Custom Market Research

A Special Analysis of the U.S. Commercial IT Outsourcing Market

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Abstract

This report analyzes the IT outsourcing market in the U.S. from the point of view of relative attractiveness of the federal and commercial markets. Based vendor and user survey results, secondary data and proprietary sources, this report analyzes the characteristics of buyers in each of these markets, the barriers to entering a new market and potential strategies available to overcome these barriers.

In addition, this report provides a summary forecast of the U.S. operational services market, which includes IT outsourcing, Business Process Operations and Processing Services (primarily transaction services). Also, the report analyzes market drivers and trends that underpin expected market growth. Finally, the report identifies various market segments and vertical industries theught to be particularly attractive for IT outsourcing vendors.

The Executive Summary provides a summary of survey results, INPUT's market forecast, and data derived from a variety of sources. This report, which attempts to answer the general question, "Should an IT vendor that is currently active in the U.S. federal market diversify into the U.S. commercial market for IT outsourcing?," constitutes the first part of a three-part research project. The second part will take as its point of departure a positive answer to this question and propose a strategic plan to implement such diversification successfully.

An appendix provides detailed responses to INPUT's survey questionnaire of select vendors and customers of IT outsourcing services. These responses are cross-indexed by company and by question. Also, the appendix provides a summary of terms and definitions used by INPUT in this report along with summary notes on vendors that participated in the survey, or analyzed in the report.

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Table of Contents

I. INTRODUCTION 1

A. Scope and Objectives 1
B. Methodology 3
C. Report Structure 10
D. Related Reports 11

II. EXECUTIVE SUMMARY 12

A. Why Move into Commercial Outsourcing? 12
1. Barriers to Entry 13
2. Profitability 15
3. Comparative Attractiveness of Federal and Commercial IT Outsourcing Markets 15
4. Vertical Industries with the Greatest Potential for Growth of IT Outsourcing 17
5. Direction of Customer Demand 17
6. Cost of Capital as an Obstacle 17
7. Changes at Work in the IT Outsourcing Market Today 18
8. Methodology for Contract Bidding 19
9. Sales and Marketing Costs 19
10. Staff Transfers Resulting from Outsourcing Activity 20
11. Union Policy 20
12. Changes in Customer Attitudes 20
B. Outlook for the U.S. Outsourcing Market 21
1. U.S. Outsourcing Market to Average 22% Annual Growth Until 2005 21
2. Commercial versus Federal Market Growth 23

III. CHARACTERISTICS OF BUYERS OF OUTSOURCING SERVICES 25

A. Federal 25
B. Commercial 28
1. Commercial Buyer IT Budgets 28
2. Buyer Skepticism 29
3. Overall Satisfaction with Outsourcing Declined Between 1997 and 2000 37
4. Vendors Need to Regain the High Ground 40
5. Improved Value for Money Remains Important 43

IV. BARRIERS TO ENTRY 46

A. Lack of Name Recognition 46
B. Insufficient Capital 49
C. Staffing 50

V. IT OUTSOURCING MARKET OVERVIEW 51

A. Market Trends 51
1. The Operational Services Market Is Splitting Up 51
2. Similarly To the Outsourcing Market, The Fastest-Growing Segments of the Processing Services Will Be Internet-Centric Ones 52
B. Market Drivers 54
1. "More and More Customers Were Telling Us, 'We Don't Want to Deal with the Technology, You Handle It. Make This Stuff Work for Us'" 54
2. The Battle to Become King of the Web Hosts 54
3. Buyers Show Growing Skepticism 55
C. Five-Year Outlook for the U.S. IT Outsourcing Market 57
1. Industry Sector Forecast 57
2. Infrastructure Operations Decline To Be Offset by Demand for Internet-Managed Services for E-Commerce 60
3. Distributed Systems (including Desktop Services) To Be Transformed .. 60
4. Network Management Divides into Slow-growing Traditional and Fast-growing Internet-related Segments 61
5. Application Management Undergoing Rapid Shift as Transformation to E-Business Advances 61
6. Applications Services Flow into Three Distinct, New Streams 62

7. Applications Services Market Splitting and Re-Splitting 64
8. Internet-Application Services, Vendor-Owned Software 65
9. Business Process Operations' Fast Growth Linked to Changing Business Models 66
10. Vertical Industry Markets 66
11. Banking & Finance Industry Market, 2000-2005 67
12. Discrete Manufacturing Industry Market, 2000-2005 68
13. Education Market, 2000-2005 69
14. Federal Government Market, 2000-2005 70
15. Health Services Market, 2000-2005 73
16. Insurance Industry Market, 2000-2005 74
17. Process Manufacturing Industry Market, 2000-2005 75

VI. ANALYSIS OF SELECT OUTSOURCING VENDORS 76

A. Market Positioning and Strategy 78
B. Financial Performance 86
C. Financial Trends 93
1. Federal Market 93
2. Commercial Market 94
D. Outlook 96
1. Federal Market Vendors 96
2. Commercial Market 98

APPENDIX 104

A. Summary Vendor Profiles 104
C. User and Vendor Survey Questionnaires 112
D. User and Vendor Survey Results 122
E. Operational Services Market Forecast Summary 228
F. Lou Gerstner Keynote Address, December 2000 234

List of Exhibits

I.

Exhibit I-1 Business Operations Outsourcing 7
Exhibit I-2 Infrastructure Operations Outsourcing Service Categories 7
Exhibit I-3 Outsourcing Service Components 8

II.

Exhibit II-1 U.S. Outsourcing Market 21
Exhibit II-2 U.S. Operational Services Market Summary, 2000-2005 23
Exhibit II-3 Comparative U.S. IT Outsourcing Markets, Projected Compound Average Growth Rates, 2000-2005 24

III.

Exhibit III-1 Current User Environment 32
Exhibit III-2 Future User Plans 33
Exhibit III-3 User Motives for Outsourcing 34
Exhibit III-4 User Reasons NOT to Outsource 34
Exhibit III-5 User Decision-Making Process for Outsourcing 35
Exhibit III-6 User Decision-Maker 35
Exhibit III-7 User Outsourcing Relationship Management 36
Exhibit III-8 User IT Outsourcing Budget 36
Exhibit III-9 User Budget Expectations for Outsourcing 37
Exhibit III-10 Change in Client Satisfaction with Outsourcing: U.S. 1997 to 2000 38
Exhibit III-11 Major Challenges for Outsourcing Vendors: U.S. 1998 to 2000 .. 39
Exhibit III-12 Satisfaction with Vendor Responsiveness: U.S. 1998 to 2000 40
Exhibit III-13 Perceived Roles of Outsourcing Vendors: U.S. 1998 and 2000 41
Exhibit III-14 Delivery of Business Benefit: U.S. 1998 and 2000 42
Exhibit III-15 Satisfaction with Vendor Cost Control: U.S. 1998 and 2000 44

V.

Exhibit V-1 U.S. Operational Services Market, including Business Process Operations 52
Exhibit V-2 Operational Services Segments, U.S. - 2000-2005 57

Exhibit V-3 US Outsourcing Industry Sector Forecast, 2000-2005

Exhibit V-4 Relative Sizes of Forecast Applications Services Market, U.S. – 2000 66

Exhibit V-5 U.S. Outsourcing Market Forecast by Vertical Industry, 2000-2005 67

VI.

Exhibit VI-1 Vendor Ranking 77

Exhibit VI-2 Select Vendors' Market Orientation 80

Exhibit VI-3 Relative Vendor Size by 1999 Revenues 81

Exhibit VI-4 Comparative Proportion of Revenues Derived from IT Outsourcing 82

Exhibit VI-5 Public Sector Market Intensity 83

Exhibit VI-6 U.S. Commercial Intensity 84

Exhibit VI-7 Market Ranking by Factors 85

Exhibit VI-8 Outsourcing Intensity and Gross Profit Margin 86

Exhibit VI-9 Outsourcing Intensity to Operating Margin 87

Exhibit VI-10 Correlation of SG&A to Outsourcing Intensity 88

Exhibit VI-11 Outsourcing Intensity to Net Profit 89

Exhibit VI-12 Outsourcing Intensity to Return on Assets 90

Exhibit VI-13 Level of 1999 SG&A Expense Correlated with Year-over-Year Change 91

Exhibit VI-14 Effective Tax Rates Correlated to Adjusted Ranking as Outsourcers 92

Exhibit VI-15 North American Market for Offshore IT Services (1999 - 2003) 103

APPENDIX

Exhibit C-1 Tabulation Of Vendor Interview Survey Responses By Question 122

Exhibit C-2 Tabulation Of Vendor Interview Survey Responses By Respondent 159

Exhibit C-3 Tabulation Of User Interview Survey Responses By Respondent 198

Exhibit C-4 Tabulation Of User Interview Survey Responses By Question . 215

Exhibit D-1 U.S. Operational Services Market, 2000-2005 228

Exhibit D-2 U.S. Outsourcing Services Market (Incl Bpo), 2000-2005 231

Exhibit D-3 U.S. Processing Services Market, 2000-2005 232

Exhibit D-4 Vertical Industry Market Breakdown, U.S. Outsourcing Market, Including Bpo 2000-2005 232

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I

Introduction

A
Scope and Objectives

The scope of this report is an analysis of the contemporary U.S. IT outsourcing market from the point of view of federal versus commercial markets, in general, and DynCorp, in particular.

The overall objective of this report is to provide an objective basis for DynCorp's decision regarding whether or not to enter the U.S. commercial IT outsourcing market.

To that end, this report will:

- Define and identify major segments of the U.S. operational services (Business Process Operations, transaction processing and IT outsourcing) market. (See attached Terms and Definitions.)
- Estimate the size (and forecast growth rates) of the U.S. operational services market by delivery mode and industry.
- Estimate the size (and forecast growth rates) of each of the market's top ten vertical segments, e.g., manufacturing, telecom, state & local, banking & finance, utilities, etc.
- Analyze the effect on growth rates of key industry trends and drivers,
- Compare and analyze revenue growth for a representative sample of ten publicly held federal and ten publicly held commercial IT outsourcing vendors.
- Compare and contrast the buying practices and characteristics of federal versus commercial IT outsourcing customers based on in-depth interviews with competitor vendors and potential customers.

- Identify key barriers to entry based on interview data and other proprietary sources.
- Identify market segments and trends in the U.S. commercial IT outsourcing market, including:
- Large vs small-size customer opportunities
- Industry and delivery mode

B
Methodology

The data shown in this study was derived from the following sources:

- Telephone interviews with 22 representative outsourcing vendors that are active in both the federal and commercial segments of the U.S. market.
- Telephone interviews with six representative industrial firms in various industries that have experience using IT outsourcing vendors.
- INPUT's previously published report, *Operational Services Market Forecast, 2000-2005—U.S.*
- Secondary sources of industry data.
- INPUT's proprietary sources of vendor and IT market data.

This report reflects data derived from these sources and a proprietary analysis as directed, in part, by DynCorp's executives.

Outsourcing is defined by INPUT as follows.

Outsourcing was previously called Systems Operations in the 1990s and 1980s and Facilities Management in the 1970s and 1960s. Outsourcing is a long-term (greater than one year) contract between a customer and a vendor in which the customer delegates all, or a major portion, of an organizational operation or function to the vendor. Outsourcing vendors now provide a variety of services in support of customers' information systems and electronic business requirements.

- The vendor can plan, control, provide, operate, maintain and manage any or all components of the customer's information systems environment (equipment, networks, applications systems), either at the customer's site or the vendor's site.
- Various Internet and Web-related categories of outsourcing service have emerged to include Internet Managed Services (included in Infrastructure Operations).
- The equipment involved may be at the customer, or vendor's, site and may be owned by the customer, or the vendor. In some markets such as the U.S. Federal Government these options are described by the terms "COCO" (Contractor-Owned, Contractor-Operated), and "GOCO" (Government-Owned, Contractor-Operated).

