provision of contractors at preferential rates and some free consultancy, it further expects to develop its presence. Whilst IMI has only strictly speaking been in the business of applications management for 2.5 years, it has been in the business of large systems management for 20 years and is currently experiencing tremendous growth.

Concerning pricing and contracts, the way IMI approaches the problem is to insist on an applications audit first. This takes between a week and a month and is not expensive to the client since the fee rates charged are more in line with cost recovery than professional fee rates. However, at the end of the audit, IMI has a system map of the applications, including such items as the number of nodes in a system, the number of lines of code, calls, Application Program Interface calls (APIs) and so on. IMI can thus present its findings and propose to set a level of service and to guarantee to either:

- Increase productivity and maintain costs
- To reduce costs and maintain productivity

Typically contracts are for about a year in length but are mostly renewed by clients. They claim not to have lost a client except in one case where IMI recommended the use of another third party company for an unusual, specific client. The typical value of contracts is on the order of \$1 million with the largest proportion coming from maintenance. Examples of contracts include:

- Client A spending \$200,000 on a Help Desk contract
- Client B spending \$1 million on a complete maintenance contract

Maintenance contracts are for systems of almost any age from zero to 10 years; such support is either temporary (one case for a company wishing to privatise) or permanent based on the renewable one-year contract.

Technology is important to IMI and its offerings, so it endeavours to maintain a competence in a wide range of tools and methods, particularly CASE (upper and lower) for examples LBMS, Yourdan, IBM Case/DB2, Maestro, Synon and CAST—the integrated support environment where modifications and updates are tested on a work station rather than on the mainframe.

E

ITnet

ITnet has been a service organisation for approximately 30 years and started life as the “Jamaican Coffee Company”—a subsidiary of Cadbury’s which provided the company’s computer services. It became an independent company in 1987 with 240 staff and began a systems operations contract with Birmingham City Council in 1989. With Simon Ricketts at its head, it turned over \$30 Million in 1991 and has 500 staff, approximately half of whom are IS professionals (including project leaders, analysts, designers and programmers). Approximately half of its revenues are captive.

ITnet focuses on large FMCG organisations, local government and the finance and service sectors. It has had particular success in supporting those organisations using Millenium—a financial application software product from Dun & Bradstreet. It believes that there are a number of major driving forces for applications maintenance management:

- The need for cost cutting to be more efficient with a lower cost
- The wish to have fixed and controlled costs, contrasting with earlier client experience and the actual high cost of maintenance, estimated to be anything up to 70% of the IT budget.

- The need for a client to retain systems knowledge despite aging of the systems and staff turnover.
- To focus existing staff on core and strategic projects

The main success factors are in actually delivering the promised cost savings or increased efficiencies through providing the right staff with the right skills sets in a flexible way. These benefits, together with the removal of the worry of managing technical staff and improvements in reliability and maintenance are seen as the key benefits to a client.

ITnet has approximately 12 applications maintenance management contracts providing annual revenues of \$8 million.

The company's applications maintenance management offering provides a customised service to provide any

