STRATEGIC MARKET PERSPECTIVE

Outsourcing Opportunities in Government

Europe, 1993-1998

Outsourcing Information Systems
Programme–Europe

OUTSOURCING OPPORTUNITIES IN GOVERNMENT

EUROPE, 1993-1998

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Abstract

Central Government departments have often been a source of major systems integration projects for external vendors. However these departments have typically been reluctant to outsource the management of IS functions.

Such outsourcing of IS functions is now beginning to occur in Europe, driven by governments' desire to obtain higher levels of value for money. This is particularly evident in the United Kingdom where the government's market testing initiative is leading to major opportunities for outsourcing vendors.

Traditionally local government has shown a higher level of propensity to outsource than central government, and the growth in outsourcing in local government continues to accelerate. In addition to IS outsourcing, significant opportunities for business operations outsourcing are emerging in the local government sector. In this respect, local government may be establishing a trend which will also be increasingly adopted by central government departments.

This report identifies the outsourcing opportunities which are emerging in the local and central government sectors in Europe.

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*Outsourcing Opportunities in Government—
Europe, 1993-1998*

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Introduction

A

Purpose

Traditionally the government sector in Europe has been a minor component of the outsourcing market. The principal opportunities in Europe so far have been in local government. Those local government bodies who have outsourced elements of their IS functions have tended to be served by specialist vendors, such as Finsiel in Italy, and CFM and Capita Group in the United Kingdom.

However, as European governments face increasing pressure to reduce public expenditure, they are seeking ways of achieving better value for money from the use of IS in central and local government. This is most pronounced in the United Kingdom with the development of the market testing and compulsory competitive tendering initiatives.

Such initiatives are extending the scope of outsourcing in the government sector in terms of the services offered and the magnitude of the opportunity. Outsourcing contracts with values in excess of $100 million per annum will emerge from central government departments over the next few years. These contracts present opportunities for new entrants to the European outsourcing market who can demonstrate either experience of handling contracts of such magnitude, for example in the U.S., or the ability to take the financial risks inherent in contracts of this magnitude. This report aims:

- To identify the outsourcing opportunities emerging in the government sector in Europe

- To identify the trends in outsourcing in local government

- To identify the nature of the opportunities arising in the central government sector

- To forecast the demand for outsourcing services in local and central government in Europe and in each of the major countries.

B

Scope and Methodology

This report is based on a mixture of face-to-face and telephone interviews with fifteen users and vendors active in outsourcing in the government sector.

For the purposes of this report, the government sector is defined as local government and national (or central) government, excluding the health sector.

INPUT views outsourcing as a change in the form of the client/vendor relationship. Under an outsourcing relationship, all or a major portion of the information systems function is contracted to a vendor in a long-term relationship. The vendor is responsible for the performance of the function.

INPUT considers the following submodes to be outsourcing-type relationships and in aggregate to represent the outsourcing market (See Exhibit I-1).

EXHIBIT I-1

**Outsourcing Components
INPUT's View**
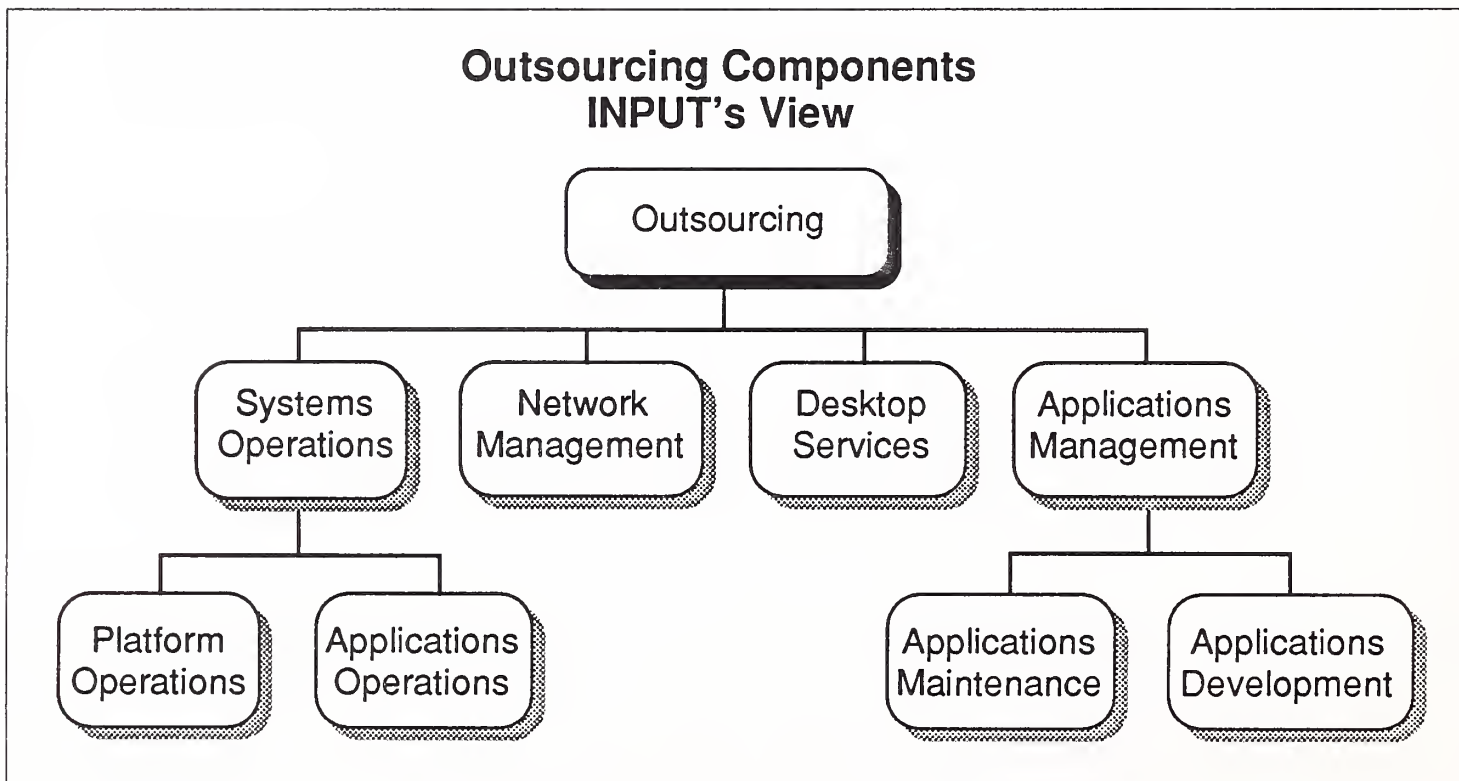
Outsourcing - This entails contracting for all or a major portion of an information systems function or process to a vendor on a long-term basis.

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 - This entails contracting to a vendor for the operations and management of the computer-related telecommunications network, transmitting data, voice, image, text, local-area and wide-area networks. Voice-only network operations are not part of information systems outsourcing.

Desktop Services - These services entail 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

C
Report Contents

Chapter II is the Executive Overview and contains a summary of the main trends in outsourcing in the government sector.

Chapter III focuses on outsourcing in local government across Europe. The chapter provides forecasts for the outsourcing market and analyses in outsourcing trends and considers the emergence of business operations outsourcing.

Chapter IV focuses on outsourcing in central government in Europe. In particular, this chapter considers the emergence of the market testing initiative in the U.K. and the opportunities for vendors created by this programme.

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*

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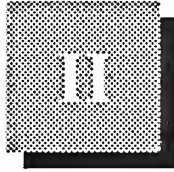
Executive Overview

A

Government Outsourcing Forecast to Grow at 29% Per Annum

Traditionally, both central and local government bodies in Europe have been reluctant to outsource their IS activities. However this is now starting to change, as governments seek increased flexibility and more efficient services.

The changes are most evident in the United Kingdom. Here the combination of high levels of government borrowing and the ideological predisposition towards free market principles is leading the government to enforce the application of concepts such as market testing in central government and compulsory competitive tendering for local government organisations.

The emergence of outsourcing in the Government sector is having a major impact on the outsourcing market as:

· Business operations contracts emerge from the local government sector

· Major contracts begin to emerge from central government bodies

· Other countries begin to follow the pattern being established in the United Kingdom.

B

Business Operations Outsourcing Emerges in Local Government

The potential growth for IS outsourcing within the local government sector in Europe is considerable. For example in the United Kingdom, the government is about to enforce competitive tendering for 80% of IS activity. In comparison, approximately 7% of local authorities currently outsource elements of their IS functions. Indeed much of the outsourcing so far undertaken has been a defensive move to protect the jobs of those in-house personnel associated with declining mainframe-based IS services.

However, a much wider opportunity is now beginning to emerge, namely business operations outsourcing. The U.K. government has a vision of local government as "enabling authorities". Such authorities remain responsible for the delivery of services to the general public, but do not deliver these services themselves.

This thinking has led the government to begin to set wider targets for competitive tendering than basic support services. For example, the government is setting a target that 25% of each authority's financial services be subjected to competitive tendering.

As a result, a number of specialist vendors such as the Capita Group and CSL have begun to offer business operations services, called managed services, to local government. So far these have concentrated on exchequer functions such as revenue collection. However, other areas of managed services such as housing management are now beginning to be outsourced.

At present, the business operations market in local government in the United Kingdom is worth approximately $30 million. This market has considerable growth potential.

The trend towards the combined emergence of IS outsourcing and business operations outsourcing in local government has resulted in the development of specialist vendors to serve these markets. The two leading vendors in IS outsourcing in the U.K. local government sector are CFM and the Capita Group. Both these organisations have access to managed services offerings. Capita Group has individual subsidiaries offering managed services and IS outsourcing. CFM offers IS outsourcing and one of its major shareholders, CSL, offers managed services.

This combined capability is assisting these vendors in differentiating their offerings, and hence maintaining their lead, in the local government sector.

Other vendors will need to follow this example in order to strengthen their presence in the local government sector.

Outsourcing in central government departments is lagging behind that in local government. As outsourcing becomes more mature in the national government sector, so business operations opportunities will also emerge.