To be included in INPUT's Outsourcing market forecast, the operation, or function, must be either solely information systems outsourcing, or include information systems as a major component (at least 30% of the costs) of the operation (Business Operations or Business Process Operations). *Note that BPO is not included in the overall Electronic Business and IT Software and Services market.*

The critical components that define an outsourcing service are:

- Delegating an identifiable area of the operation to a vendor
- Single-vendor responsibility for performing the delegated function
- Intended, long-term relationship between the customer and the vendor, where:
- The contract term is for at least one year
- The customer's intent is not to perform the function with internal resources
- The contract may include non-information systems outsourcing activities, but information systems outsourcing must be an integral part of the contract.

Business Process Outsourcing is a relationship in which one vendor is responsible for performing an entire business/operations function including the IT outsourcing that supports it. The IT outsourcing content of such a contract must be at least 30% of the total annual expenditure in order for INPUT to include it in the BPO market. (N.B.: the IT operational services market forecast excludes the BPO segment.)

Information Technology (IT) outsourcing can be viewed as a component of the Business Operations Outsourcing market (*i.e.*, Information Technology systems Outsourcing is a business/ operations function, *see* ***Error! Reference source not found.***). However, in order to delineate between outsourcing contracts that are solely IT versus those that include IT as well as other functions, IT Outsourcing will be segregated from Business Operations Outsourcing. Information Technology outsourcing is divided into four service components as shown in Exhibit I-2.

Infrastructure Operations outsourcing describes a relationship in which a vendor is responsible for managing and operating a client's computer system/data center (Platform Systems Operations) or developing and/or maintaining a client's application as well as performing Platform Operations for those applications (Applications Systems Operations). Internet Managed Services comprises a complementary subsector related to, but distinct from traditional, mainframe-oriented Platform Operations.

Distributed Systems (Desktop Services) describes a relationship in which a vendor assumes responsibility for the deployment, maintenance and connectivity of personal computer, workstations, client/server and LAN systems in the client organization. In addition, this market segment includes management services for a wide variety of portable, wireless and other handheld computing/telecom devices that are increasingly Internet-enabled.

To be considered as Distributed Systems (Desktop Services) outsourcing, a contract must include a significant number of the individual services listed below.

- Software Product Supply
- Equipment Supply
- Equipment/Software Installation
- Equipment Maintenance
- LAN Installation and Expansion
- LAN Management
- Network Interface Management
- Client/Server Support
- Logistics Management
- User Support
- Help Desk Functions
- User Training and Education

Network Management outsourcing is a relationship in which a vendor assumes full responsibility for operating and managing the client's data telecommunications systems. This may also include the voice, image and video telecommunications components.

Beginning with the current forecast report, this segment has been divided into traditional IT network management and Internet Network Management. While this sub-segment is expected to grow rapidly during the forecast period, toward the end of the period the distinction between the two segments will become progressively less important as "Internet-enabled" becomes the new standard.

Application Management is a relationship in which the vendor has full responsibility for developing and maintaining all of a software application, or software function. Beginning with the current report, this segment has been divided into "IT Applications" and "Internet/Web Applications" in order to highlight e-business and e-commerce-related applications.

As was the case with *Network Management*, the Internet/Web segment is expected to grow rapidly. However, toward the end of the forecast period, the distinction will become less important as most, if not all software applications are sold and used in Internet/Web environments.

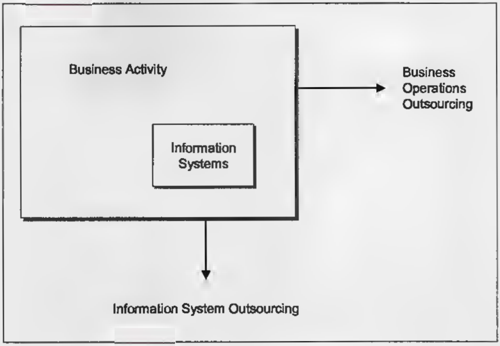
During the 2000-2005 forecast period, INPUT believes that the traditional, legacy IT Applications segment of the Applications Operations market will grow slowly at a CAGR of 11%. The Internet Applications Services stream that represents software delivered via the Internet directly by software developers, such as Oracle, PeopleSoft and SAP, will grow much faster at 47%. However, this growth will moderate toward the end of the period as many developers abandon their direct distribution channels in favor of partnering with ASPs—which is already happening. Accordingly, the very high growth of the third-party software, or ASP, segment will moderate as the market matures and as vendor consolidation is largely completed.

The Processing Services market comprises Transaction Processing, Utility Processing, and Other Processing.

- **Transaction Processing** - The client uses vendor-provided information systems—including hardware, software and/or data networks—at the vendor's or customer's site to process specific applications and update client databases. Required application software is typically provided by the vendor.
- **Utility Processing** - The vendor provides basic software tools (language compilers, assemblers, DBMSs, graphics packages, mathematical models, scientific library routines, etc.), enabling clients to develop and/or operate their own programs or process data on the vendor's system.
- **Other Processing Services** - The vendor provides a service—usually at the vendor site—such as scanning and other data entry services, laser printing, computer output microfilm (COM), CD preparation and other data output services. This category also includes backup, contingency and disaster-recovery services.

Exhibit I-1

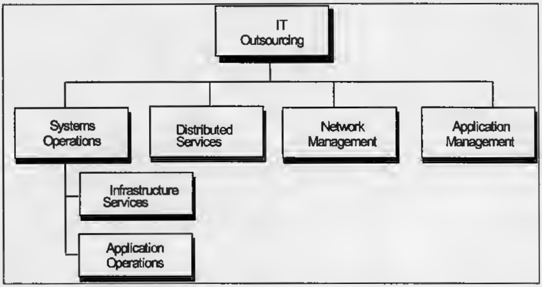
Business Operations Outsourcing



Source: INPUT

Exhibit I-2

Infrastructure Operations Outsourcing Service Categories



Source: INPUT

The above definitions focus on the services covered in the outsourcing contract. For example, an Application Operations contract can include all facets of Information Technology Outsourcing (platform operations, desktop services, network and application management).

The key to INPUT's market definition is the service contract. If a customer only wants to outsource the network, the contract would be considered network management outsourcing. If an airline, for example, wishes to outsource its reservation operation, which includes not only the network, but also its infrastructure, applications and the people running the operation, the agreement would be considered a Business Operations Outsourcing contract.

Exhibit I-3 shows the service components that may be included in each outsourcing service category.

Exhibit I-3

Outsourcing Service Components

Component	Infrastructure Ops	Appl. Ops.	Distributed Systems (Desktop Services)	Network Mgt.	ApplMgt	Business Ops.
Project/Contract Management	x	x	x	x	x	x
Data Center Management	x	x				x
Client/Server Operations	x	x	x			x
Equipment Maintenance	x	x	x			x
System Software Maintenance	x	x	x	x		x
Application Software Maintenance		x	x		x	x
Application Development		x			x	x
LAN Management		x	x	x		x
Network Management		x		x		x
Transaction Processing Services		x				x
Other Professional Services		x	x		x	x
Business Process Operations						x

Source: INPUT

The largest, most visible contracts awarded over the past year have been typically Application Operation outsourcing contracts since they included management of the infrastructure (various computing platforms) and the support of legacy applications. In the past, most Application and Platform Operation outsourcing contracts included network management, but recent contracts have also included desktop services.

INPUT excludes from the outsourcing category the following:

- Project based services are not considered as part of outsourcing. Thus, systems integration and application development projects are excluded

- Services that were never intended to be performed internally. Maintenance-only services do not constitute an outsourcing function in themselves. However, responsibility for hardware and software maintenance is assumed in most outsourcing contracts
- Processing services contracts of less than one year
- Voice-only network management
- Business operations with minimal information systems content. For example, the outsourcing of the marketing communication function to an outside agency is not covered by INPUT's analysis. A function or business operation must at least have 30% of its budget attributed to information technology to be included.

C
Report Structure

Chapter II consists of the Executive Summary, which is a summary of the key findings of the report.

Chapter III analyzes characteristics of buyers of outsourcing services in both the federal and commercial markets.

Chapter IV analyzes barriers to entry for outsourcing vendors that are attempting to enter a new market, in particular, the U.S. commercial market.

Chapter V provides a discussion of market trends and drivers that are affecting growth by segment and by industry in the U.S. IT outsourcing market.

Chapter VI provides an analysis of twenty representative IT outsourcing vendors that are active in both the federal and commercial markets, comparing identifiable differences in their respective financial performance.

The Appendix includes:

- Copies of the Vendor and User survey questionnaires;
- An excerpt from INPUT's handbook of terms and definitions for reference;
- A summary of recent events and background regarding the vendors analyzed in Chapter VI.
- A summary excerpt of INPUT's market forecast for the U.S. operational services market during the period 2000-2005 for reference.

D
Related Reports

Operational Services Market Forecast, U.S. 2000-2005

Outsourcing Vendor Performance Analysis U.S.- 2000

IT Services Contract Activity Summary – 3Q 2000

IT Services Contract Activity Summary, 2Q 2000

IT Services Contract Activity Summary - 1Q 2000

The New Electronic Business Services Industry, U.S.

Leading Electronic Business Vendors

Evaluation of Business Process Outsourcing, U.S. 1999

II

Executive Summary

A

Why Move into Commercial Outsourcing?

While commercial IT outsourcers as a group show no clear-cut trends toward higher profitability than federal outsourcers or non-outsourcers, nevertheless, there are compelling advantages to being active in this market, including:

- The IT outsourcing and IT-related BPO markets are poised for faster growth than most other IT market segments.
- The commercial IT market is growing at a faster rate than the federal market; some segments are growing dramatically faster (as shown in **Error! Reference source not found.**).
- The expertise and experience gained in the commercial market will enhance success in federal market, which prizes commercial best-practices.
- Commerical market work facilitates attracting and retaining top IT skills because it provides exposure to more challenging and varied types of work (of at least such is the perception).
- The most profitable IT vendors are diversifying their sources of revenue by being active in as many markets as possible.
- Establishing long-term relationships with commercial companies facilitates expansion outside of the U.S. by following client activities abroad.
- Expanding the number and diversity of clients in itself promotes greater efficiency in the use of resources.

- Finally, as an executive at Getronics remarked, "Seat management (or outsourcing in general) is like getting the camel's nose under the tent." There was a consensus among survey respondents that participation in the outsourcing market served as an excellent means of learning about customer needs as a prelude to bidding on incremental, more profitable, non-outsourcing work in the future.

1. Barriers to Entry

Despairing that "the commercial world is vast," at the same time, vendors admitted that there is little evidence of any significant bias against IT vendors that have primarily, or exclusively, federal experience.

However, vendors and commercial clients alike are skeptical about the very concept of industry-neutral, vertical applications, such as HR, accounting and CRM. Commercial customers prefer vendors able to demonstrate expertise in their particular industries.

Also, entering a new market without established partnering relationships is very difficult. Generally, effective vendor partnering was cited frequently as an excellent means of entering a new market and overcoming otherwise insurmountable barriers. Once "in," this work as a sub can be used as reference work to gain new work in the same industry as a prime.

Ability to obtain and keep good partner relationships depends on vendors understanding accurately what their core competencies really were.

There is a consensus that partnering with larger, prime vendors is one key means by which to gain this needed industry experience.

At the same, ability to select and negotiate these partnership agreements is critically important. There is always a certain level of competitive tension today among partners that are likely to be adversaries and competitors tomorrow.

Top-tier IT vendors are highly vulnerable to price competition. Vendors able to offer convincingly attractive service packages at substantially lower cost will always find commercial takers. Even the most satisfied users are ready to listen to such offers.

Overall, INPUT has documented significant erosion in vendor loyalty among commercial customers for IT outsourcing over recent years. This means that a growing number is receptive to switching vendors, which reduced they value of incumbency and provides opportunity to new market entrants.

Partly for this reason, selecting prospective commercial customers according to revenue size is less likely to succeed than targeting specific types of industry-specific outsourcing work that can be offered at lower cost—even to the largest organizations.