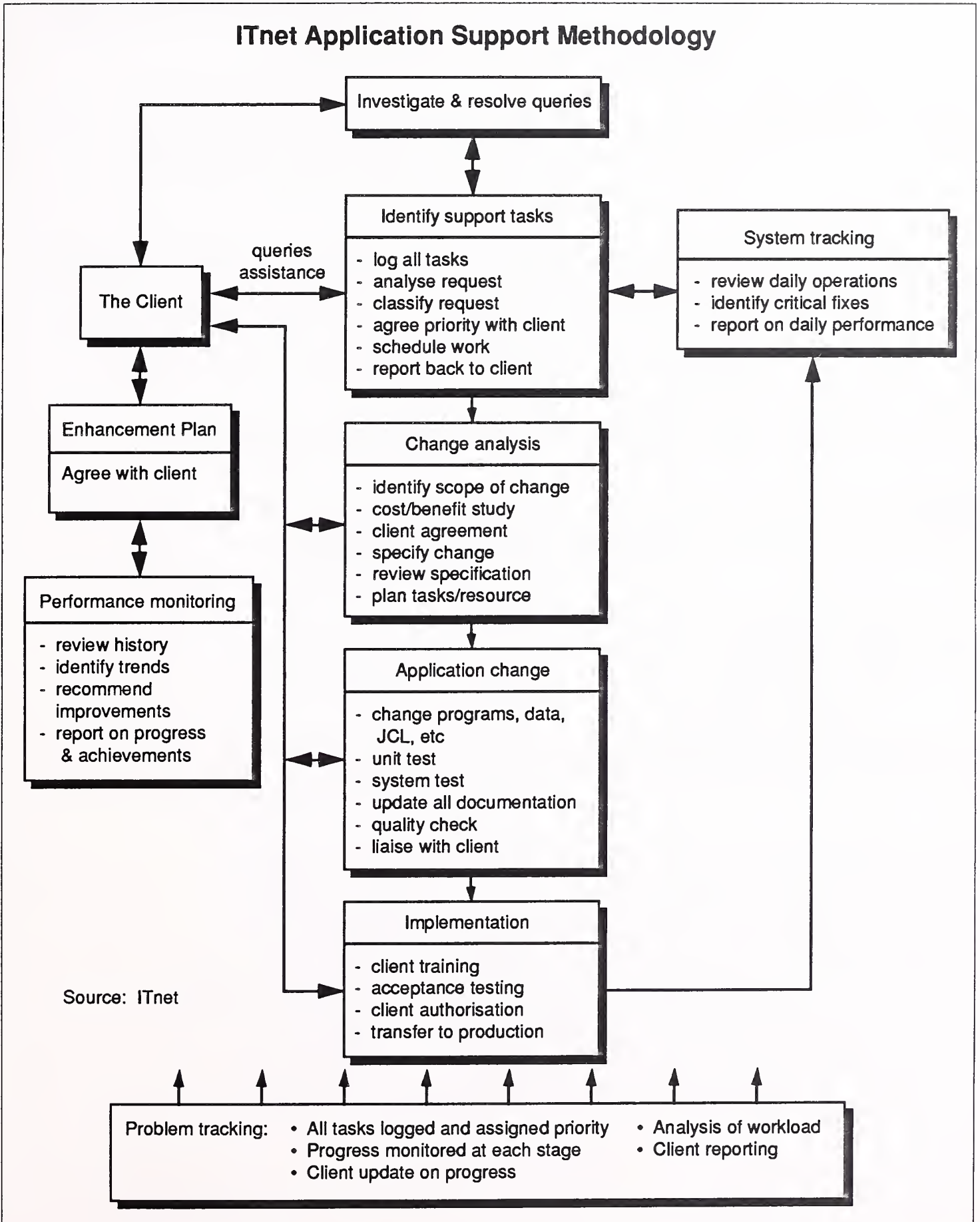
- Help desk
- Problem resolution
- User assistance
- Enhancements: evaluation through to implementation
- On-site or remote site options

ITnet is currently organised into five groups for service delivery, namely:

- Project managers to manage the individual projects for a client
- Business managers who retain account management for all activities for a client
- Applications support group for mainframe, mid-range and PC support
- Development group for the development of new systems (this is likely to reduce in size as packages continue to have 80+% fit with clients' requirements).

ITnet's methodology for applications maintenance management is shown in Exhibit V-6.