The Customs & Excise is already considering outsourcing its revenue collection functions in the U.K. while EDS provides business operations services on behalf of the Department of Social Security.

C

Major Contracts Favour Emergent Outsourcing Vendors

Market testing in central government can lead to massive outsourcing contracts. For example, the IS functions of the U.K. Inland Revenue could eventually generate contracts worth $350 million per annum. The Inland Revenue is believed to favour using a single prime contractor even though its IS outsourcing will be phased. The first phase is likely to be the outsourcing of the operation of its mainframe-based services and to be worth approximately $100 million per annum.

Contracts of this size pose problems for the established outsourcing vendors in Europe. For example, the European outsourcing revenues of third-placed Sema Group in 1991 amounted to only $100 million. A contract of $350 million would exceed the outsourcing revenues achieved by any vendor in Europe in 1991 or 1992.

Accordingly, the outsourcing experience of vendors such as Hoskyns and Sema Group is no longer enough to make them the principal contenders for such contracts. Large government departments such as the Inland Revenue are seeking vendors who can safely manage the risk involved in contracts of this size.

This is leading to the formation of consortia as vendors assemble all the necessary skills and experience. This situation presents a major opportunity for the leading systems vendors to establish their leadership of the European outsourcing market. IBM, Digital and ICL have entered discussions with the Inland Revenue. Because of their size and ability to absorb risk, it is probable that either one of these systems vendors or one of the US-based outsourcing specialists—CSC and EDS—will take prime contractorship for delivery of the first phase of the Inland Revenue's services.

Accordingly the emergence of such contracts presents an opportunity for new market entrants to establish themselves rapidly. It also presents a threat to may of the current market leaders who may be perceived as lacking the critical mass to handle such contracts.

The nation government sector also presents vendors with an opportunity to establish themselves in business operations. EDS already manages business operations services on behalf of the Department of Social Security in the U.K. The requirement for business operations services will develop further in the central government sector as market testing develops over the next few years.

D

Outsourcing of Government IS Will Grow in France and Italy

Exhibit II-1 provides forecasts of IS outsourcing within the government sector for the period 1993 to 1998.

EXHIBIT II-1

Government Outsourcing by Country, 1993-1998

Country	1993 $M	1998 $M	CAGR (Percent)
United Kingdom	380	1,200	26
France	82	300	30
Italy	120	350	24
Rest of Europe	180	870	37
Europe	760	2,700	29

The drive towards outsourcing will be particularly strong in the United Kingdom over the next five years. The government will pass legislation in 1993 requiring local authorities to submit a minimum of 80% of their IS activities to competitive tendering. Competitive tendering requires an in-house IS department to demonstrate at regular intervals that its services provide at least comparable value for money to that which can be offered by any external vendor.

This immediately places tremendous pressure on any in-house mainframe platform operations services, for example. In-house suppliers within local government are not permitted to compete for external business. Hence they have little chance of achieving the economies of scale necessary to demonstrate their ability to compete on value for money. This situation is exacerbated by the decentralisation of local government and the associated move away from central, mainframe-based IS to local, open systems-based IS. This further erodes the efficiency level which can be achieved by an in-house service provider offering mainframe-based services.

Following its initiative in local government, the U.K. government is requesting that central government departments set targets for market testing. IS functions remain a comparatively minor component of the overall market testing programme at present. However, IS activities are a

prime target for market testing. Accordingly, the IS functions of central government departments will increasingly be outsourced over the next five years, following the example currently being set by the Inland Revenue.

Driven by growth in IS outsourcing in both local government and central government, the United Kingdom will remain the major country market for government sector outsourcing over the next five years.

The markets for IS outsourcing in local and national government in the United Kingdom are forecast in Exhibit II-2.

EXHIBIT II-2

Government Outsourcing—United Kingdom, 1993-1998

Sector	1993 £M	1998 £M	CAGR (Percent)
Local Government	100	400	32
National Government	140	350	20
Total Government	240	750	26

Despite the size of the contracts likely to emerge in the national government sector—in excess of $100 million per annum in the case of the Inland Revenue, the IS outsourcing market in local government will remain the larger of the two over the next five years because of the large number of contracts originating here.

After the United Kingdom, the second largest government outsourcing market in Europe is Italy. Forecasts for the IS outsourcing in local and national government in Italy are shown in Exhibit II-3.

EXHIBIT II-3

Government Outsourcing—Italy, 1993-1998

Sector	1993 L B	1998 L B	CAGR (Percent)
Local Government	85	230	22
National Government	80	250	26
Total Government	240	750	26

In Italy, there are also trends towards IS outsourcing in both local and national government. Finsiel dominates the government sector of the software and services market in Italy. The company has outsourcing contracts with both local government and national government departments. Finsiel and a number of local government bodies have formed a joint venture company, Informatica Trentina, which offers outsourcing services to local government.

Finsiel also has a number of outsourcing contracts with the Ministry of Finance and the Ministry of Education. Following the recent formation of a government committee established to consider all aspects of the use of IS in government, it is expected that the use of outsourcing in central government will rise over the next few years.

The development of outsourcing in central government in France is expected to be slow. Forecasts for government sector IS outsourcing in France are shown in Exhibit II-4.

EXHIBIT II-4

Government Outsourcing—France, 1993-1998

Sector	1993 FFM	1998 FFm	CAGR (Percent)
Local Government	430	1,100	21
National Government	-	500	-
Total Government	430	1,600	30

However the recent change in government in France many provide an impetus to IS outsourcing in national government towards the end of the forecast period.

Again the move towards IS outsourcing is expected to be greatest in the local government sector.

Overall there will be steady progress towards IS outsourcing in local government throughout most of Europe. Progress in the national government sector will be less pronounced with the United Kingdom and Italy setting the trend. The overall market forecasts for IS outsourcing in local and national government across Europe are shown in Exhibit II-5.

EXHIBIT II-5

Government IS Outsourcing by Sector—Europe, 1993-1998

CAGR
(Percent)

Local Government
- 435 (1993)
- 1,500 (1998) — 28

1993
1998

National Government
- 330 (1993)
- 1,100 (1998) — 27

Market Size ($ Millions)
0   400   800   1200   1600
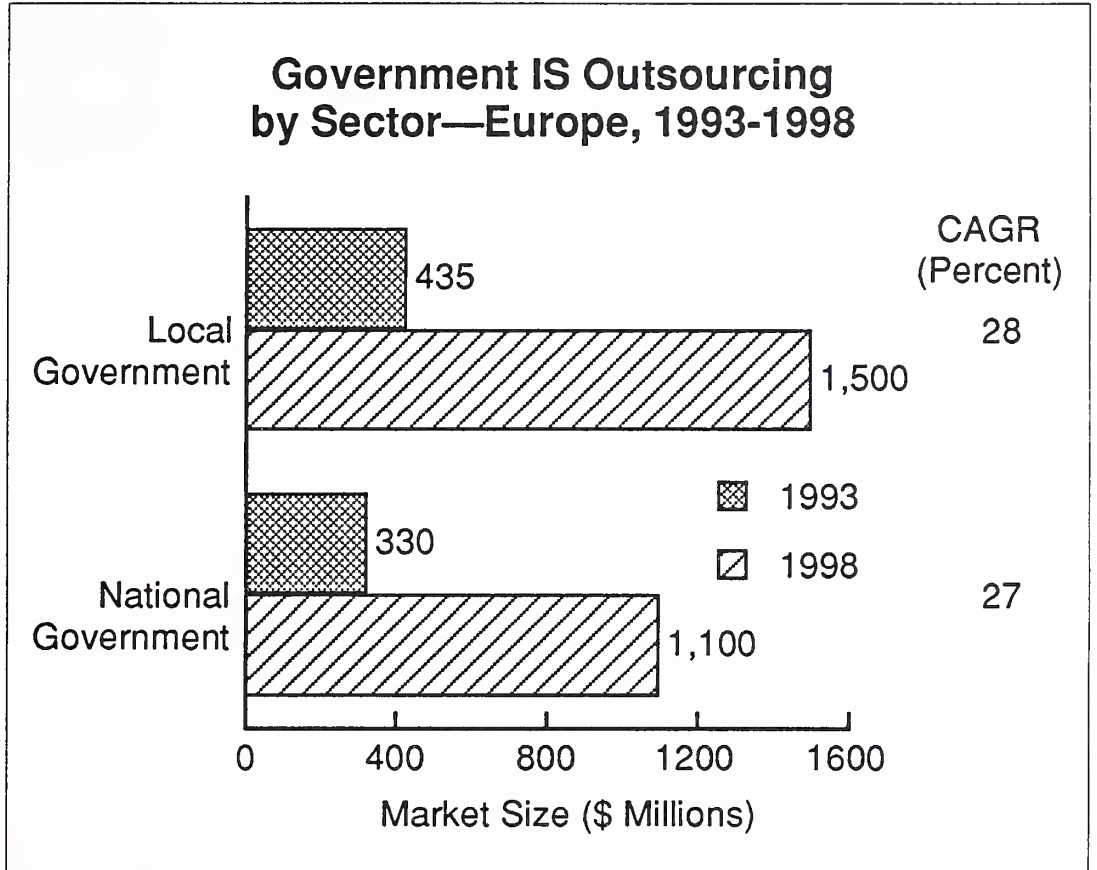
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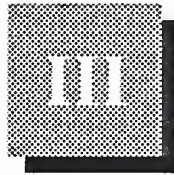
Local Government Outsourcing Sets Trends for Central Government

A

Local Government IS Outsourcing Forecast to Grow at 28% Per Annum

Exhibit III-1 provides forecasts for the growth in the adoption of IS outsourcing by local government bodies across Europe.

EXHIBIT III-1

Local Government Outsourcing by Country, 1993-1998

Country	1992 $M	1993 $M	1998 $M	'93-'98 CAGR (Percent)
United Kingdom	80	160	630	32
France	65	82	200	20
Italy	50	62	170	22
Rest of Europe	105	130	500	31
Europe	300	435	1,500	28

Outsourcing by local government is well recognised in France, the United Kingdom, and Italy. In these countries, local government outsourcing is more advanced than that in central government in both market penetration and nature of service. Indeed local government in the United Kingdom is the most advanced sector in Europe in the use of business operations outsourcing.