While sales in both federal and commercial markets benefit from having good inside contacts, this appears to be more of a factor in the federal market—despite efforts to make the procurement process transparent and efficient.

Prospective commercial customers value inside referrals, but they are obligated to put their highest priority on cost and performance—which is often linked to demonstrated industry expertise.

Larger vendors, such as EDS, are positioning themselves to be long-term, strategic advisors to customer managements rather than suppliers of short-term IT solutions. For many, this is clearly the direction of the commercial market.

Significantly, users concur, but show some growing resistance to depending too heavily on vendors for such guidance from lingering fear of conflicts of interest, or inability to really understand their industry-specific problems.

Federal vendors attempting to enter the commercial market may be unprepared for "cut-throat" nature of commercial competition," cited by one survey respondent.

- In his opinion, federal market salesmen are more collegial and adopt easily a cooperative stance among each other.
- In contrast, commercial vendors have no need to deal with GSA schedules, or similar bureaucratic obstacles.
- Also, salary levels commanded by commercial sales staff are much higher than those applicable to the federal sales staff. For example, while salesmen work in the federal market for $75,000, their counterparts in the commercial market are earning $200-300,000 annually in commission income.
    - ❑ Overall, vendors believe that moving from the federal to the commercial market requires forming and fielding an entirely new sales team. A few dissenters, such as ACS, believe that there is merit in regular collaboration between the teams—to the point of bringing commercial clients to see work underway in the federal market. However, most vendors insist that this constitutes one of the most significant barriers to be overcome.

2. Profitability

Many vendors, such as Litton/PRC, believe that low-margin seat management (or distributed services) outsourcing is an excellent way to get a "foot in the door" for more profitable business, such as network management. Overall, vendors stress that the more customer work can be done remotely, the more profitable it will be.

There is a consensus among both customers and vendors that customer cost and vendor profitability can be ranked as follows by IT function from most profitable to least profitable:

1. Consulting
2. BPO
3. Systems integration
4. Network services
5. Application management and services (including development)
6. Infrastructure services
7. Distributed services (desktop and seat management)
8. Staffing and facilities management
9. Processing services

- By definition, only the middle four segments qualify as IT outsourcing. Nevertheless, most vendors aspire to be active in those markets because they lead the way to the more profitable segments and can be structured so as to include the segments that are less profitable on a stand-alone basis.

- For some vendors, "the critical key to profitability is not the size of the margin associated with a given contract, but the way in which the contract is managed and strategized, i.e., how this contract/business fits into a comprehensive sales/marketing plan."

- Expect break-even 1-2 years into a contract assuming a seven-year term. Outsourcing is typically low-margin in the early years.

3. Comparative Attractiveness of Federal and Commercial IT Outsourcing Markets

Vendors not active in the federal market were generally repelled by what they perceived to be excessive bureaucracy, the slow pace of change and the long sales cycle. Also, the federal market was perceived to be less profitable than the commercial market—with lower growth potential.

Other vendors avoided the federal market because they didn't believe that there was demand there for the type of products and services that they offered.

In contrast, many of the vendors that were already active and experienced in the federal market saw attractive potential in seat management, network services, security and other outsourcing market segments.

- For example, Fed Data sees excellent potential for new business desktop management business (task orders) from the DoD, Army and Air Force. These agencies are now trying to follow the example of the Navy's NMCI contract. While they don't anticipate any dramatic new budget allocations, the DoD appears increasingly willing to change existing budget allocations in order to roll up GSA task orders and other BPA contracts in to evermore comprehensive "bundled" large contracts for a wider range of work. In this context, the respondent corroborated opinions expressed by other vendors to the effect that the federal government's entire IT infrastructure would be virtually obsolete in less than five years. This reality, along with the skills shortage, budget restrictions and pending retirements, would make IT outsourcing unavoidable.
- Raytheon sees the intelligence agencies (partly for this reason) as particularly fertile grounds for new business.
- In addition, vendors believe that many skills are transferable between the federal and commercial markets—which argues in favor of participating in both. These skills include: program management, ability to deal in complex issues, application of externally documented technical expertise, whether from Carnegie Mellon or the Software Institute.
- A few vendors, such as Lockheed Martin, believed that "the government is a better buyer than commercial market buyers of IT outsourcing services." Reason:
  - The government knows how to deal with outsourcing services and has senior executive IT managers.
  - In the commercial market, outsourcing project liaison is often handed over to junior IT staff.

4. Vertical Industries with the Greatest Potential for Growth of IT Outsourcing

Vendors as a group are most sanguine about telecom, financial services, manufacturing and retail as the industry sectors with the best potential for growth of new outsourcing business. As an example, Convergys derives 80% of its revenue from the telecom sector; Bisys and Fiserv are similarly heavy the financial services sector.

Some vendors, such as EDS and Perot Systems, are very bullish on the prospects for the health care, transportation and energy sectors (including utilities). EDS targets the "emerging" transportation sector of car rental and airfreight.

A few vendors, such s Keane, singled out the public sector (state & local) as having outstanding growth opportunities.

While there was understood to be little difference between verticals from a technology point of view, vendors and customers both stressed the importance of industry-specific expertise that permitted vendors to understand the business problems of customers.

Some vendors, such as Lockheed Martin, avoid specialization around particular vertical industries; others view this as both required and inevitable.

5. Direction of Customer Demand

Almost without exception, vendors believe that the outsourcing market is moving "upstream" toward more comprehensive, bundled solutions because customers want to simplify and streamline their operations by offloading as many management burdens as they can relate to IT.

Vendors had mixed opinions regarding the attractiveness of non-IT-oriented facilities management. Some thought it too low-margin to be attractive; others saw it as growing more rapidly than IT outsourcing and, therefore, too big to avoid, even if more difficult to work in profitably.

6. Cost of Capital as an Obstacle

No vendor survey respondent believe that either cost or availability of capital has been (or should be) a barrier to growth of IT outsourcing business. Reasons: some vendors have very deep pockets and respondents couldn't recall every being told that capital wasn't available; others insisted that capital requirements could easily be covered by using leasing companies as partners.

Dissidents, such as SAIC, insisted that the use of leasing imposed a cost burden on customers that few would find acceptable. Beyond that, most vendors believed that availability of capital was only an issue with data center outsourcing—and few of them found this to be an attractive market for a variety of reasons.

A few vendors cited problems of increased tax burdens that arose when federal agencies transferred assets to commercial vendors (government agencies are not subject to property tax while private organizations are).

For their part, customers generally prefer to obviate risks of hardware obsolescence, network management burdens and the skills shortage by buying IT services (software, hardware and management services) by the "sip" on an as-needed basis.

7. Changes at Work in the IT Outsourcing Market Today

The ASP model may be the "outsourcing light" and attractive to customers, but few, if any, pure ASP vendors are profitable. Vendors should consider ASP (remotely delivered applications) as only part of a comprehensive solution or customer relationship.

A Keane survey respondent went further, insisting that "the ASP model has failed—at least insofar as having an appeal for Keane's target market of Global 2000 organizations. They require significant amounts of customization, cannot use "plain Vanilla" applications. Therefore, ASPs cannot serve their needs cost-effectively."

Customers are outgrowing their IT infrastructures and use outsourcing as a solution to their scalability problems.

Cost-savings remain important, but they are not paramount in importance (partly because of the difficulty in measuring them).

Customers are using outsourcing consultants with increasing frequency. Some vendors saw the move as very positive and reflecting a growing sophistication of vendor/client relationships. Others were skeptical that consultants, who are paid on a T&M basis, could easily abuse vendors by running up their costs as a means of currying favor with customers (as well as higher fees). Many survey respondents urged caution in regard to the use of consultants. Consultant costs can run up to 5% of total contract value and be paid both by vendors and customers.

Overall, vendors see the outsourcing market as moving strongly in the direction of BPO contracts, in which IT plays only a limited role.

However, one survey respondent was skeptical, saying:

- "At the same time, vendors should be aware that the opportunity is greater than the reality.
- Clients continue to be reluctant to hand over to vendors too much of what they perceive to be "control" over their core business processes, so fulfilling the market's potential remains a hard sell.
- Also, never forget that there is always internal resistance to BPO. Incumbent employees always fear that headcount reductions will inevitably follow any BPO contract, if not all outsourcing."

8. Methodology for Contract Bidding

Few vendors admit to having any "black box" comprising sophisticated computer models used either to prepare outsourcing contract bids, or compute contract profitability on an on-going basis. Of, if they did have such a box, they weren't willing to provide any details.

Overall, vendors stress the importance of approaching outsourcing with a repeatable discipline the sales and bid preparation process all the way through the project management cycle, including the development and implementation of technical solutions.

Use of Total Cost of Ownership studies as part of the sales and bid process is becoming more common. However, care should be taken that these are prepared by independent, third-parties in order to maintain credibility.

Some vendors, such as Getronics, admitted that it was common for vendors to "take hits" for unexpected costs and that this was unavoidable as conditions changed unpredictably.

9. Sales and Marketing Costs

There is a general perception that sales and marketing costs are higher in the commercial market, even though in some cases, very lengthy federal bids can cost millions of dollars.

Some vendors, such as CSC, use a "pursuit model" that caps permissible sales and marketing costs as a percentage of total contract value—typically 5-10%.

While in the minority, Fed Data reports marketing costs of up to 20% of the total cost of doing business, with 10-15% being considered "normal" in the federal market and 6-9% in the commercial market.

Lockheed Martin believes that costs are lower with commercial outsourcing deals because the federal procurement process can be quite lengthy: "As an example, a $750 million federal market deal took three years to negotiate and cost LM millions in expense. In contrast, a commercial deal valued at $350 million required only 12 PowerPoint slides to close the sale." In fact, vendors often believe that which side of the market that they are active in—federal versus commercial—costs on the other side are lower.

10. Staff Transfers Resulting from Outsourcing Activity

No vendor believes that inability to absorb customer staff as part of an outsourcing contract has caused problems. However, they stress the importance of being able to attract, employ and retain staff.

One key to success is having an organizational structure that offers newly acquired staff ample opportunity for advancement. In particular, a matrix organizational structure whereby staff can move freely among projects and industries is considered advantageous—if well executed.

11. Union Policy

No vendor believes unions to constitute an obstacle to new outsourcing business. However, some believe that forging good relations with unions can be highly advantageous.

Most vendors believe that unions will be "marginal players" in the IT industry for the foreseeable future.

12. Changes in Customer Attitudes

In the federal market, pricing caps are an increasingly effective barrier to new business. Vendors complain that bids more than 5% higher than that of a competitor are rejected immediately.

Today, time-to-market issues are more important than ever. Vendors need to good, cheap AND fast.

Service levels and business value have top priority among customers today.

Neither vendors nor customers want to form their business partner relationships based on size of revenues. The key criterion is trust and the nature of core competencies.

B

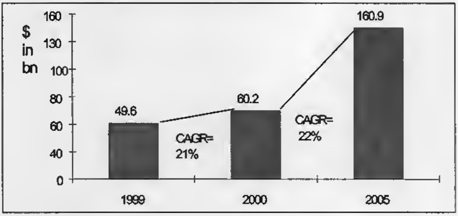
Outlook for the U.S. Outsourcing Market

1. U.S. Outsourcing Market to Average 22% Annual Growth Until 2005

INPUT's overall forecast for the U.S. outsourcing market, including Business Process Operations, is shown in Exhibit II-1Exhibit II-1.

Exhibit II-1

U.S. Outsourcing Market



Source: INPUT

The U.S. market for operational services is splitting along two tracks—traditional, legacy services and Internet-centric services. In last year's outsourcing market forecast, INPUT included "Internet/intranet management" as a single, functional segment. This year, virtually every functional segment has been split and forecasts provided for each separately.