EXHIBIT V-6

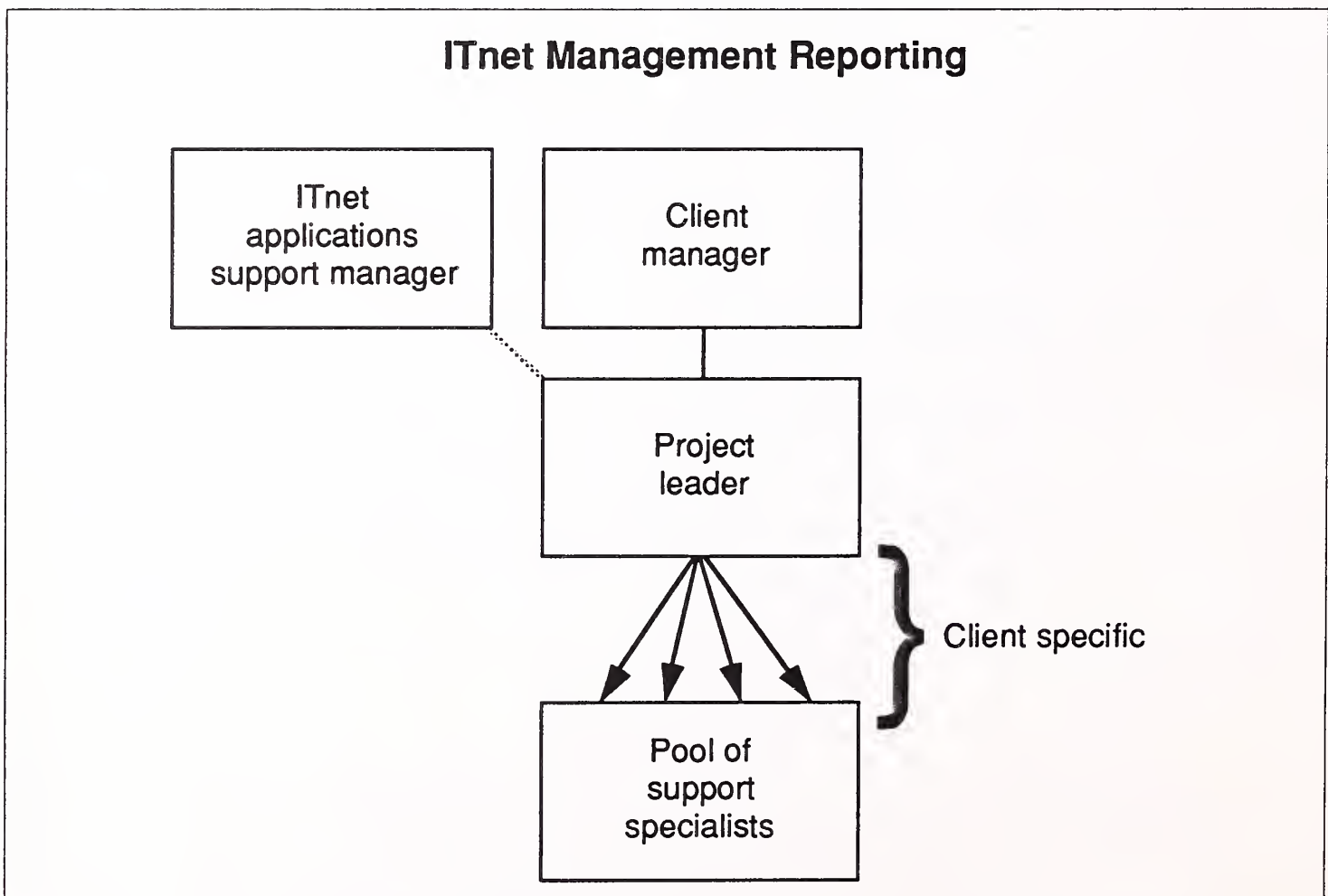


ITnet establishes a clear set of service levels for every applications support project providing the client with a clear view of the service and its minimum level, with only minor fluctuation and guaranteed resource availability. Service levels typically cover the following:

- The extent of support covered (hours per day, week and year)
- Guarantees to log, prioritize and follow-up every call or incident
- A definition of priorities related to the business
- A schedule and definition of regular management reports to be provided
- Minimum percentage of high priority tasks to be resolved in a day
- Initiatives to be undertaken to stop recurring problems and improve performance

Exhibit V-7 shows the reporting structure used for each project.

EXHIBIT V-7



Client calls for assistance are routed through the ITnet Help Desk to the Applications Support Help Desk to the pool of support specialists as shown in Exhibit V-8.

ITnet believes that technologies such as Telon and Code Surveyor have their place but the real key to success with a client's applications management lies in the project management and methods and procedures tailored to suit the client's needs.

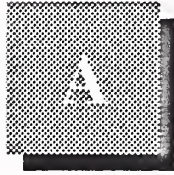
Example contracts include the following:

- CCSB (Coca Cola Schweppes Bovril) - This is a three-year contract worth \$1.7 million per year where ITnet provides applications management support for the Sales and Marketing, distribution, customer accounting and PC systems.
- Tarmac - A further three-year contract generating \$200,000 per year providing applications support, primarily on payroll using Peterborough software. (ITnet claims to have specialist knowledge of Peterborough Software's products since they are in use with many clients).
- Cadbury International - A three-year contract providing support on the Dun & Bradstreet Millennium financial and accounting software generating \$130,000 per year.
- Westminster City Council - About to be announced is a seven-year contract for a complete systems operations and applications management outsourcing. The value of the applications management activity is estimated at \$1 million per year.

Many of the company's applications maintenance management contracts are combined with other services such as network management or systems operations.

The majority of the applications are about 20 years old and include some PLAN and COBOL-based systems, but some of the new clients have provided some new or recently developed systems for support. Typically the contracts are seen as a long term measure with contract lengths being three to five years although most commonly at the lower end of the range. Clients tend to be IS or Finance Directors in the main, since IS staff tend to wish to buy or hire people rather than a service contract. In other cases, the client may be a general manager or a development controller (in a Building Society) where these are the budget holders. Sometimes contracts are of a shorter duration, for example 12-18 months, when the application is being run down prior to replacement. ITnet and the IS

department see the service as better than the standard inhouse service due to the focus caused by it being one of ITnet's core businesses, having teams trained to use tried and tested methodology and being perceived as being "lean and mean".