Outsourcing of IS functions by local government bodies is forecast to progress steadily in France and Italy over the forecast period. In the United Kingdom, there will be an appreciably higher level of growth in this market, driven by the government's impending legislation regarding Compulsory Competitive Tendering.

In addition to the outsourcing of IS functions, Compulsory Competitive Tendering will lead to a substantial increase in business operations. In 1992, the market for business operations and services to U.K. local government was valued at approximately £20 million.

In France, opportunities are beginning to emerge in regional administration.

In Italy, approximately 20% of Finsiel's revenues accrue from the local government sector. The company has specialist subsidiaries which focus on the local government market. These are:

· Insiel
· Informatica Trentina
· Datasiel
· Sispi
· Venis.

Informatica Trentina is a joint venture between Finsiel and local government, which offers a range of outsourcing and processing services to the local government sector.

B

Compulsory Competitive Tendering—A Major Force in Local Government Outsourcing

1. The Vision of the Enabling Authority

The trend to outsourcing of IS services in central government in the U.K. is still in its early stages. At this early stage, the government is being tentative in its approach and has so far avoided insisting on target levels for outsourcing of IS services.

However, the use of outsourcing is much more advanced in local government. Here the government has a clear vision. This vision is to transform local authorities into enabling authorities. This involves a complete separation of the functions of service delivery from the organisation's strategic responsibilities. In the long-term, if this philosophy remains politically acceptable and the present government remains in office, then many local authorities will become devoid of all service delivery functions.

Of course, many local authorities will remain politically opposed to such an approach. Such authorities will be co-erced into adopting the approved policy via the legal system.

At present, the government is passing legislation in the area of compulsory competitive tendering which will require local authorities:

· To submit 80% of their IS activities to competitive tendering
· To submit 25% of their financial services to competitive tendering.

2. Business Operations and IS Outsourcing Opportunities

This is leading the major suppliers of IS outsourcing to develop access to business operations capabilities.

Some examples of recent business operations contracts are listed in Exhibit III-2.

EXHIBIT III-2

Business Operations Contracts in Local Government

Client	Contract Value (£M)	Scope of Service
Oxfordshire County Council	6	Payroll processing Pensions administration Revenue collection
Bromley District Council	24	Exchequer services
Rutland District Council	10	Housing operations

Oxfordshire County Council has signed a contract with CSL to outsource one-third of the operations of its finance function by value and to transfer fifty of the council's personnel to CSL. The council anticipates achieving savings in excess of 10% of expenditure within those functions outsourced.

The majority of business outsourcing within the local authority sector currently involves transfer of exchequer services such as revenue collection. Revenue collection became a major problem for many local authorities with the introduction of the community charge. Faced with a high level of non-payment, it became attractive for local authorities to enter into payment-by-results contracts with third parties.

Other business functions besides financial services are also beginning to be outsourced. For example, CSL has signed a contract with Rutland District Council to manage its entire housing and property management function including the provision of services such as rent collection, provision of housing advice, and maintenance of the housing stock.

Business operations are frequently called managed services in the local government sector.

The two principal suppliers of managed services in the United Kingdom are CSL and the Capita Group. Both also have access to IS outsourcing capability. The Capita Group has its own computer services subsidiary, Telecom Capita. CSL owns 25% of CFM, its joint venture with ICL.

Both CSL and the Capita Group wish to provide one-stop shopping for local authorities covering both their business operations and IS outsourcing needs. However local authorities often wish to maintain a high level of competition between their potential suppliers, and avoid any possibility of supplier lock-in.

Accordingly, in the case of Oxfordshire County Council:

· CSL manage the revenue function

· Telecom Capita manage the IS services.

3. Exchequer Services—Principal Form of Business Operations

CSL was formed by a management buy-out of CIPFA Services in 1980. CIPFA stood for the Chartered Institute of Public Finance and Accountancy. Initially the company concentrated on consultancy for the health sector and on raising funds for public sector organisations such as housing associations.

CSL introduced its managed services in 1987, and estimates that it has undertaken approximately 120 managed services contracts.

CSL's managed services revenues are currently £8 million. CSL Managed Services employs 350 personnel, deployed as shown in Exhibit III-3.

CSL Managed Services

Business Function	Number of Personnel Employed
Financial management	81
Revenue collection	72
Benefits	61
Payroll & pensions	47
Housing management	89
Total	350

The primary focus of CSL Managed Services is financial services though the company is also extensively involved in housing management. The company has a long history of working with housing associations.

All of CSL's £8 million in revenues from managed services accrue from the public sector. However, only one-third of these revenues are received from local authorities. The remainder are derived from contracts such as:

· Licence fee collection for the BBC

· The management of services on behalf of the Disablement Services Authority

· Provision of financial services for the Warrington and Runcorn Development Corporation.

4. Strong Demand to Outsource Central Systems

There are approximately 540 local authorities in the United Kingdom, including all county councils, district councils, London boroughs and other unitary authorities.

At the end of 1992, approximately 40 of these organisations had adopted IS outsourcing, ahead of the legislation which will force them to undergo competitive tendering for their IS functions.

In addition, the local government Society of IS Managers estimated that a further 50 councils had adopted a client/contractor split within their IS functions in preparation for compulsory competitive tendering.

The current value of IS outsourcing within local authorities is estimated to be £50 million. With local authorities required to put out 80% of their IS activities by value to competitive tendering, the market potential of IS outsourcing in local government could rise to £500 million.

Examples of current IS outsourcing contracts in the local government sector are provided in Exhibit III-4.

EXHIBIT III-4

IS Outsourcing Contracts Local Government

Client	Contract Value (£M)	Scope of Service
Birmingham City Council	40	All IS services
Kent County Council	15	Mainframe platform operations and corporate data network
Berkshire County Council	12	Mainframe platform operations and corporate data network

To a certain extent, outsourcing of IS activities in the local government sector in the United Kingdom is following an analogous path to that already undertaken within the National Health Service.

The National Health Service is organised on a two-tier structure with regional and district health authorities mirroring the organisation of county and district councils in the local government sector. In both instances the government is endeavouring to devolve authority from the regional organisations to the local bodies. Similarly computing services have historically been provided from centralised, regional resources using mainframe-based systems.

In the late 1980s, the move to decentralisation of authority, and also IS systems, within the health service led to decreasing dependence on the centralised systems of Regional Health Authorities. As a result, the data centres of each of these Regional Health Authorities were outsourced, typically as medium-term transition outsourcing contracts.

The same phenomenon is now appearing in the local government sector.

For example, Kent County Council has divided its IS department into a number of business units. One of these business units was the central IS unit responsible for running the ICL mainframes and corporate data network. This business unit had a budget of £3.7 million per annum and employed fifty personnel.

However, demand for the department's services was steadily declining as a result of decentralisation of authority within the council and the trend for end users to purchase their own systems. This situation led to concerns over service pricing as utilisation levels fell and concerns for the future of the personnel employed in this business unit.

An outsourcing contract with Telecom Capita addressed these issues. Firstly, it offered Kent County Council savings of £4 million over a five-year period. Secondly, Capita has created a regional services centre on the basis of its agreement with Kent County Council, offering the IS personnel the possibility of expanding their contract base.

The desire to protect the jobs of their own IS personnel has led a number of councils to become early adopters of outsourcing. Since local government expertise will be in short supply amongst vendors at this stage, IS staff transferred to vendors at this point will have a secure future. Accordingly, it is the IS personnel from councils that only accept outsourcing at a late stage in the development of the market who will be made redundant.

However, there are limits to the number of regional centres which can be established, and some councils are beginning to perceive that it may already be too late to protect jobs in this manner.

Nonetheless there is a strong move to outsource centralised systems, for example:

· Payroll
· Accounting
· Community charge/council tax
· Housing benefits/rent collection.

In the medium-term, it is probable that both the IS and the business operations aspects of these services will be outsourced.

Accordingly, it is important for vendors to offer business operations/ managed services in addition to IS outsourcing.

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IV
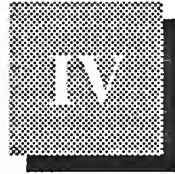
Central Government Outsourcing Set to Become a Reality

A

Outsourcing Will Become Established in United Kingdom and Italy

Exhibit IV-1 provides forecasts of the value of IS outsourcing within central government over the next five years.

EXHIBIT IV-1

Central Government Outsourcing by Country, 1993-1998

Country	1992 $M	1993 $M	1998 $M	CAGR (Percent)
United Kingdom	60	220	550	20
Italy	50	60	180	25
Rest of Europe	40	50	370	49
Europe	150	330	1,100	27

The size of the European central government outsourcing market is forecast to double in 1993. This rapid growth will result from the adoption of the government's market testing programme in the United Kingdom. Indeed much of the growth in the market in 1993 and 1994 will arise from a single contract, namely the first phase of outsourcing within the Inland Revenue's IS activities.

However, there are signs that the lead being taken in the United Kingdom in outsourcing central government IS functions will gradually spread throughout Europe. For example:

- The European Commission has indicated that it will consider outsourcing its mainframe data centres and its corporate network.

- The Italian government is establishing an "Authority for IS in Public Administration" to review the use of IS within central government.

- The new government in France is likely to be ideologically in sympathy with the concept of outsourcing the administration's IS functions.

As a result, INPUT expects that outsourcing will become established in central government in the United Kingdom, Italy and the European Commission over the forecast period. The first central government outsourcing contracts may begin to appear in France towards the end of the forecast period.

B

U.K. Market Testing Leads to Major Contracts

1. Improved Standards Equals Greater Efficiency

The concept of market testing was introduced into the United Kingdom by the Citizen's Charter initiated in 1991.

The stated objectives of the Citizen's Charter are to raise the standards of public services and to make them more responsive to their users. However, the government perceives that resources to fund public services are limited. Accordingly, improving standards depends more and more upon delivering services efficiently within their allocated resources.