Although the year-over-year growth of the Internet-centric segments is forecast to remain high over the next few years, before the end of the forecast period a convergence will begin that signals the effective disappearance of a non-Internet-enabled legacy IT infrastructure. At that point, the Internet will be so thoroughly integrated into business processes and operations that all operational services will take it into account.

Accordingly, the decline in mainframe platform operations services that would otherwise have been expected will reverse itself as the demands of e-commerce and the requirements for massive data storage for e-business give mainframes new importance.

Currently, applications services are separated into three streams:

1. Those required by traditional enterprises for their own licensed software (or customized software to be purchased on a license basis)

2. Applications purchased on an outsourced basis directly from software developers

3. Applications provided to value-added resellers (Application Service Providers) of various types that make them available on a pay-as-you-go basis

The last two market segments will grow rapidly over the next few years, but before the end of the forecast period INPUT foresees much of today's business in this market falling into the Business Process Operations and Processing Services categories.

They key criterion will be the extent and nature of the responsibility assumed by vendors for their customers.

Similarly to the outsourcing market, the fastest-growing segments of the processing services will be Internet-centric ones. Yet, before the end of the forecast period, they will begin to converge with the heretofore designated "legacy," or traditional segments of the market as the Internet is used ever more widely and as the transformation of enterprises to e-business (and e-government) continues. Eventually, the distinction between the two streams (Internet-centric and legacy) will lose relevance.

Exhibit II-2 forecasts in summary the U.S. Operational Services market by delivery mode over the period 2000-2005.

Exhibit II-2

U.S. Operational Services Market Summary, 2000-2005

	Market Forecast (U.S. $ Billions)				
	1999	Growth 1999-2000 (%)	2000	Growth 2000-2005 (%)	2005
Infrastructure Services	8.7	*10%*	9.6	*17%*	20.6
Applications Operations	16.5	*19%*	19.7	*17%*	43.0
Distributed Systems (Desktop)	6.1	*25%*	7.6	*19%*	17.7
Network Management	6.7	*27%*	8.5	*26.4%*	29.0
Applications Management	1.9	*32%*	2.5	*27%*	8.2
Total IT Outsourcing	**40.0**	***19%***	**47.7**	***19%***	**115.9**
Business Process Operations	9.6	*30%*	12.5	*29%*	45.0
Processing Services	42.2	*14%*	48.1	*15%*	98.8
Total Operational Services and BPO	**91.8**	***18%***	**108.3**	***19%***	**259.7**

Source: INPUT

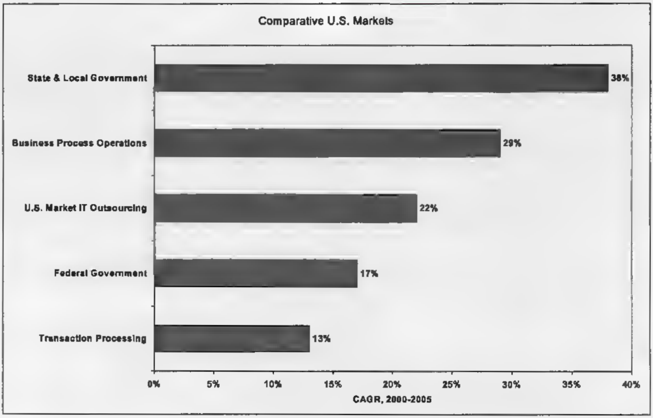
2. Commercial versus Federal Market Growth

Exhibit II-3 portrays the comparative, projected growth rates of various components of the U.S. outsourcing market by relative attractiveness.

While small, INPUT projects superior growth for the State & Local Government market (38%) and much slower growth (13%) for the Transaction Services (or transaction processing) market. Nevertheless, the difference between the relative sizes of these markets today is great. Overall, the mature Processing Services market at $54 billion is 32 times larger than the emerging State & Local market at $1.7 billion, based on projected, year-end 2001 projections.

Exhibit II-3

Comparative U.S. IT Outsourcing Markets, Projected Compound Average Growth Rates, 2000-2005



Source: INPUT

III

Characteristics of Buyers of Outsourcing Services

A
Federal

Vendor participants in INPUT's survey undertaken for this report had some very sharp impressions of the characteristics of the federal market customer. From the point of view of IT outsourcers, they had a number of positive characteristics, including:

- The government's concept of seat management is evolving and becoming increasingly comprehensive. Eventually, it will become something like BPO in the commercial market. This process will take 4-5 years. At present, they are putting out to bid increasingly extensive pieces of work.

- Management considers the public sector (including federal) market unattractive because of excessive bureaucracy and the slow pace of change. Applicast wants to work with customers that are ready to transform themselves, and quickly. Applicast management perceives the public market as lacking in opportunity to achieve innovative implementations in a short timeframe. Conversely, it is seeking to build a client base among fast-growing, innovative commercial companies. It would rather expand into complementary vertical industries.

- Convergys doesn't believe there is a place for it in the federal market because it specializes in mission-critical applications. Its customers prefer its solutions because they are field-tested. Respondent doesn't believe that the kind of work that the company does has a wide application in the federal market, except perhaps at the IRS. In his view, "the federal market is a world unto itself."

- The DoD, among other agencies, appears increasingly willing to change existing budget allocations in order to roll up GSA task orders and other BPA contracts in to evermore comprehensive "bundled" large contracts for a wider range of work.

....as well as some that made the federal market significantly <u>unattractive</u>, including:

- For some federal customers, seat management contracts are used as a back door vehicle to buy hardware when they can't access a capital expenditure budget. HW purchases are built into the seat management contract under the guise of periodic equipment "refresh" and using existing GSA schedules.

- Federal budget politics often requires agencies to spend money on a time & materials basis even when this is contrary to the best interest of both the government and the taxpayer.

- Even if there is a great deal of similarity between the business processes of government agencies and commercial businesses, vendors can trip on unforeseen differences in approach. For example, Getronics prepared TCO studies for its seat management solution (a common practice on the commercial side) only to be told that they violated FAR 9.5, which prohibits vendor conflicts of interest. (Solution: these need to be prepared by a third-party, not the vendor directly—especially if based on privileged information that is available only to qualified federal contractors).

- One obstacle to federal business that was cited by numerous vendors in the federal market was the anti-outsourcing lobby. Respondents believed strongly that union-led efforts to kill federal outsourcing would lead to disaster. The A-76 machinery in place that attempts to verify the cost-effectiveness of outsourcing is not working well because of the many difficulties in the way of computing federal costs. "Savings" can be deceptive, primarily because they ignore the need for technology "refresh." The desire of federal employees to assure their job security is understandable, but doomed. The skills shortage will grow ever more acute. Also, the federal "customer" is incapable of foreseeing technological advances. The slow procurement cycle ensures that almost whatever is purchased will be obsolete, or almost obsolete by the time it is implemented.

- The federal skills shortage will worsen—which also exacerbates the ability of federal market vendors to serve the federal customer. Vendors ask why young techies would want to work for the government, "when they typically have more computing power on their wrist watches, or in their PDAs than they can find on many agency desktops." In their view, techies will be attracted to work environments were they can use cutting-edge technology.

- "Currently, Perot Systems does not compete for Federal contracts. Tbis should provide the strongest answer of tbe burden in pursuing that business."

Overall, vendors complain about the extended sales cycle and potentially high bid preparation costs imposed by efforts to do business in the federal market.

While some executives praise federal buyers as sophisticated and demanding, a larger number lament the bureaucracy of the decision-making process, and the limited scope of IT outsourcing to be done—at least in comparison with national and global commercial markets. Finally, although tbey are impressed by the size of some federal contracts, tbey are underwhelmed by tbe profit margins available AND by the scrutiny that margins attract.

Because DynCorp has been active in the federal market and his familiar with it on a direct basis, it is more important to understand characteristics of commercial buyers, as follows.

B
Commercial

If federal buyers are difficult, commercial buyers are skeptical.

At the same time, there are numerous signs that point to a significant slowdown in spending—partly a result of macroeconomic factors and partly as resistance to vendor efforts to sell them technology that they don't need.

A recent study by securities broker Merrill Lynch surveyed 50 U.S. and 20 European CIOs and concluded that IT budget growth in the U.S. could slow by more than half to about 5% in 2001 compared with about 11% growth in 2000 (compared to INPUT's forecast of 19% growth). Almost one-third of respondents said they had not factored a slowing economy into their budgets, and 22% had yet to complete their budgets for 2001.

- Microsoft's Windows 2000 operating system was top of the list of IT products that would be purchased this year. Microsoft warned last month it faced slower revenue growth because of PC market woes and softness in IT spending.
- Network equipment, data storage systems and servers and PCs were also high on the list of IT budget spending.

1. Commercial Buyer IT Budgets

A December 2000 survey of 150 CIOs conducted by Morgan Stanley Dean Witter suggested that corporate IT budgets should rise at a more modest rate in 2001 than they did in 2000.

- CIOs surveyed said their companies plan to increase IT spending by an average of just 8% in 2001 compared to an average budget increase of 12% in 2000.
- Fully 16% of the respondents said their IT investments will actually decrease from 2000 to 2001.

...however, in some cases, the reasons were quite positive.

For example, Ed Tobin, CIO at Colgate-Palmolive Co. in New York, said that he's cutting his technology budget this year, mainly as a result of the efficiency of recently installed enterprise application integration systems.

Jack Cooper, CIO at Bristol-Myers Squibb Co. in New York reported that his IT spending will remain level only because his company installed Y2K-compliant software in 1999. Bristol-Myers installed SAP AG's R/3 enterprise resource planning software and Ariba e-commerce applications, which saved a lot of money. Cooper said that technology initiatives in 2001 will focus on productivity issues, including supply-chain management and business-to-business e-commerce. He added that his shop is also planning to equip the Bristol-Myers sales and marketing force with more laptops and wireless communications devices and to implement video streaming.

2. Buyer Skepticism

Macroeconomic concerns have left many corporate leaders wary of overspending on IT, Phillips added. In fact, 12% of the CIOs who responded to the survey reported that they recently downsized their IT budgets because of the slowing economy. Tom Millikin, a spokesman for Procter & Gamble Co. in Cincinnati, said the company's IT budget has been growing moderately but is expected to change dramatically in 2001. Expenditures for infrastructure, for example, will level off or decline, while spending on Web-based applications will increase. He added that, "Also, most organizations have an insatiable appetite for bandwidth, and we're no different. We'll continue to invest in bandwidth around the world."

Data from a variety of sources regarding commercial user buying intentions suggest that they remain very much interested in e-business, e-commerce and electronic marketplaces, along with wireless "m-commerce," they are afraid of making commitments in advance of industry standards and indications of strong customer demand.

A recent survey conducted by the trade publication INFOWorld to measure commercial user attitudes toward IT outsourcing yielded many confirmations from 100 respondents of prior INPUT surveys, along with a few surprises.

Preliminary conclusions by INFOWorld were as follows:

- Most companies currently outsource one or more IT functions; they are satisfied with the results, and they will continue to outsource IT responsibilities in the future.

- Companies are outsourcing not just a chosen few IT functions, but the whole gamut. In addition to application development, software maintenance, and Web site hosting, companies are putting e-commerce applications, ERP (enterprise resource planning), network management, help desk services, and even security in the hands of service providers.

- Among the dozen, or so, IT functions that survey respondents' companies would consider outsourcing, only help desk and ERP services showed signs of increasing popularity. Although 10% and 12% of surveyed readers are currently outsourcing help desk and ERP services, respectively, nearly twice as many would consider outsourcing them in the future.

- Taken as a whole, respondents indicated that they wouldn't outsource anything tomorrow that they weren't already outsourcing today.

- Nor do they expect to increase spending on outsourcing in the near term. Although nearly one-third of respondents didn't know how much their companies spent on outsourcing, about half of the rest expected outsourcing costs to make up 30%, or less, of their company's total IT budget, both currently and during the next 12 months.