User Case Studies

A

Case Study 1

EXHIBIT A-1

User Case Study—Government Sector— Scenario

IS Objective

- Improve user service/lower costs of economic model

Old Age Problems

- Plan to replace suit of applications
- Some software 20 years old
- Many change requests still
- Obsolete systems hardware/software
- Boring for staff, poorly documented
- High security site

Exhibits A-1 and A-2 summarise the experience of a Government department in contracting out the maintenance and support of a very old database application used for assessing the economic impact of EEC and local policy changes on a national industry.

The objective of contracting out to a third party was to improve the service received by the end-user and to lower the costs of running the service. Some applications are over 20 years old, and although the number of code changes is small, end-users are continually requesting changes to the application parameters and database fields.

To add to the difficulties of keeping the end-users satisfied, the applications run on an old mainframe using an obsolete operating system. The support staff were poorly motivated and eager to acquire a replacement system. The site and the application are subject to high security regulations.

Three vendors were invited to tender. The solution adopted after a careful analysis by the vendors meant a hand-over period of three months, during which one or two of the eight staff remained available to train the vendor's employees.

The final terms of the service were a fixed price for an agreed level of support service, plus a time and materials portion for responses to end-user special requests.

EXHIBIT A-2

User Case Study—Government Sector— Outsourcing

Solution—Outsourcing

- 3rd-party staff working on-site
- Mix of time-and-materials and fixed-price
- 3 months parallel working hand-over
- Users interface direct with vendor

Benefits

- >50% cost saving on staff ≈\$740K p.a.
- 8 full-time staff replaced by 4 part-time
- System life extended 5 years
- Vendor handles all staffing

Perhaps the most interesting aspect of this example is the way the IS department passed full responsibility to the service vendor who now deals directly with the end-user department on all issues.

The potential cost of any changes is now visible to the end-user management in the form of costed quotations. This has allowed the end-user to improve his own decision-making as to the cost effectiveness of changes being requested.

The exercise has been very successful, freeing eight IS staff for use on other projects, reducing the overall workload and dramatically improving the reliability of the system. This has enabled the replacement plans to be put off, freeing the budget for other uses.

The improvements in reliability are a spin-off from the vendor's strong management methods applied to the whole applications software environment. Far less time is now spent analysing and fixing problems (down to only 5%), or re-inventing solutions to problems which have occurred before. This has allowed the vendor to negotiate a lower cost service level which still satisfies the end-users needs.

B

Case Study 2

EXHIBIT A-3

User Case Study—Telecommunications Sector— Scenario

IS Objective

- Free-up staff & improve user service in materials management

Problems

- Demand for new business systems
- Database growing out of hand
- 5-year history of fast fixes to software
- Bad system response times
- 23 people—fire-fighting support

The second case study is outlined in Exhibits A-3 and A-4. It concerns a large IS group within a Telecommunications PTT, where there is tremendous pressure for new applications which reflect a more customer-facing business stance. Freeing up IS staff with valuable business knowledge was the main objective of considering outsourcing some support and maintenance activities.

The application chosen was a major inventory and warehouse management system implemented at several locations for a regionally organised end-user management.

The five-year-old system had been treated like most heavily used applications—speedy fixing of problems had taken precedence over elegant solutions. So short-cuts had been taken, resulting eventually in some response times, at peak hours, being totally out of hand.

With 23 people employed in supporting the applications, it seemed an excellent test case on which to judge the promises of the service vendor.

In this case the knowledge transfer required to release 19 of the in-house support and development staff took six months. There was also considerable spin-off in knowledge transfer to the computer operations staff, as the vendor applied improved working practices to establishing a stable and reliable software environment.

EXHIBIT A-4

**User Case Study—Telecommunications Sector—
Outsourcing****Solution—Outsourcing**

- 3rd-party took prime responsibility
- Mix of in-house and 3rd-party staffing
- 6 months for knowledge transfer
- Client's quality system
- Planned reviews under client's direction

Benefits

- 19 staff released for new projects
- Users happy—good response times
- Call-outs reduced ten-fold
- System reliability and life extended
- Working practices adopted by client

The vendor established procedures for configuration control, software testing and release, which conformed to the users own internal quality procedures and standards. In fact considerable energy was put into establishing a tight teamwork approach with shared office space and good communications at all working levels.

The results were exceptionally good, with response times down to a level at which it is going to be hard to find an adequate replacement system in the future. There is no doubt that the system's life has been extended by pro-active management—compared to its previous reactive fire-fighting status.

The original high level of end-user complaint has given way to silent satisfaction and the original 24-hour emergency service level has been reduced to a normal working hours service.

Many of the new working practices introduced by the vendor have been adopted by the IS client management.

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