To achieve this aim of increased efficiency, the government has introduced market testing. Market testing means testing a particular service to see which supplier—in-house or external—offers the best combination of value for money and quality of service for the user.

Following the publication of the white paper "Competing for Quality" in 1991, government departments and agencies were required to set targets for market testing areas of their operations.

The values of the activities to be market tested prior to September 30th, 1993 are shown in Exhibit IV-2.

EXHIBIT IV-2

Value of Market Testing By Department, 1993

Department	Value £M
Ministry of Defence (MOD)	323
Inland Revenue	282
Department of Social Security (DSS)	127
Home Office	120
Department of Trade and Industry	80
Department of Environment	72
Department of Employment	58
Customs and Excise	53
Ministry of Agriculture, Food & Fisheries	42
Northern Ireland	40
Others	241
TOTAL	**1,438**

The activities included within the scope of Exhibit IV-2 are widespread, ranging from:

· Building and estate management to milk hygiene enforcement for the Ministry of Agriculture, Fisheries and Food

· Vehicle maintenance to elementary flying training for the Ministry of Defence.

Market testing has now moved beyond traditional support services such as catering and cleaning to the management of IS functions and business operations.

2. Market Potential Exceeds £1 Billion

Some examples of market testing which can be viewed as potential business operations contracts are listed in Exhibit IV-3.

EXHIBIT IV-3

Market Testing of Business Operations, 1993

Department	Functions
Customs & Excise	Debt collection Import & betting duty collection
Department of Education	Payroll Services Services promised to Teachers Pension Agency
Department of Employment	Payroll services Pensions administration Publications distribution
Department of Social Security	Accounting Services

Department of Trade and Industry	Accounting (Insolvency
	  Service)
	Companies House
	Pay
	Oil and gas royalties
	Trade marks examination
	  research

HM Treasury	Economic model building and development

Government departments are beginning to market test basic financial business operations such as:

· Payroll & pensions administration
· Revenue collection
· Accounting services.

Accordingly central government may over the next few years follow the trend already being set in local government towards outsourcing of exchequer services.

The value of market testing by activity for the year ending September 30, 1993 is shown in Exhibit IV-4.

EXHIBIT IV-4

Value of Market Testing by Activity, 1993

Activity	Value (£M)
Department Specific	1,034
Estate Management	104
Office Services	85
Information Systems & Services	79
Reprographics	54
Personnel	29
Payroll	9
Pensions	7
Other	37
TOTAL	1,438

IS systems and services account for only 5% of the activities planned for market testing in 1993. However, this ignores the IS content of business operations services such as accounting services.

It is important not to confuse the terms market testing and outsourcing. Market testing involves comparing the value for money provided by an in-house supplier with that which could be provided by external suppliers. It is intended that a level playing field should be provided for all potential suppliers. There is no automatic assumption that the service will be contracted out. Indeed both external vendors and in-house suppliers perceive that the rules favour the other party.

Secondly, the manner in which any contracting out occurs will vary widely. In some instances, the contract will involve outsourcing—that is, the management of a function over a number of years. In other instances, the contract will be for a specific project activity, and so not considered to be an outsourcing arrangement by INPUT.

Details of the IS services which were contracted out by the U.K. government prior to September 1992 are listed in Exhibit IV-5.

EXHIBIT IV-5

IS Services Contracted Out, 1991-1992

Department	Services
Ministry of Agriculture, Fisheries & Food	Consultants support (£4.5m p.a.) Some outsourcing to run existing systems
HM Customs & Excise	Customs freight computer system (DEPS) run by BT BT developing replacement (CHIEF) BT contract values £14m Other development services worth £4m
Department of Health	Bought in IS and management consultancy services worth £15m
Northern Ireland	Central Computing Services Division (£6.2m)
Scottish Office	IS Services (£2m)
Department of Social Security	Contracting out three Area computing centres including printing and output handling of benefit payments to 13 million customers.

The IS services contracted out during this period consist of a mixture of project activity and outsourcing.

Examples of project activity include:

· Consultant support for the Ministry of Agriculture, Fisheries & Food
· System development assistance for HM Customs and Excise.

However, there is a significant trend towards outsourcing contracts, and this trend will continue as market testing becomes established over the next few years. Examples of outsourcing contracts include:

- CFM's contract with the Northern Ireland office in which the company acquired responsibility for the provision of ICL mainframe-based systems previously managed by the Department of Finance and Personnel

- BT's contract to run the customs freight computer system (DEPS) for HM Customs & Excise

- EDS' business operations contract covering benefit payments on behalf of the Department of Social Security.

The scope for contracting out IS services is now increasing rapidly. The U.K. government spends £2 billion per annum on information services and employs approximately 20,000 IS personnel. The Treasury has set a minimum of 12% on the staff activities to be submitted for market testing by central government departments before 30 September 1993. In the longer term, the Treasury states that its preferred level of market testing is 25% of staff activities. However, this stance may change over the next few years as market testing in the central government follows the pattern of Compulsory Competitive Tendering in local government. In 1993, local authorities will be required to seek outside bids for 80% of their computing activities. In addition, local authorities will be required to seek outside bids for 25% of their financial services, leading to considerable business operations outsourcing revenues.

In central government, market testing of IS services will lag behind market testing of simpler functions because of the complexity of market testing IS services. The CCTA estimates that the market testing process for a central government department's IS activities will require a period of 14 months. Accordingly, few outsourcing contracts will appear during 1994, but the market will rapidly gain momentum during 1994 and 1995.

The IS activities which have been proposed for market testing by central government departments in 1993 are listed in Exhibit IV-6.

EXHIBIT IV-6

IS Activities Proposed for Market Testing, 1993

Department	Activity
Ministry of Agriculture, Fisheries & Food	IS facilities management IS systems, services and development
Central Statistical Office	RPI Computing
HM Customs & Excise	Information Technology division (part)
Department for Education	IS Services (some) Payroll services provided by Chessington Computer Centre
Department of Employment - Headquarters - Employment Services	IS help-desk Non-mainframe support Payroll services IS mainframe services (for accounting system) IS applications maintenance IS applications development
Department of Environment - Planning Inspectorate Agency	IS Project Management
Foreign Office	IS Project Management IS Training
Forestry Commission	Software development
Home Office - Headquarters - Prism Service	Computing/Police national computer Computing Services
Ordnance Survey	Computer Operations and Data control
Paymaster General's Office	Mainframe Operations
Department of Trade & Industry	Information Technology Services
Department of Transport	Driver and Vehicle Operation Information Technology (DVOIT) Agency

EXHIBIT IV-6 (CONT.)

IS Activities Proposed for Market Testing, 1993

Department	Activity
Welsh Office	IS Services
Inland Revenue	Facilities Management of IT Services
Intervention Board	Computer Services Operations
Department of National Heritage	IS Facilities Management
Northern Ireland	Computerisation
Office of Public Service & Science - Occupational Health Service - Chessington Computer Centre	Financial Systems Facilities Management
Customs and Excise	IS division (part)
Ministry of Defence	IS services
Lord Chancellor's Department	IS services

3. Inland Revenue Favours Major Vendors

In the short-term the major opportunities for outsourcing vendors lie within the Inland Revenue and the Department of Transport.

The Inland Revenue was authorised to begin market testing its IS services by the Treasury in Autumn 1992. The Inland Revenue has an annual IS budget of £250 million and employs 2,700 IS personnel. These personnel are deployed across three development centres and thirteen data centres.

If the tendering process now underway reveals that the Inland Revenue would benefit from contracting out elements of its IS services, then the government is aiming to agree on contracted details with the selected supplier by the end of 1993.

It is unlikely that complete outsourcing of all the department's IS functions will be adopted initially. A phased introduction of outsourcing

will probably be adopted with the first phase estimated to be worth £50 million in 1994.

The Inland Revenue is a particularly sensitive department to select for the first major market testing exercise. Accordingly, the government will take an extremely cautious approach. Two safeguards currently being insisted upon are that:

· All tax records remain in the U.K.

· Any outsourced data centres will be regularly inspected to ensure that strict confidentiality and security applies to all data.

In addition, the list of suppliers shortlisted is a conservative one. The vendors favoured initially were:

· IBM
· Digital
· ICL
· EDS
· CSC.

So even the outsourcing market leader in the U.K., Hoskyns, was initially considered too minor a player to bid for the contract in its own right.

The Inland Revenue is believed to favour a contract with a single organisation or consortium. Vendors are having to establish consortia to acquire the range of skills and the capacity to handle contracts of such size and scope. For example, Digital has formed a consortium consisting of itself, Barclays Computer Operations (BCO) and Logica to bid for the Inland Revenue contract.

However, the rumours within the industry currently suggest that EDS is the most probable winner of the contract.

The U.K. government also intends to privatise the Next Steps Agencies. The first of these agencies to be privatised will be the Driver Vehicle Operators Information Technology (DVOIT) agency. DVOIT provides computer services to the Department of Transport, principally to the Driver and Vehicle Licensing Agency which registers and licenses drivers and vehicles and collects vehicle excise duty. The agency is expected to be privatised towards the end of 1993, and a number of companies have already been approached to ascertain their level of interest in purchasing the agency.

Personnel issues will feature strongly in the negotiations. DVOIT estimates that it currently has a staff surplus of between 100 and 150 personnel. The agency employs approximately 500 personnel.

4. In-House Bids are Encouraged

Central government departments in the U.K. are now required to assess the scope for extending market testing to new areas of their operations and to set targets for market testing.

An Efficiency Unit—part of the Office of Public Service and Science— has been established to monitor and reach agreement on these targets. Undoubtedly, government departments will be strongly encouraged to market test a wide range of their activities. The targets agreed for market testing in 1992 cover activities valued at £1.5 billion.

In market testing IS services, it is intended that civil service business managers will become the direct customers of these services with responsibility for ensuring that they receive value for money from their suppliers.

However, these business managers will not be the principal decision makers in deciding the outcome of a market testing exercise. This role will be taken by the department's market testing unit. Each market testing unit will have responsibility not just for market testing IS services, but for market testing all activities nominated to undergo this process.