Even though one of the traditional motives for outsourcing has been to draw on expertise outside the company, few respondents cited a lack of internal expertise as a chief reason for outsourcing. By the same token, nearly half of the respondents whose companies are not outsourcing IT functions indicated sufficient equipment and staff for keeping IT functions in-house.

The key reason stated most often for outsourcing IT, cited by nearly 60% of InfoWorld respondents, was a lack of IT staff. In most cases it seems outsourcing allows the company to redeploy IT resources for higher-priority work. *In other words, it's not a shortage of skills, but a shortage of bodies that is steering IT executives toward service providers.*

- Some anomalies: Although saving money was often cited as a key reason for outsourcing, most respondents were unaware of how much their companies are saving; 12% were aware of no cost-savings at all.

Despite the wide variety of IT functions these companies are outsourcing, no respondents said that they were planning to outsource wireless services—despite the heavy burden that e-commerce and the global network place on corporate security capabilities, and only 20% of respondents plan to outsource security services.

INPUT would draw some additional conclusions from the data:

- In the near future, many companies will increase their dependence on IT outsourcers from necessity rather than enthusiasm. The 23% of respondents that are not outsourcing any IT functions today, and the 22% that anticipate no such outsourcing in the future are unlikely to win awards for forecasting.

- If 59% of respondents say that they are outsourcing due to staff shortage, and 48% are not outsourcing because they have adequate in-house resources, there appears to be a huge gap between *haves* and *have nots* on this point—and one that is likely to diminish as a convergence of trends favor an increased use of outsourcing, even by companies with large internal IT departments.

- Worth noting, already a quarter of all decisions on outsourcing are being made by non-IT department managers, probably in consultation with top management, which suggests that INFOWorld survey respondents as a group may become increasingly side-lined in the decision-making process.

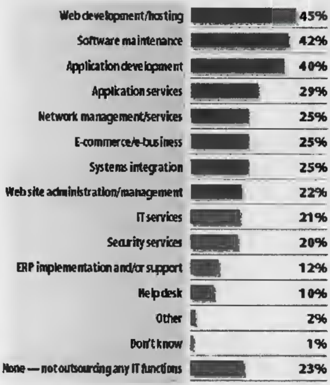
- Similarly, respondent comments regarding budget are likely to be understated because a growing amount of spending for IT outsourcing will be funded outside of the traditional IT budget. The more critical numbers is the proportion of total revenues that is being spent on IT and on IT outsourcing. As the transformation to e-business continues, the "IT budget" will comprise primarily infrastructure and special-project spending. Large amounts of "other" spending by and for operational units will be considered part of ordinary overhead rather than "IT."

Exhibit III-1 to Exhibit III-9, which follow, document INFOWorld's findings.

Exhibit III-1

Current User Environment

Which IT functions is your company currently outsourcing all or part of?



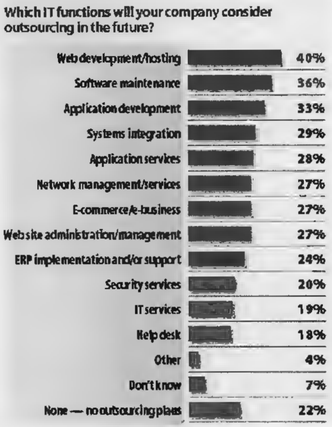
Source: INFOWORLD, February 12, 2001

- The high level of outsourcing recorded for application development and application services corroborates the demonstrated demand for the ASP delivery model.

- At the same time, in an attempt both to raise profit margins and better meet customer needs, there is a strong trend toward bundling several of these services into a single contract awarded to a single vendor.

Exhibit III-2

Future User Plans

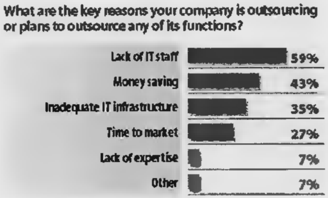


Source: INFOWORLD, February 12, 2001

- Comparing this set of responses to the prior one, one might conclude that customers anticipate little more than an extension of current trends, with no change in priorities.
- However, worth noting, virtually every category of service shows a rising trend in favor of increased outsourcing in the future.

Exhibit III-3

User Motives for Outsourcing

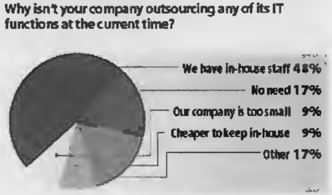


Source: INFOWORLD, February 12, 2001

- If so, a successful IT vendor's must be able to convince prospective customers that it has depth of technical staff, ample hardware and network infrastructure, and demonstrated ability to deliver promised solutions as promised on time.

Exhibit III-4

User Reasons NOT to Outsource

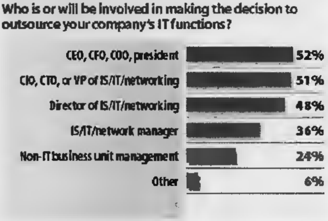


Source: INFOWORLD, February 12, 2001

- The first defense, or objection to outsourcing, listed above will be the first to crumble. When it does, customer resistance to outsourcing will vanish.

Exhibit III-5

User Decision-Making Process for Outsourcing

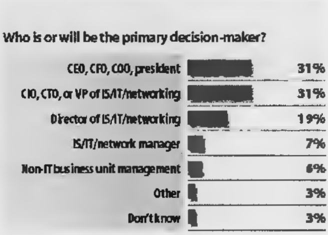


Source: INFOWORLD, February 12, 2001

- The importance of these responses cannot be overestimated. As outsourcing decisions are made at increasingly higher levels, vendors must be able to rise to the challenge of being able to present themselves, not merely as providers of technical solutions, but potential, long-term strategic partners of top management, sharing responsibility for developing the company's strategic plan.

Exhibit III-6

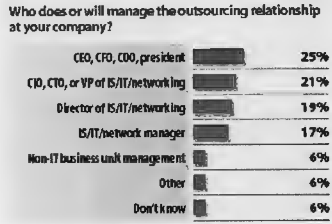
User Decision-Maker



Source: INFOWORLD, February 12, 2001

Exhibit III-7

User Outsourcing Relationship Management

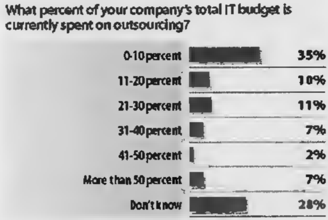


Source: INFOWORLD, February 12, 2001

- These responses suggest a natural attempt by top company management to offload daily project management on lower-level executives. Nevertheless, it is worth noting that the CEO remains the person most likely to manage outsourcing relationships on a continuing basis.

Exhibit III-8

User IT Outsourcing Budget



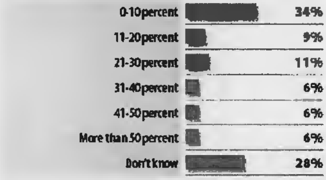
Source: INFOWORLD, February 12, 2001

- The validity of these answers is obscured by the extent to which sending for various types of outsourced IT services is being funded outside of the traditional IT budget.

Exhibit III-9

User Budget Expectations for Outsourcing

During the next 12 months, what percent of your company's total IT budget will be spent on outsourcing?



Source: INFOWORLD, February 12, 2001

- The gap between the first and third response likely reflects the differing situations at very large enterprises and smaller ones. Larger companies may spend smaller percentages of their budgets on outsourcing, but the nominal amounts will be much higher than at smaller firms.

- Nevertheless, it is worth noting that, consistent with INPUT's believe that the transition from traditional business to e-business will track a dramatic increase in the size of the IT budget in proportion to revenues, about 25% of respondents expect outsourcing to comprise 20-50% of their IT budgets, which suggests an extraordinary tactical shift in how businesses provide for their needs.

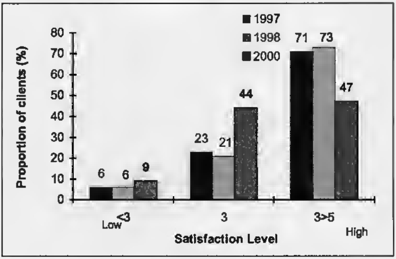
In contrast to INFOWorld's satisfied group of users, INPUT's proprietary surveys of outsourcing vendor performance over recent years discovered a significant erosion of satisfaction and a growing willingness to switch vendors when current contracts expire.

3. Overall Satisfaction with Outsourcing Declined Between 1997 and 2000

The overall profile of satisfaction exhibited by clients of outsourcing vendors in the U.S. remained roughly constant between 1997 and 1998, but has declined markedly between 1998 and 2000. Exhibit III-10 shows the profiles of overall satisfaction ratings given to outsourcing vendors in the U.S. between 1997 and 2000. Clients were asked to rate their overall satisfaction on a scale of 1 to 5 where 1 = very dissatisfied and 5 = very satisfied.

Exhibit III-10

Change in Client Satisfaction with Outsourcing: U.S. 1997 to 2000



Sample of 35 respondents *Source: INPUT*

In addition to their level of overall satisfaction, clients were asked the likelihood of their renewing contracts with their current supplier. There is frequently a lag between changes in levels of satisfaction and changes in renewal intentions with clients retaining a high level of loyalty for some time after a serious decline in satisfaction levels.

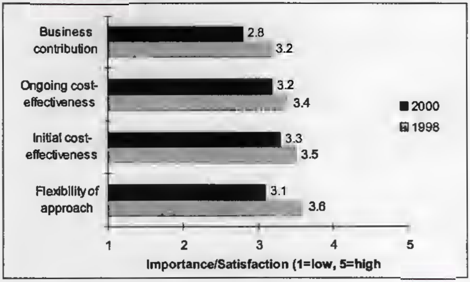
This appears to have happened in this case with 80% of clients still showing a high vendor loyalty. At present only 15% of clients are currently likely to switch outsourcing vendors on contract renewal.

However it is unlikely that these predicted low switching rates will be maintained in the coming years. It is probable that the decline in satisfaction levels will soon be followed by a marked decline in vendor loyalty. Vendors will need to deliver service improvements in many areas in the coming years if the predicted high renewal rates are to become a reality.

Exhibit III-11 lists some of the key summary criteria against which vendors need to deliver immediate improvement.

Exhibit III-11

Major Challenges for Outsourcing Vendors: U.S. 1998 to 2000



Sample of 35 respondents. Standard error = 0.2 *Source: INPUT*

The three principal themes in 2000 were the needs for vendors to deliver:

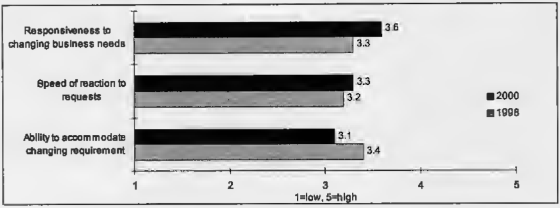
- Higher levels of client responsiveness
- Achievement of business benefits
- Improved value for money.

Vendors Must Deliver Higher Levels of Client Interaction

Exhibit III-12 lists the importance and satisfaction perceived by clients against a number of measures of vendor responsiveness.

Exhibit III-12

Satisfaction with Vendor Responsiveness: U.S. 1998 to 2000



Sample of 35 respondents. Standard error = 0.2 *Source: INPUT*

Clients perceive vendors' reactive service capabilities to have improved in some areas between 1998 and 2000. In some respects, vendors seem to have become flexible contractually.

However, there is a perception that despite this increased willingness, it is becoming more difficult for vendors to respond. The reasons for this situation principally seem to be the sheer rate of business and technology change prompted by e-business, resulting in:

- Greater difficulty for vendors in understanding their clients' businesses and the new competitive pressures faced. Vendor personnel who had achieved some level of understanding of clients' business processes are now seen to be increasingly out-of-touch with the new business reality

- Change management processes that are inappropriate in times of rapid change. The formal planning sessions followed by formal consultancy studies that have been established by many outsourcing vendors to manage change control may be too slow-moving for the new economy. In the new economy, exchanges of information between client and vendor may need to be much more frequent and informal if the client is to respond rapidly to changes in the business environment.