The market testing process recommended by the CCTA is shown in Exhibit IV-7.

The first stage is to establish a project team to carry out the market test and to identify the manner in which any subsequent contract is to be managed and controlled. While external vendors will be subject to legally binding contracts should their bids be successful, such contracts are not possible between two government departments. However, successful in-house bidding teams will become subject to a Memorandum of Understanding, the purpose of which is to formalise the relationship between the client and the in-house provider.

If an in-house bid is to occur, then the government department must separate the project team which is to evaluate the market testing exercise from the in-house bid team. A number of in-house bidding strategies are possible, namely:

· No bid
· Sub-contract uncompetitive elements of in-house operations
· Bring in additional skills and experience from the private sector
· Use only civil service staff.

EXHIBIT IV-7

The Market Testing Process

Source: CCTA
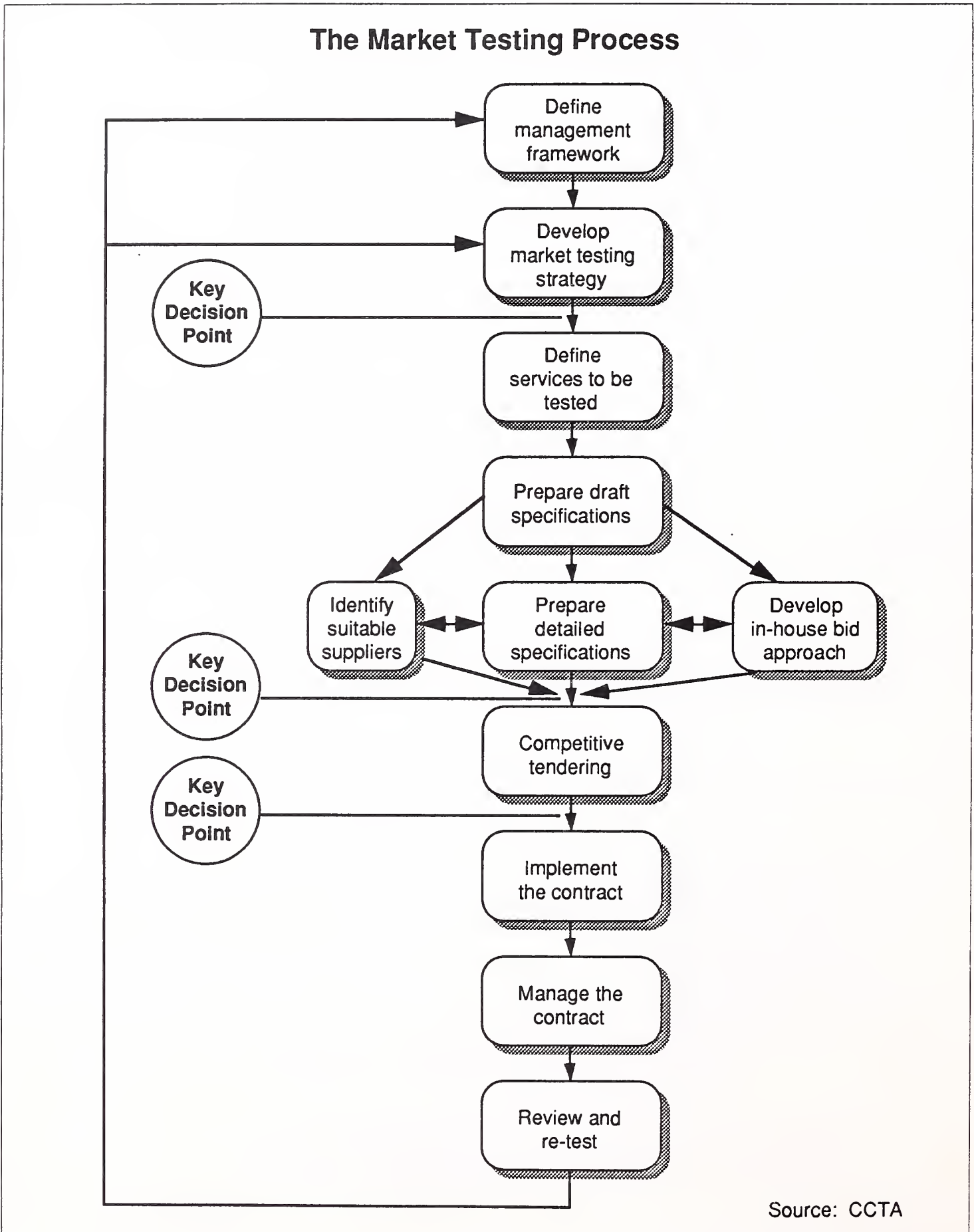
However, partnerships between the in-house team and an external supplier are not allowed. The in-house team must remain the prime contractor for all bids which they submit.

Each department's market testing unit will be responsible for advising whether or not an in-house bid is viable. An in-house bid will not be allowed if senior management perceive it to be a waste of taxpayers' money. However the government wishes to encourage in-house bids wherever possible to help preserve staff morale. The existence of an in-house bid also enables the department to ensure that any external vendor appointed does indeed provide greater value for money.

Government departments in the process of developing their market testing strategies can issue Requests for Information to selected vendors at this stage to assist them in ascertaining the feasibility of outsourcing particular services.

Hence it is important for vendors to adopt a pro-active stance in ascertaining departments' intentions. While it is government policy that such requests for information will not bias the formal competitive tendering process, vendors who wait for requirements to be published in the EC Journal may find themselves at a competitive disadvantage.

Vendors will need to approach government departments directly to ascertain their market testing plans. The CCTA has stated that it will not divulge details of individual departments' plans to vendors.

5. Vendors Have Choice of Roles

Within each market testing exercise, it will be possible for a vendor to take one of the following roles:

· Adviser to the client
· Supporter of the in-house bid team
· Bidder.

Vendors cannot take on more than one of these roles in any given market testing exercise. This means that it is not possible for a vendor to assist the client in developing the specification of requirements and then submit its own bid to supply the service.

However, there are significant opportunities for vendors in each of the three areas identified above. For example, both the client and the in-house bid team will require extensive financial, legal, personnel and technical skills.

Some in-house teams will require extensive support in developing the necessary commercial skills to compete. Key areas where guidance or supplementary skills may be required include:

· Financial aspects such as costing and pricing service requirements

· Marketing and selling their services in a competitive environment.

Similarly, clients may require extensive assistance in preparing specifications of the services required, in evaluating bids, and in developing contract terms and conditions.

The typical structure of an in-house bid team is shown in Exhibit IV-8.

EXHIBIT IV-8

Structure of In-House Bid Team

```
            ┌──────────────┐
            │   Project    │
            │    Board     │
            └──────┬───────┘
                   │
     ┌─────────────┴──┐        ┌──────────────┐
     │     Bid        │────────│ Consultants  │
     │   Manager      │        │              │
     └──────┬─────────┘        └──────────────┘
            │
     ┌──────┴───────┐
     │    Stage     │
     │   Managers   │
     └──────────────┘
```
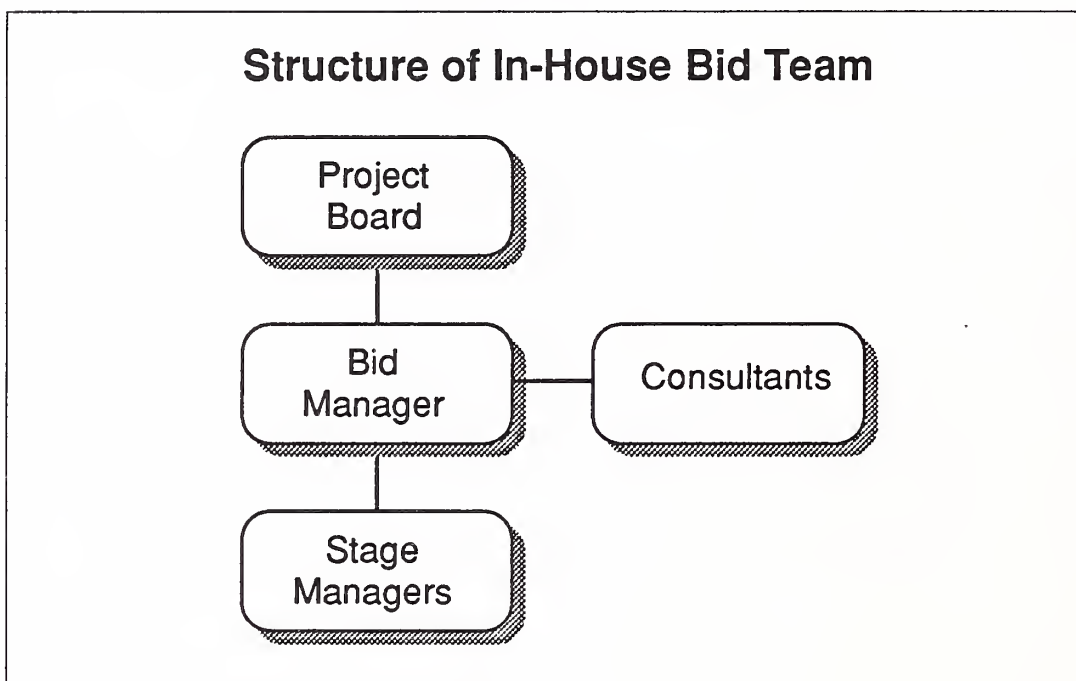
The CCTA wants to ensure that a level playing field exists between internal and external suppliers. In line with this reasoning:

· The in-house team will be given the final Statement of Service Requirements (SSR) at the same time as external vendors

· Redundancy costs where applicable will have to be incorporated into in-house bids

· VAT chargeable on bids from external vendors will be discounted at the evaluation stage

· Consultancy costs incurred to assist in-house teams in bidding will be treated as sunk costs and not costed into the in-house bids.

The CCTA also wishes to prevent supplier lock-in so that a competitive market can be maintained. Standards such as GOSIP, SSADM, and PRINCE are expected to play a vital role in this respect. It is important that the cost of change is minimised so that functions can be retested in the future.

The pattern of IS market testing will vary considerably from one government department to another. For example:

· Department of Employment

   - "Market tested" its mainframe operations several years ago and does not plan to retest these in the short-term

   - Is actively seeking value for money from

   - LAN support

   - Application development

· Home Office

   - Is initially market testing the operation of its data centres

   - Is not including systems development in the initial tranche of market testing.

In addition to outsourcing, considerable levels of project activity will arise out of market testing. The Home Office perceives that its end users are reluctant to commit to a single vendor in advance for systems development. Systems development activity will be contracted out on a project-by-project basis as the need arises.

The CCTA itself appears to favour the unbundling of IS services. Unbundling increases competition and helps to prevent the market from being dominated by the largest vendors. It also enables the most suitable vendor to be selected for each type of service, and reduces complexity and risk by enabling a phased approach to contracting out or outsourcing.

One area of uncertainty for vendors remains the Transfer of Undertakings (Protection of Employment) (TUPE) regulations. When the TUPE regulations apply, the contractor must take over employees on their existing terms and conditions. However bids could vary markedly between differing vendors, one believing that TUPE did apply, the other believing that it did not. In order to limit the resulting confusion, each market testing exercise will be referred to the Treasury solicitor for a ruling on whether or not TUPE applies. This legal advice will then be issued along with the appropriate Statement of Service Requirements.

The issue of pensions is currently being considered by Treasury solicitors.

Vendors are advised to consult their own legal advisers in each instance for an independent ruling on whether or not TUPE will apply. There are no plans to indemnify contractors who win contracts believing that the regulations do not apply and subsequently find that they do.

C

Finsiel Active in Central Government Outsourcing in Italy

The central government in Italy currently outsources only a small proportion of its IS activities. However, unlike France and Germany, some major activities are outsourced and the level of outsourcing is expected to increase over the next five years.

One of the major software and services vendors to the Italian government is Finsiel. Finsiel has two subsidiaries focused on central government— Sogei and Agrisiel. The organisations' activities are complemented by those of another subsidiary—Italsiel. Overall, approximately 50% of Finsiel's revenues derive from the central government sector.

Most of these revenues arise out of major development projects such as:

· Sogei's development of a Tax Information System for the Ministry of Finance

· The integration of the Italian customs system with those of the other member States of the European Community

· Automation of the National Library Services.

However, Finsiel also has a number of outsourcing contracts with the Italian government. These include:

· Italsiel's application operations contracts for IS systems on behalf of the National Accounting Office and the National Court of Auditors

· Management of the Schools Information System on behalf of the Ministry of Education.

These contracts illustrate the willingness of Italian government departments to enter into IS outsourcing contracts. A separate government department has now been established to consider all aspects of the use of IS within government. It is expected that the formation of this organisation will lead to an increased adoption of outsourcing in central government.

In addition to systems operations contracts, there is potential for outsourced network management and business operations contracts in Italy. The computerisation of government departments is moving from the automation of internal administrative activities towards providing greater links with the general public. This type of activity creates opportunities for vendors to offer business operations services whereby the vendor becomes responsible for the delivery of the service to the general public.

Secondly, there is an increasing need to establish links between government departments. This creates opportunities for outsourced network management services.

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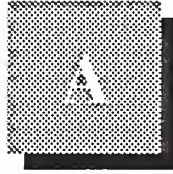
Vendor Profiles

A

Télésystèmes—Expansion of Geographic Coverage via Co-operation with Sema Group

At present, Télésystèmes has approximately 25 outsourcing clients and total outsourcing revenues of FF460 million—40% of which are derived from its parent company France Télécom. The majority of these revenues are derived from platform operations contracts, though these tend to have an appreciable network management content.

Some of the Télésystèmes current outsourcing clients are listed in Exhibit A-1.

EXHIBIT A-1

Télésystèmes Outsourcing Clients

- CNES (National Centre for Space Studies)

- France Télécom

- Heidelberg Harris France

- Thomson

- Paris Port Authority

- Constructions Industrielles de la Méditerranée

Télésystèmes has recently re-organised its operations emphasising the importance of outsourcing in the company's corporate strategy. To further develop its outsourcing business, Télésystèmes:

· Has been reducing the cost of its platform operations services by consolidating its data centres

· Has developed a comprehensive outsourcing service portfolio

· Is endeavouring to enter into co-operative relationships with Sema Group and DIAGRAM to expand its European coverage.

1. Consolidation of Data Centres

Télésystèmes reorganised to the structure shown in Exhibit A-2 in 1992.

EXHIBIT A-2

Télésystèmes Organisation

G. Leblon

CEO

MC. Lambert

- Finances
- Control
- Accounting
- Internal IT
- International

- Marketing   M. Lacroix

F. Négrerie

- Legal
- Human Resources
- Administration

C. Chalumeau

Corporate Relations

S. Lipiec

Quality

A. Harmand
HJ Röhl

A. Flamant

FACILITIES
MANAGEMENT
SERVICES

C. Welsch

ENGINEERING
SYSTEM
INTEGRATION

M. Mesle

SYMEDIA

P. Morlière

CITCOM

IOP

SETIB

SEDIT
FACICOM
E3X

Previously, the company's sales activity had been organised by sector while the production units were organised along functional lines. This has now changed with the creation of a division—Facilities Management Services (FMS) with full profit and loss responsibility for outsourcing, processing and network services. This division employs 500 personnel.

To reduce costs within this division, Télésystèmes is in the process of consolidating to a single data centre in Paris, though the company still finds that it needs to maintain local data centres throughout the French Regions to remain competitive in these areas.

Currently, Télésystèmes has data centres located in Paris, Lille, Nancy, Nantes, Toulouse, Lyon and Marseille.

Télésystèmes' main capabilities within these data centres are concentrated on Bull, IBM and Digital equipment.

2. Developing Comprehensive Outsourcing Portfolio

Historically, Télésystèmes' outsourcing revenues have been dominated by the company's platform operations activities. However the Facilities Management Service division now offers a complete portfolio of platform operations, applications operations, network management and desktop services. In addition to its outsourcing offerings, the FMS division contains an accounting and payroll service bureau and offers cheque processing and electronic fund transfer services.

Exhibit A-3 indicates the breakdown of Télésystèmes' total revenues by industry sector.

EXHIBIT A-3

Télésystèmes 1992 Market Analysis by Industry Sector (FF Millions)

Industry Sector	Revenue	Percent
Telecommunications	790	45
Banking and Finance	90	5
Government	120	7
Industry	400	23
Distribution and Services	350	20
TOTAL	1,750	100

Source: Télésystèmes

The breakdown of Télésystèmes' outsourcing revenues largely mirrors this activity with France Telecom accounting for 40% of the company's outsourcing revenues, and the other principal areas of outsourcing focus being:

· Manufacturing companies
· Public sector
· Radio and television companies.

To support its development of outsourcing in these sectors, Télésystèmes will increasingly focus on application operation contracts which involve re-engineering mainframe-based applications onto UNIX platforms.

To support the development of its application operations services, Télésystèmes views access to UNIX-based application software products as essential.

The company can be expected to expand its application software product portfolio.

This portfolio contains the following products applicable to the manufacturing sector:

· *Triton* - production management system

· *Scope Achats* - Télésystèmes' own purchasing system

· *SCOPE Gestion* - accounting and business management.

For local government, Télésystèmes offers:

· *SCOPE Collectivities* - business administration for town and regional councils

· Proconsulix for the administration of Chambers of Commerce.

In addition to these products, Télésystèmes has functional expertise in engineering database management and geographical information systems.

For TV and radio stations, Télésystèmes offers a range of multimedia applications, such as PRIAM and SYMLOOK.

Télésystèmes will focus predominantly on application software products which run under UNIX. All products are currently available under UNIX except Scope Achats which is awaiting conversion from a Bull GCOS 7 environment.

In addition to applications operations, Télésystèmes expects to increase its activity in transition management and network management. Télésystèmes currently only derives 5% of its outsourcing revenues from transition management, though there are signs of the transition management market beginning to grow substantially in France. The company will also become more active in network management. Télésystèmes has recently developed the FRANCE TELECOM product for E-mail systems.

3. Co-operative Relationship with Sema Group

Until 1993, Télésystèmes and Sema Group were competitors in the French outsourcing market. However, in the last year Sema Group has sold its shareholding in Axone to IBM and France Télécom has acquired a 19% shareholding in Sema Group, forging links between Télésystèmes and Sema Group.

Both Télésystèmes and Sema Group recognise the importance of being able to offer outsourcing services widely across Europe, as transEuropean outsourcing contracts became more commonplace and vendors such as Cap Gemini Sogeti, IBM and EDS begin to develop this level of capability.

Neither Télésystèmes nor Sema Group on its own has a wide geographic coverage of the European outsourcing market. However, their national strengths are largely complementary. Hence, it is probable that the two companies will enter a co-operative agreement with respect to outsourcing with Télésystèmes developing its own presence in France, Germany, and Benelux and relying on Sema Group's complementary expertise in the UK, and Sweden.

A co-operative agreement with DIAGRAM will extend Télésystèmes' outsourcing coverage into Spain and Italy.

B

CFM—Working in Partnership with CSL

CFM is a U.K.-based outsourcing vendor jointly owned by ICL (75%) and CLS (25%); a consultancy specialising in assisting public sector organisations. In 1991, the company had outsourcing revenues of approximately £25 million, sufficient to give the company a ranking of sixth place in the U.K. outsourcing market and ninth in Europe. The company is growing rapidly and CFM expects its revenues to exceed £45 million in 1992. By 1995, CFM is targeting revenues of £150 million and a top-3 ranking in the United Kingdom.

In addition to establishing itself more firmly in the United Kingdom, CFM expects to expand its position elsewhere in Europe, via acquisition, to become one of the leading European outsourcing vendors.
CFM aims to achieve its targets by:

· Increasing its proportion of private sector business

· Further developing a full range of outsourcing services

· Providing "totally managed services" or business operations in the Public Sector.

1. Increasing its Proportion of Private Sector Business

Exhibit A-4 provides a breakdown of CFM's client base by industry.