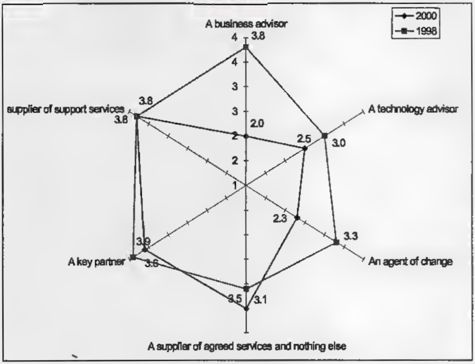
The net impact of these factors may be a perceived lack of ability to respond that is frustrating for both parties.

4. Vendors Need to Regain the High Ground

Exhibit III-13 lists U.S. clients' overall perception of the role of outsourcing vendors.

Exhibit III-13

Perceived Roles of Outsourcing Vendors: U.S. 1998 and 2000



Sample of 35 respondents. Standard error = 0.2 *Source: INPUT*

Vendors are to some extent still regarded as key partners by their clients. However the nature of this partnership is becoming a supporting one rather than a strategic one. Clients are increasingly regarding outsourcing vendors as organizations that supply agreed support services on demand rather as change agents. Clients, no longer, typically expect outsourcing vendors to behave as:

- Business advisors
- Technology advisors
- Agents of change.

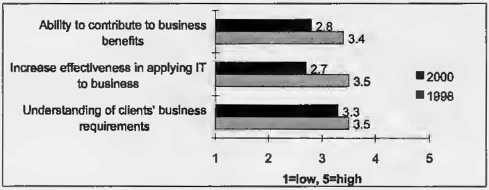
However, this is a dangerous change in the role of outsourcing vendors from the vendor perspective. To continue to strengthen the sense of partnership with their clients, outsourcing vendors need to be seen either as key technology advisors and implementers or as business advisors and business change agents. Unless outsourcing vendors can begin to deliver the levels of technical and business innovation required by their clients, there is a danger that they will become just commodity suppliers of support services.

Although the skills of many outsourcing vendors are primarily technical, it is important that vendors can use their skills to deliver business benefit on behalf of their clients.

Exhibit III-14 shows vendor performance against selected measures of delivery of business benefit.

Exhibit III-14

Delivery of Business Benefit: U.S. 1998 and 2000



Sample of 35 respondents. Standard error = 0.2 *Source: INPUT*

The typical levels of achievement in this area remain low and have deteriorated further between 1998 and 2000.

Vendors' understanding of clients' business requirements has deteriorated and this has severely impacted their ability to contribute to their clients' business success.

However, it is unlikely that vendor performance has deteriorated over the past two years. The principal factors likely to be causing this change in perception are the rapid changes in technology and the business environment.

As organizations seek to redefine themselves in the new economy so it has become more difficult for vendors to keep up with industry and individual strategies and contribute to these in a timely fashion.

If vendors are to make a contribution to their clients in times of rapid change, then they will have to take steps to:

- Track industry and technology developments more closely
- Work more informally and closely with their clients
- Put in fast reaction mechanisms that allow them to react quickly to identified changing needs.

5. Improved Value for Money Remains Important

A traditional disadvantage of outsourcing is that it can potentially slow-down the rate at which new systems and technologies are introduced. This effect has in the past been caused by contractual style and pricing mechanisms, irrespective of vendor capabilities.

However, it appears that man vendors have now addressed the issue of lack of flexibility in contractual approach. The issue is now one of expectation management and delivery of value for money.

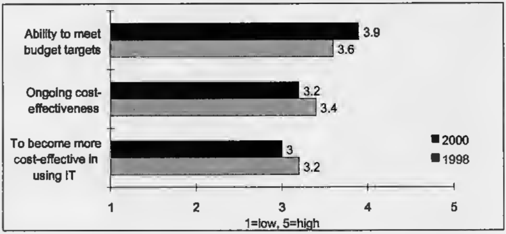
Clients expect a reducing cost for support of existing systems and infrastructure over time. These cost reductions do not always manifest themselves as strongly as clients expect and, as a result clients are increasingly critical of vendors' abilities to meet budget targets and deliver ongoing cost reduction. It is also a question of approach. Clients expect vendors to pay the same level of attention to cost management on their behalf as would be taken by in-house management. Accordingly, vendor personnel need to constantly seeking ways of saving money for their clients and recommending cost-reduction strategies to them. Again, these cost reduction strategies should not necessarily result from major formal, chargeable studies, but should also arise at a more incremental and informal level.

At the same time, the level of change that can arise as a result of e-business initiatives can have a huge impact on existing expenditure plans. Therefore, it is important that vendors manage expectations accordingly and seek other areas in which savings can be made.

Exhibit III-15 lists the levels of satisfaction from the client perspective against a number of cost-control criteria.

Exhibit III-15

Satisfaction with Vendor Cost Control: U.S. 1998 and 2000



Sample of 35 respondents. Standard error = 0.2 *Source: INPUT*

Cost control and/or reduction and delivery of business benefit are not viewed by clients as mutually exclusive. Clients would like outsourcing vendors to be more proactive but, at the same time, to supply the basic services underlying such activity at competitive rates. Clients are more likely to favor forms of risk sharing where the vendor takes the risk of falling workloads, than forms of risk sharing that merely enhance vendor profitability.

Clients also frequently perceive that they receive poor value for money from any changes in operational service volumes. They perceive that they are expected to pay additional charges when volumes increase but do not receive a proportionate decrease in charges when transaction volumes decrease.

Overall clients:

- Dislike pricing mechanisms such as time and materials that allocate the major elements of risk to the client rather than the vendor. This particularly applies to systems development contracts where clients perceive themselves to carry the bulk of the burden of commercial risk

- Would like to encourage greater vendor creativity but with the vendor taking a major share of the risk.

In particular, clients would like greater flexibility in service usage with considerable flexibility to adjust the volume of services used according to their business requirement and circumstances. In extreme cases, this could entail turning services on and off at short notice with the vendor taking the commercial risk over whether the services are utilized or not.

Overall there is an increasing tendency for clients to insist on value for money throughout the life of outsourcing contracts. Some clients are ensuring that they achieve this by developing contracts that permit them to benchmark vendor pricing throughout the contract. This will place greater margin pressure on vendors by making it more difficult for them to significantly increase their profitability in the later stages of the contract.

Ideally, clients would like vendors to behave as though they owned the client IT budget and continually seek out ways in which IT services can be delivered within a set budget and at increased value for money. Clients tend to disapprove as vendors who are continually trying to increase IT expenditure at the clients' expense, regardless of the worthiness of the projects and services themselves.

Vendors need to take a more holistic view on behalf of their clients and this includes both the achievement of business benefit and the management of the IT budget. At the moment, there is a danger that vendors are merely responding to requests for individual projects and services from the client without taking this overall perspective of effectiveness and value for money into account.

IV

Barriers to Entry

A
Lack of Name Recognition

Beyond the obvious drawbacks associated with lacking name recognition in a new market, vendors everywhere face the challenge of differentiating themselves from competitors.

In the Executive Summary to this report, survey respondents propose in brief (and in the Appendix in full) a few consensus remedies, including:

- Partnering with established vendors that have already respected positions in a target vertical industry;
- Utilizing industry consultants to establish new customer relationships;
- Attempting to specialize in horizontal applications where expertise in the application, such as ERP or HR, will be more important than the vertical industry expertise.

Another tactic is to play the "name game," whereby vendors attempt to create name recognition by dominating ever-narrower and more obscure market segments, such as those that follow—based on a compilation published in *InformationWeek*:

- **Application Service Providers**: ASPs use centrally managed facilities to deploy, host, and manage access to packaged applications, which are delivered over networks on a subscription basis. Currently, there are between 500-1,000 vendors in this category. Few are profitable; stronger vendors are attempting to survive by acquisition, specialization and increasing their consulting/customization services.
    - Vendors include Corio, Interliant, Qwest Cyber.Solutions, and USinternetworking.

- Pricing depends on application type and add-on services. Corio, for example, charges $70-100 per user per month to host ChangePoint's professional services application.

- **Management Service Providers**: MSPs manage combinations of applications, networks, systems, storage, and security, and also can provide, by subscription, Web-site and systems-performance monitoring via the Internet. Vendors in this niche are generally considered to be low-margin plays whose role is limited to monitoring the work of either in-house, or other outsourcing vendors. Their role is a difficult one because it requires cooperation among a variety of organizations, often incurring conflicts of interest.

  - Vendors include Nuclio, Silverback Technologies, SiteRock, Totality, and Triactive.

  - Monthly MSP charges vary from a few thousand dollars to more than $100,000.

- **Storage Service Providers**: SSPs offer hosting and access to storage devices and storage area network technology. Vendors in this market appear to be tapping into a rich demand that is linked to e-commerce, which generated huge numbers of transactions (for which customers have run out of storage). Upmarket vendors are combining storage offers with data-mining and other knowledge management services.

  - Vendors include Comdisco, Compaq Global Services, IBM Global Services, StorageNetworks, and Storability.

  - The price of Compaq's Private Storage Utility service is $35 to $55 per gigabyte per month; pricing for IBM's On-Demand storage services ranges from $25 to $75 per gigabyte per month.

- **Business Continuity Service Providers**: These providers define and document procedures for assessing, responding to, and recovering from events-application errors or natural disasters-that threaten vital business operations. While vendors in this market are building on a long-accepted need, the virtual nature of emerging e-businesses brings a new urgency to the market and provides a large, new pool of potential customers.

  - Vendors include Comdisco, Compaq Global Services, EDS, IBM Global Services, and SiteSmith.

- Comdisco's disaster recovery, rapid recovery, and continuous Web-availability services range from $10,000 to $100,000 per month.

- **Help Desk/Customer Service Providers**: These companies handle E-mail and telephone calls pertaining to desktop applications, computer security, and passwords. As the volume and importance of integrated electronic communications rises exponentially, customers are losing the ability to cope with the volume and complexity of coping with client communications. Service providers in this niche market have a very positive growth potential.

  - Vendors include CompuCom Systems, IHS Helpdesk Service, Service Management International, and Stream International.

  - CompuCom charges $18 to $35 per call, depending on coverage, which ranges from five days per week to around-the-clock service.

- **Corporate/IT Training, HR, and Recruitment Service Providers**: These companies let businesses outsource finance, accounting, HR, training, and recruiting functions.

  - Vendors include Caliber Learning Network for training, *Ledgent for HR, and Recruitsoft .com for recruiting.*

  - *Caliber's hosted E-learning services average about $2,000 per hour per user.*

B
Insufficient Capital

Putting aside the obvious advantages enjoyed by the top-tier IT vendors with virtually unlimited financial resources, vendors and customers both agree that smaller vendors with limited resources can achieve credibility in new markets by adhering to a few basic principles, as follows:

- Avoid trying to overextend or oversell yourself. The primary virtue is identifying core competencies and being able to deliver on all promises made.

- Leverage insofar as possible you prior work by using contacts and expertise gained in that market to gain a foothold in new, related markets.

- Target your marketing and sales efforts according to a rational geographical and industry strategy. Unplanned efforts will be wasteful of time and money and jeopardize success at every level.

- Remember that customers, whether large or small, are almost always ready to believe that the top-tier vendors have high levels of overhead and are growing complacent. Customers are usually always ready to listen to a focussed presentation by a lean and aggressive competitor.

- Apart from either purchasing or building data centers, most other forms of outsourcing contract services can be provided relatively inexpensively on either a remote or customer-site basis.

- While there is a trend toward vendors buying software licenses (and therefore investing their own capital in them), most large customers will prefer to purchase software licenses directly. Although they do want to avoid the headaches associated with hardware purchases and technology refreshes, they expect vendors to build these functions into their contracts in such as way as to optimize, rather than replace customer capital investments.