EXHIBIT A-4

Breakdown of CFM Contracts by Industry

Sector	Proportion of Contracts (Percent)
Local Government	50
Central Government	20
Utilities	10
Health	5
Financial Services	5
Construction	5
Discrete Manufacturing	5

At present, CFM's activities are heavily concentrated in the public sector. The company has an estimated 32 outsourcing clients.

Approximately three-quarters of these are public sector organisations, with around half of its clients based in local government.

Examples of public sector clients include:

· Gloucestershire County Council
· Northern Ireland Civil Service
· Wandsworth Borough Council

· Derby City Council
· English Heritage.

CFM can expect substantial growth in its public sector revenues and client base over the next few years, with the introduction of Market Testing. This will lead to many more local authorities evaluating, and adopting systems operations. CFM's local government client base is also increasing by its purchase of Municipal Mutual Computing (MMC), and with 5 local government clients.

However, CFM now wishes to increase its proportion of private sector business to around 40%. This is a difficult challenge in the short term, given the anticipated high growth in public sector outsourcing. The company sees the financial services sector, in which it already has a contract with Barclays Financial Services, as a prime area of opportunity.

2. Developing a Full Range of Outsourcing Services

CFM views outsourcing services as developing outwards along the lines shown in Exhibit A-5.

EXHIBIT A-5

CFM Outsourcing Development Strategy

Totally managed services (Business operations)

Desktop support and IT training of users

Application maintenance and development

Network management

Computer operations
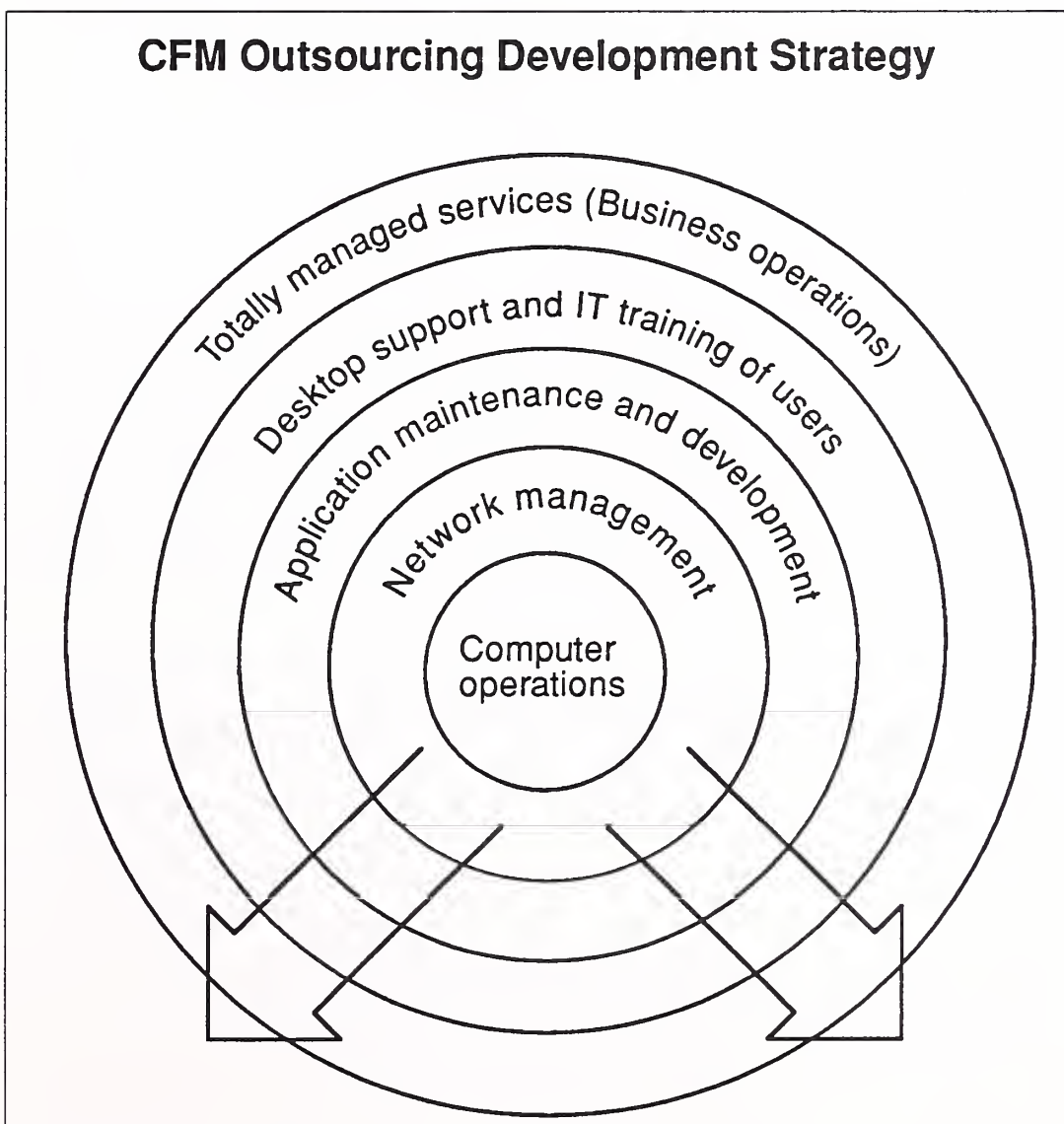
3. CFM Outsourcing Development Strategy

The company intends to offer a full range of outsourcing services, including all of the services shown on this chart. The main areas where it has yet to offer fully packaged solutions are services for the UNIX and desktop environments.

It is likely that CFM will develop a partnership to assist its delivery of desktop services with a major PC dealership.

The current breakdown of CFM's contracts by systems operations subsector is estimated in Exhibit A-6.

EXHIBIT A-6

Breakdown of CFM Contracts by Subsector

Subsector	Proportion of Contracts (Percent)
Applications Operations	60
Platform Operations	
- Transition Outsourcing	30
- Other	5
Network Management	5

Overall, approximately 80% of CFM's local government contracts are applications operations contracts that include systems development. Outside local and central government, the majority of CFM's contracts involve transition outsourcing. Transition outsourcing is a form of platform operations in which the vendor manages the "old systems" on behalf of a client while the "new systems" are developed. It most commonly occurs when users downsize or undergo a major transition between differing platforms.

CFM intends to continue to develop its ability to manage transitions from proprietary architectures to open systems. CFM's data centres already support platforms from IBM, ICL, Digital, Bull, Data General, MDISL and NCR, and the company is actively targeting users of IBM equipment.

4. Providing Business Operations to the Public Sector

CFM's public sector capability is a major strength, and its position in this sector is being strengthened by the acquisition of MMC.

The public sector is also a major outsourcing opportunity in the United Kingdom. Outsourcing growth in the public sector will be above average over the next few years, fueled by the introduction of competitive tendering for local government, and the political inclination to outsource the IS activities of major central government departments.

CFM's partnership with CSL is a major source of capability in the public sector. CSL currently manages several local government treasury departments, and CFM in partnership with CSL will try to make an impact in business operations by offering services such as revenue collection in competition with Telecom Capita. Telecom Capita is the market leader in providing business operation services—principally revenue collection—to local government.

CFM will also move to consolidate its data centres serving local government. At present, CFM has 16 data centres due to local government's concern with protecting the position of its former employees, and this has acted against any consolidation of activities. This is likely to change as the public sector places a greater emphasis on the cost reductions that can be achieved by running a centralised service based around a small number of data centres.

C
BIS—Presence in Local Government Outsourcing through Acquisition

Many of the leading outsourcing vendors in Europe are endeavouring to expand their geographic coverage more widely within Europe. However, one exception to this rule is BIS, which prefers to concentrate on its home market in the United Kingdom, where the company has set itself the objective of being one of the leading five vendors by 1996. Such a target is clearly ambitious, requiring the company to increase its outsourcing business at a rate in excess of 50% per annum over the next four years.

BIS is aiming to achieve this objective by:

· Undergoing repositioning during 1991

· Positioning outsourcing as part of a wider full-service offering

· Stressing the role of outsourcing in unlocking the potential of departmental computing for its clients.

1. Repositioning During 1991

BIS purchased the specialist outsourcing vendor Perthcrest in 1990 as the basis for its systems operation activities in Europe. Perthcrest specialised in targeting the local government sector in the United Kingdom and was largely limited to ICL equipment platforms.

In the last year, BIS Perthcrest has become fully integrated into the systems operations division of BIS Information Systems. During this process its focus has been on three key areas. Firstly, to drive through a customer care programme delivering excellent services at low cost. Secondly, to ensure stable and rewarding careers for staff and thirdly, to develop partnerships which enable clients to exploit new technologies and deal with the rising tide of legislation.

BIS' systems operations division has also supplemented Perthcrest's expertise with increased emphasis on private sector outsourcing and the acquisition of an IBM mainframe data centre from John Laing.

BIS now has three main data centres:

· One in Cambridge with ICL mainframe capability
· One in London with IBM mainframe capability
· One dual-site AS/400 data centre in London.

These key control centres are attached to a further ten satellite centres.

The breakdown of BIS' outsourcing revenues by equipment platform is listed in Exhibit A-7.

EXHIBIT A-7

1992 Revenues by Equipment Platform

Equipment Platform	Proportion of Outsourcing Revenues (Percent)
IBM mainframe	60
ICL mainframe	30
Bull and midrange	10
Total	100

Accordingly, BIS now has a spread of platform capability which is much more appropriate for targeting private sector outsourcing in the United Kingdom.

In total, BIS has approximately 20 outsourcing contracts in the U.K. divided equally between the public and private sectors. Examples of the company's outsourcing contracts are provided in Exhibit A-8.