C
Staffing

The cost of acquiring and retaining skilled IT staffs that transfer from customers to vendors as part of an outsourcing contract seldom incur burdensome costs on vendors. Most consider this process to be one of the collateral benefits of outsourcing.

Typically, the promise transferred staff two years of employment, on terms equal or better than those at their former employers. Many employees are scarcely aware of the transfer at all when they continue working in the same offices with the same colleagues.

Over a period of time, the vendor challenge is to identify, retain and promote the most capable individuals and terminate those for whom they have no place. If this process is handled intelligently and with skill, it can reinforce a vendor's market position.

In particular, customers favor vendors with attractive market reputations such that potential staff transfers are enthusiastic about their potential for career advancement with the outsourcer. Vendors unable to achieve a positive reputation or effect smooth transfers put their entire customer relationships in jeopardy.

Some vendors have commented that it is easiest to utilize staff efficiently when using a matrix organization whereby staff assignments are made flexibly and efficiently independently of business unit or vertical industry. However, success with this approach depends on mangers being alert and flexible enough to make assignments intelligently. The system can lead to idle, underutilized staff.

Vendors such as CSC believe strongly that they have prospered because they have been able to retain and promote a large number of highly qualified individuals that joined the company through transfers from customer outsourcing contracts. To make this work requires a commitment from the highest levels of the organization and a management structure that rewards performance more than seniority—which is easier described than achieved.

V

IT Outsourcing Market Overview

A
Market Trends

1. The Operational Services Market Is Splitting Up

The U.S. market for operational services is splitting along two tracks—traditional, legacy services and Internet-centric services. In last year's outsourcing market forecast, INPUT included "Internet/intranet management" as a single, functional segment. This year, virtually every functional segment has been split and forecasts provided for each separately.

Although the year-over-year growth of the Internet-centric segments is forecast to remain high over the next few years, before the end of the forecast period, a convergence will begin that signals the effective disappearance of a non-Internet-enabled legacy IT infrastructure. At that point, the Internet will be so thoroughly integrated in to business processes and operations that all operational services will take it into account.

Accordingly, the decline in mainframe platform operations services that would otherwise have been expected will be reverse itself as the demands of e-commerce and the requirements for massive data storage for e-business give mainframes new importance.

Currently, applications services are separated into three streams—(1) those required by traditional enterprises for their own licensed software (or customized software to be purchased on a license basis). (2) applications purchased on an outsourced basis directly from software developers, and (3) applications provided to value-added resellers (Application Service Providers) of various types that make them available on a pay-as-you-go basis.

The last two market segments will grow rapidly over the next few years, but before the end of the forecast period INPUT foresees much of today's business in this market falling into the Business Process Operations and Processing Services categories. They key criterion will be the extent and nature of the responsibility assumed by vendors for their customers.

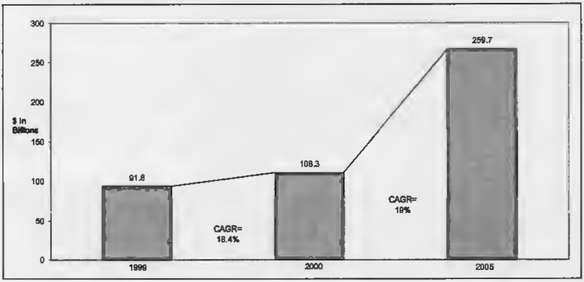
2. Similarly To the Outsourcing Market, The Fastest-Growing Segments of the Processing Services Will Be Internet-Centric Ones

Yet, before the end of the forecast period, they will begin to converge with the heretofore designated "legacy," or traditional segments of the market as the Internet is used ever more widely and as the transformation of enterprises to e-business (and e-government) continues. Eventually, the distinction between the two streams (Internet-centric and legacy) will lose relevance.

INPUT's overall forecast for the U.S. operational services and BPO market is shown in Exhibit V-1.

Exhibit V-1

U.S. Operational Services Market, including Business Process Operations



Source: INPUT

This forecast includes IT outsourcing, Business Process Operations outsourcing, and transaction processing.

Over the last few years, Business Process Operations (BPO) has become increasingly accepted by a wide variety of companies in various industries. Over the period, 2000-2005, INPUT forecasts a long-term growth rate of 29% for a market expected to grow during the period from $12.5 billion to $45 billion.

B
Market Drivers

1. "More and More Customers Were Telling Us, 'We Don't Want to Deal with the Technology, You Handle It. Make This Stuff Work for Us'"

This comment by Hill Husted, VP for Web-hosting at PSINet, exemplifies the driving force behind both the growth in demand for operational services in general, and the heightened pace of merger & acquisition activity during the past year. Computer equipment vendors want to increase their diversification away from hardware toward services, and vendors of services want to expand their capabilities so that they can increase their account penetration, *i.e.*, give customers less reason to look elsewhere for business and technology solutions.

This was one motive behind Cap Gemini's May 2000 acquisition of the consulting unit of Ernst & Young—Ernst & Young Consulting in a deal worth 11.3 billion euros. The sale was motivated partly by the American Securities & Exchange Commission's insistence that public accounting firms eliminate potential conflicts of interest caused by selling both auditing and consulting services (particularly to the same clients). For the same reason, PricewaterhouseCoopers may sell its consulting business to Hewlett-Packard. KPMG elected to spin off its consulting operations as an independent enterprise and, for similar reasons, Andersen Consulting split from Arthur Andersen. But it was also motivated by CG's need to be able to offer its clients increasingly more comprehensive business solutions rather than narrow technical ones.

This was also the partial motive behind HP's September 11, 2000, confirmation that it was a leading contender to acquire the consulting arm of PricewaterhouseCoopers in an $18 billion deal. If realized, the transaction would substantially reinforce HP's services offer and make it much more attractive to corporate clients that are considering the purchase of big computer systems. The challenge: combining HP's tradition-oriented workforce with PwC's innovators.

2. The Battle to Become King of the Web Hosts

"If you think about it, anytime anybody accesses the Internet, that has to come from a server somewhere," commented Bobby Patrick, VP of strategy for Web-hosting heavyweight Digex as a way of explaining why his company foresees outstanding growth and profitability potential for this market segment. INPUT forecasts that the global Web-hosting segment of the e-business, Network Services market will grow from $11 billion in 2000 to $35 billion in 2005. Of this, INPUT estimates that the

U.S. represents 80% in 2000 ($8.8 billion), declining to 60% in 2005 ($21 billion). Furthermore, the time is rapidly ending when almost any large organization with excess capacity at its data centers can hope to operate a Web-hosting business profitably. Profit margins at the low-end of the business (*i.e.*, without value-added services) will be progressively squeezed. On the other hand, demand for (and the profitability of) selling a variety of value-added services along with plain Web-hosting appears to have no visible ceiling. This is why another industry executive insisted that "hosting is a way to deliver higher revenue per customer than the Internet services can make simply from hooking businesses up to the Net. Hosting is like peanut butter AND jelly."

This rosy outlook should, however, be contrasted to the ugly present: virtually none of the major Web-hosting vendors is yet profitable due, primarily, to low prices resulting from excess capacity. MCIWorldCom's UUNet unit, the largest Internet carrier, is not profitable, even though it does produce a spin-off, or halo effect that enhances the profitability of other parent businesses.

But the battle for market dominance will not be pretty.

PSINet, which operates a global Internet network, acquired IT services provider Metamor by paying $1.9 billion, which represented a significant premium to its stock price at the time. PSINet's strategy is to become an "Internet supercarrier" able to offer its clients increasingly more comprehensive packages of technical services. Post-merger, PSINet's strength will extend beyond infrastructure and hosting services, creating the potential for it to become a prominent provider of applications. This could position it to become a true ASP with hosting facilities, applications, and services—which will only ratchet upward the pressure on MCIWorldCom and the other large competitors in the attractive Web-hosting market.

3. Buyers Show Growing Skepticism

Demand for IT outsourcing and processing services will continue to be strong, but competition is becoming more intense (and exacerbated by active merger & acquisition activity). At the same time, buyers are increasingly skeptical of overly optimistic vendor claims. Also, buyers are looking more carefully at vendors' financial viability. The highly publicized financial difficulties of numerous well known Web consultants and Internet integrators—climaxing with the demise of Pandesic—have clearly benefited the established, traditional service providers. While the demise of Inacom in June 2000 did little to affect the competitive structure of the operational services market as a whole, it did contribute to undermining customer confidence in outsourcing vendors as a whole.

Once customers are convinced to trust a vendor to deliver critical services, they feel particularly betrayed when they are abandoned unexpectedly and left to pick up the pieces—which can be both costly and risky.

C

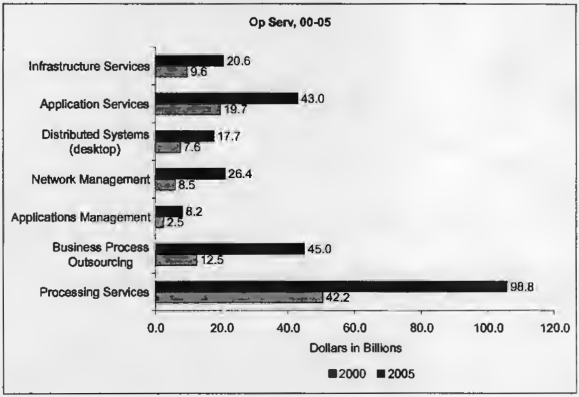
Five-Year Outlook for the U.S. IT Outsourcing Market

1. Industry Sector Forecast

Exhibit V-2 summarizes INPUT's 2000-2005 forecast for the U.S. operational services market by functional segment.

Exhibit V-2

Operational Services Segments, U.S. - 2000-2005

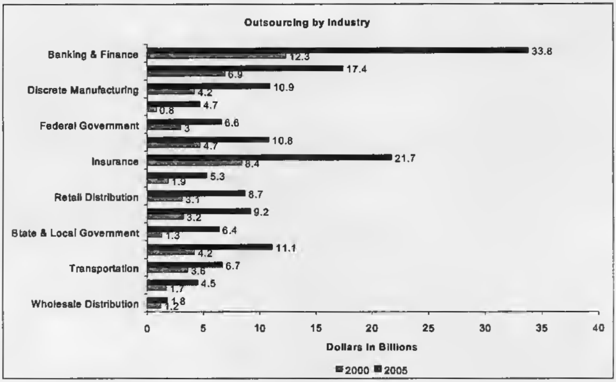


Source: INPUT

Exhibit V-3 provides a forecast for the US operational services and outsourcing market by industry sector. The forecasts shown in this exhibit include Business Process Operations in addition to IT outsourcing.

Exhibit V-3

US Outsourcing Industry Sector Forecast, 2000-2005



Source: INPUT

"Infrastructure Services" is being used for the first time in this forecast report as a replacement for the prior term "Platform Operations," which becomes one of two components of the Infrastructure Services market. This market has been divided this year into traditional, mainframe-oriented platform operations and the faster-growing, "Internet/Web Managed Services" sub-segment. The inflection point between these two market segments will occur in 2005, at which time Internet/Web Managed Services segment is expected to be larger than the legacy IT Platform Operations segment. Toward the end of the forecast period, a price/performance curve effect will result in lower levels of spending/purchasing and ever higher levels of performance. This segment includes Internet Data Centers operating on long-term contracts. The high forecast rate of growth for the Internet sub-segment will peak during the 2000-2005 period. At the end of the period, the two segments will begin to merge again as all IT infrastructures become totally integrate with the Internet and the distinction between the two segments loses importance.

"IT Application Services" include legacy IT applications that may, or may not include Internet-enabled functions. In the future, virtually all applications will be Internet-enabled. As with Platform Operations, toward the end of the forecast period the distinction between "legacy" and "Internet/Web" applications will become moot; at a certain point, the Internet will become the legacy.