EXHIBIT A-8

Examples of Outsourcing Contracts

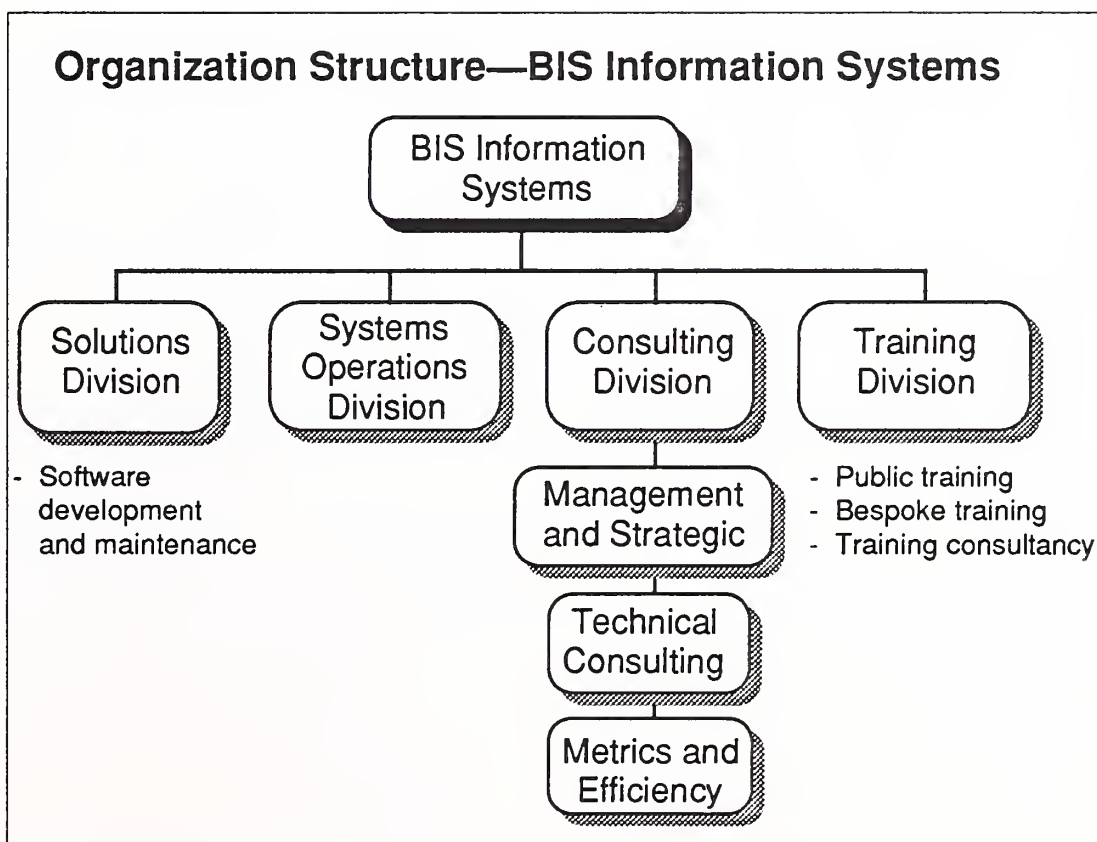| Client	Contract Value (£M)	Length of Contract (Years)
John Laing	10.0	3
Three Rivers District Council	2.6	5
Spelthorne Borough Council	3.0	5
Rochford District Council	2.0	5

2. Part of a Full-Service Offering

The BIS Group, which is owned by NYNEX, consists of the following:

- BIS Banking Systems
- BRANN
- BIS Strategic Decisions
- BIS Information Systems.

BIS Information Systems is organised as shown in Exhibit A-9.

EXHIBIT A-9

Organization Structure—BIS Information Systems

```
                    BIS Information
                       Systems
                          |
   ┌──────────┬───────────┼───────────┬──────────┐
Solutions   Systems    Consulting    Training
Division   Operations   Division     Division
           Division        |
                      Management
- Software            and Strategic      - Public training
  development             |              - Bespoke training
  and maintenance     Technical          - Training consultancy
                      Consulting
                          |
                      Metrics and
                      Efficiency
```

The company envisages that the boundary between the Solutions Division and the Systems Operations Division will gradually disappear, in favour of an Outsourcing Division. This will enable outsourcing clients to take advantage of BIS' software infrastructure, including a BS5750 approved software factory.

As BIS' account managers build on their knowledge and understanding of clients' businesses, so BIS will be able to make a larger contribution in assisting clients to plan their use of IS. This, in turn, will lead to a grater involvement in integrating systems on behalf of clients, and to BIS becoming a full-service provider to the client. BIS is monitoring the progress of the business operations market, and may target such services in the future.
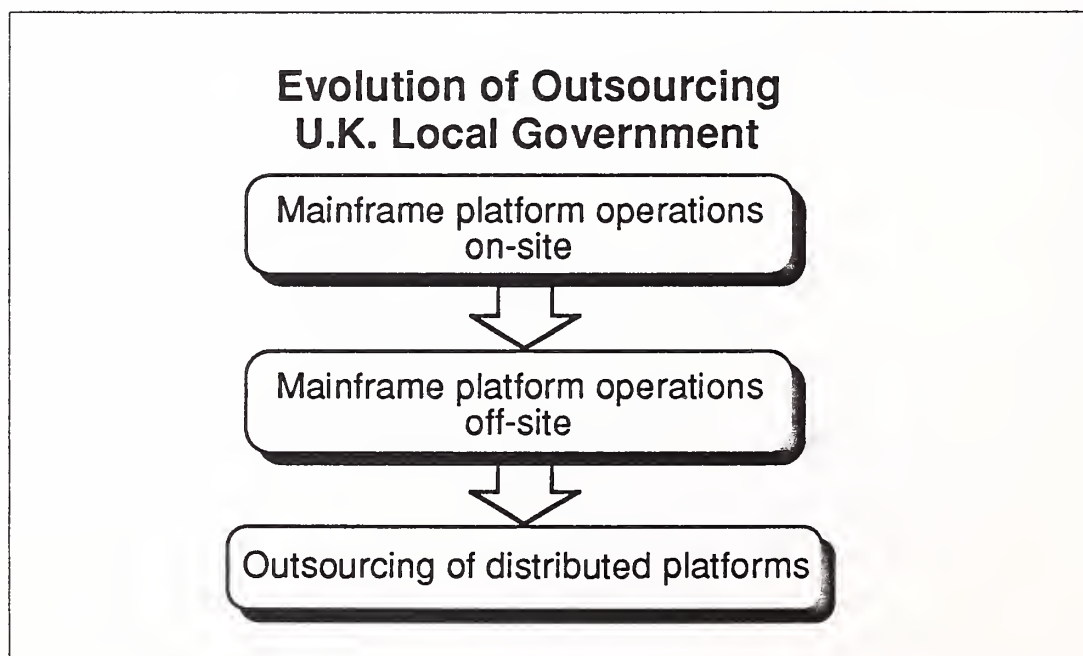
BIS is actively seeking partnerships with application software product vendors to assist BIS in developing its full-service capability. Industry sectors which are being targeted by BIS include:

· Government
· Utilities
· Finance sector
· Retail.

3. Unlocking the Potential of Departmental Computing

BIS expects local authorities in the U.K. typically to follow the pattern of outsourcing shown in Exhibit A-10.

EXHIBIT A-10

**Evolution of Outsourcing
U.K. Local Government**

Mainframe platform operations on-site

Mainframe platform operations off-site

Outsourcing of distributed platforms

Organisations often start by outsourcing their mainframe operations on their own site. Within local government, there is often a strong emphasis on protecting the jobs of former employees. Later organisations recognise that substantial savings can be made by agreeing to off-site platform operations contracts. Finally, organisations recognise the need to migrate to distributed platforms.

This is happening at Rochford District Council, a U.K. local authority, where BIS is managing the implementation and subsequent operation of the new departmental systems.

In the private sector, BIS has a role to play in assisting companies to unlock the potential of departmental computing. Often this will initially involve the transition outsourcing of the company's mainframe, but there are considerable opportunities for vendors to become involved in the subsequent implementation and operation of the departmental systems themselves. Accordingly, BIS is developing its desktop services capabilities. The company has already become involved in LAN implementations for John Laing, although the contract originated solely as transition outsourcing of the IBM mainframe platforms.

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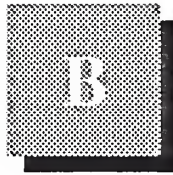
Exchange Rates

Exhibit B-1 shows the exchange rates adopted for use in all INPUT's European forecasts during 1993. Exhibit B-2 shows the changes in country inflation assumptions which will be incorporated into any new forecasts.

All growth forecasts in this report include the inflation figures shown in this exhibit.

EXHIBIT B-1

U.S. Dollar and ECU Exchange Rates, 1993

Country	Currency	U.S. Dollar	ECU
Europe	$	1.00	0.790
France	FF	5.26	6.64
Germany	DM	1.55	1.97
United Kingdom	PS	0.634	0.800
Italy	Lira	1,360.00	1.73
Sweden	Sek	6.24	7.96
Denmark	DK	5.98	7.58
Norway	NK	6.41	8.15
Finland	FM	4.96	6.10
Netherlands	Dfl	1.74	2.20
Belgium	BF	31.91	40.34
Switzerland	SF	1.39	1.75
Austria	Sch	10.89	13.82
Spain	Ptas	110.82	140.30
Ireland	IP	0.589	0.745
Portugal	Esc	138.26	174.00
Greece	Dra	202.32	255.00
Eastern Europe	$	1.00	0.790

Source: OECD February 1993

EXHIBIT B-2

Inflation Assumptions, 1992 and 1993

Country	Percent Assumptions 1992-1997	Assumption 1993-1998	Change (Percent)
France	3.0	2.7	-0.3
Germany	2.7	3.9	1.2
United Kingdom	4.8	3.7	-1.1
Italy	4.4	5.2	0.8
Sweden	6.3	4.0	-2.3
Denmark	2.7	2.4	-0.3
Norway	4.9	3.4	-1.5
Finland	5.0	1.4	-3.6
Netherlands	2.4	3.3	0.9
Belgium	3.3	3.2	-0.1
Switzerland	3.3	3.5	0.2
Austria	2.6	3.2	0.6
Spain	4.7	5.0	0.3
Portugal	8.0	12.5	4.5
Greece	12.0	11.0	-1.0
Ireland	3.0	3.0	0.0
Eastern Europe	-	-	-