"Internet/Web Applications Service – vendor-owned software" comprises software sold on either a license or pay-as-you-go rental basis by software developers directly to users. While INPUT foresees rapid growth in this sub-segment, exemplified by Oracle, software developers are unlikely to want to depend entirely on direct sales, even when delivered cost-effectively over the Internet. Proliferating demands for ancillary services are likely to dissuade them from foregoing the participation of channel partners and Value-Added Resellers (VARs). As a result, INPUT foresees a moderation in the rate of growth of this market segment by the end of the forecast period as many vendors return to their core competencies. Increasingly, this market will become dominated by the simple delivery of package products, such as Microsoft's proposed direct delivery of its Office Suite of applications on a rental basis directly to consumers. Businesses tbat are unable or unwilling to use one-size-fits-all package software and that require customization will return to VARs and/or traditional systems integrators.

The "Internet/Web Applications Services – Third-party software (ASP)" sub-segment will continue to experience rapid growth over coming years, but this growth will moderate toward the end of tbe forecast period for several reasons: competitive pressures will force many so-called ASPs to specialize. As they do, much of their business will be more properly classified as Business Process Outsourcing or processing services. As price competition becomes intense, this market will divide clearly into low-margin, high-volume commodity software distributors and higher-margin, higher value-added resellers.

INPUT forecasts a strong CAGR of 19% in the Distributed Systems segment, which subsumes the prior category of "Desktop Services." Due to rapid changes in technology underway, the "desktop" is becoming mobile. As it loses its fixed location, spending in this segment will be fueled by the urgent need for outsourced management of a wide array of portable computing and Internet-enabled band-beld devices. Future INPUT forecasts will provide estimates of market size for the most important of these types of portable desktops.

The "IT Network Management" of the Network Management market includes both legacy and Internet-related components. This segment will be heavily affected by the transformation underway among large telecom vendors. Price points will drop, pricing will become critically important; toward the end of the forecast period, this segment will merge with the "Internet Network Management" segment.

Processing services differ from outsourcing services primary on the basis of contract tenure (outsourcing contracts are for one, or more, years) and by level of responsibility: processing vendors take no responsibility for the customer's software application or business process.

E-commerce and the proliferation of a wide variety of electronic exchanges will fuel growth of vendors of processing services in the Applications Services market. Utility and other commodity processing services will grow more slowly, partly as a result of unfavorable pricing and partly as a result of technological changes that render some of the services that utility processors perform obsolete.

"Input/output storage services" include print/scan, CD-ROM and Storage Area Network services. These are forecast to grow somewhat more slowly than the higher value-added segments of the market.

"Other" processing includes performance monitoring, security services, authentication and related services.

The legacy utility processing services market will shrink due to the growing dominance of Internet-enabled applications.

2. Infrastructure Operations Decline To Be Offset by Demand for Internet-Managed Services for E-Commerce

The growth rate of the Infrastructure Operations segment comprises the slow-growth IT (Platform) Operations segment, with a CAGR of only 1% over the period 2000-2005, and the fast-growing Internet Managed Services segment, with a CAGR of 68% over the same period.

Nevertheless, this sector had been the second largest, accounting for 24% of the outsourcing market in 1996, 22% in 1997 and 19% in 1998, slipping to only a forecast of 13% in 2005. INPUT projects that this market will grow at a CAGR of 17% between 2000-2005, increasing from $9.6 billion in 2000 to $20.7 billion in 2005.

3. Distributed Systems (including Desktop Services) To Be Transformed

The U.S. Distributed Systems (desktop services) market reached $6.1 billion in 1999 and will rise to an estimated $7.6 billion in 2000. INPUT forecasts that it will grow to $17.7 billion in 2005, representing a CAGR of 19% over the five-year period ending in 2005.

In the past, desktop services came to be regarded as a "commodity" suitable for "body shop" vendors (who staff their operations with indistinguishable "bodies"). As prices for desktop services fell, large, high-overhead vendors ceded the field to smaller, specialized vendors—except in those cases where desktop services could be bundled together with other, more lucrative services. Accordingly, market growth would be expected to fall as a reflection of lower prices.

Although demand for desktop services outsourcing benefited from the long-term migration of organizations from centralized computing architectures and away from mainframes, that trend is largely a spent force. Falling hardware prices and an increasingly competitive environment for desktop services drove down the attractiveness of this market. However, INPUT believes that this downward trend is being reversed as wireless computing and other Internet appliances proliferate among businesses.

Over the next five years, companies that find themselves burdened with the management of a large number of portable, laptop computers, handheld and other wireless devices will turn back to vendors of "desktop." Their domain will have expanded from the tangible, wired desktop to the virtual desktop—resulting in a transformation of this market segment into a more complex (and profitable) one.

4. Network Management Divides into Slow-growing Traditional and Fast-growing Internet-related Segments

Reflecting the transformation underway from traditional to e-business methods of operation, large amounts of money are being spent on upgrading legacy IT networks to the demands of Internet-enabled transactions.

While the Network Management market overall is forecast to grow at a CAGR of 25% between the period 2000-2005—faster than the 19% CAGR forecast for Operational Services as a whole.

The legacy IT segment is forecast to grow by 18% compared to 57% for the Internet segment. The total size of the Network Management market is forecast to reach $26.4 billion by 2005, by which time year-over-year growth in the Internet segment will moderate. After 2003, the distinction between these two segments will decline in importance to the extent that the transformation of legacy systems will be largely complete.

5. Application Management Undergoing Rapid Shift as Transformation to E-Business Advances

The market for Applications Management outsourcing will reach an estimated $2.5 billion by year-end 2000 and is forecast to reach $8.2 billion in 2005.

As was the case with Network Management, the Applications Management outsourcing market comprises the slower-growing, legacy IT applications segment and the faster-growing Internet/Web Applications segment—a CAGR of 23% for the former compared to 49% for the latter between 2000 and 2005.

Overall, user spending is undergoing a significant shift away from Infrastructure Operations toward Application Management and Network Services, if budgets are assumed to comprise these three broad categories.

By 2005, INPUT believes that the bulk of spending under the IT budgets of most enterprises will be allocated to applications, including both software licenses and application management services. At the same time, the greater amount of spending by far is being allocated to applications that enable enterprises to compete in the world of e-commerce (or e-government) as well as to advance their transformations to becoming e-businesses.

For the Applications Management market overall, the forecast Compounded Annual Growth Rate (CAGR) over the period 2000-2005 is 27% which is significantly higher than the outsourcing market as a whole (22%), and up from the estimated 20% growth that occurred between 1998 and 1999. However, it is also lower than the year-over-year growth between 1999 and 2000 of 29%.

6. Applications Services Flow into Three Distinct, New Streams

The Applications Services (formerly "Applications Operations") segment continues to dominate the U.S. outsourcing market, accounting for nearly 41% of the 2000 U.S. market. At the end of the forecast period, in 2005, that proportion is expected to decline slightly to 37%. In contrast, the Internet Applications Services segment, which includes the ASP market for remote delivery of third-party applications, will grow from 3% of the total Applications Operations market segment to 17% by 2005. Year-over-year growth of this segment will, however, moderate substantially from 85% between 1999 and 2000 and 130% between 2000 and 2001.

During the 2000-2005 forecast period, INPUT estimates that the traditional, legacy IT Applications segment of the Applications Services market will grow slowly at a CAGR of 11%. The Internet Applications Services stream that represents software delivered via the Internet directly by software developers, such as Oracle, PeopleSoft and SAP, will grow much faster at 47%.

However, this growth will moderate toward the end of the period as many developers abandon their direct distribution channels in favor of partnering with ASPs—which is already happening. Accordingly, the very high growth of the third-party software, or ASP, segment will moderate as the market matures and as vendor consolidation is largely completed.

Beyond that, INPUT believes that **the ASP segment** itself will increasingly split into some form of either Processing Services or Business Process Operations. Surviving ASP vendors will need to move either "downstream" toward high-volume, specialized transaction processing, or "upstream" into the BPO market in which Internet Applications Services are bundled with other value-added services in order to deliver comprehensive solutions.

By INPUT's definition, "Applications Services" denotes work done by vendors to manage and operate computers systems in order to perform client business functions, which includes maintaining (or developing and maintaining) client application systems.

In contrast, "Applications Management" work includes full responsibility for maintaining and upgrading some, or all, of a client's applications systems used to support business operations. Vendors doing this work often develop and implement new applications systems for clients. In both cases, the client mandate is not limited to discrete projects, but extends beyond 12 months in time and beyond single functions.

Currently, the distinctions are being obscured by Application Service Providers (ASPs) that may take responsibility for some maintenance and upgrading of applications along with computer system management. In other cases, they undertake only one of these functions.

ASPs and other (in effect) Value-Added Resellers of third-party software (*i.e.*, developed by a software developer unrelated to either the client or the service provider), offer a range of services, including:

- Hosting the client's application at a data center owned by the client;
- Hosting the client's application at a data center owned by the ASP;
- Hosting the client's application at a data center owned by another supplier;
- Providing clients with access to specific software applications, either over the Internet or via a VPN on a turnkey basis, *i.e.*, the ASP takes full responsibility for maintaining and upgrading the software.

Also important, a growing number of software developers are offering customer's access to their software on a hosted, pay-as-you-go rental basis rather than selling traditional licenses. Or, software developers may partner with ASPs—the developer taking responsibility for Application

Management and the ASP taking responsibility for Application Operations.

For the purpose of this forecast report, INPUT has segmented both outsourcing and processing services markets according to the nature of the relationship between the end-user and the vendor. Consequently, some ASP revenues fall in the Applications Operations management, some other categories. INPUT believes that the ASP, or software re-seller market, is undergoing a rapid transformation and consolidation. What will emerge within the next 24 months will be a smaller number of financially viable and tested vendors able to offer a range of flexible products. Many of those that contract with end-users on a monthly, pay-as-you go basis will be classified as vendors of processing services. Those that take complete responsibility for providing a package of software and services, on a multi-year contract basis, that constitutes fulfillment of a distinct business function will be classified as Business Process Outsourcing vendors.

Beyond that, vendors that find themselves under extreme competitive pressure in their initial market segments are re-inventing themselves as ASPs. For example, because most marketplaces generate revenues from transaction fees, low trading volume can foretell financial disaster. When some of the vertical industry partners of fledgling exchanges decide to set up their own exchanges, thereby causing disintermediation of the pioneer e-marketplaces, the disaster scenario can advance rapidly.

As a defense, some exchanges are seeking to rent their software to small and midsize companies that don't want to build their own e-business applications, or they license e-marketplaces to big companies that want to run private exchanges for their own suppliers.

7. Applications Services Market Splitting and Re-Splitting

Currently, this market segment—*Internet Application Services—Third-Party Software* - is under intense competitive and financial pressure. For example, ForRetail.com, a San Francisco-based marketplace for the home-furnishings and giftware industry, was recently forced to revise its business model. The company had signed up 400 manufacturers and 25,000 retailers, but lacked significant revenue from the 5% transaction fee that it charges vendors. When ForRetail sought a second round of funding in July, it learned that investors were no longer interested in funding B2B exchanges.

Another vendor, AviationX of Arlington, Virginia, dropped its exchange completely in favor of renting applications—it had planned to build an online marketplace for the aviation industry. In July, management announced that the company would be focusing solely on providing applications for buying and tracking spare airplane parts for regional airlines that can't afford to build their own e-procurement systems. Unfortunately, by the time this decision had been taken, the airlines themselves announced their own exchanges, specifically, a group led by Air Canada (ACNAF) , Lufthansa and Singapore Airlines and another backed by American, Delta and United Airlines. As a result, AviationX is working with three regional airlines, Mesaba of Minneapolis, Chautauqua of Indianapolis and Express Airlines I of Memphis, Tennessee, to develop software applications.

AviationX wasn't the only marketplace that found itself squeezed into an unexpected niche. E-Chemicals, an exchange launched in 1998 in Ann Arbor, Michigan, competed against a handful of similar chemical industry marketplaces, none of which was generating sufficient liquidity to survive independently. As a result, the company shifted its emphasis toward developing software that lets chemical buyers and suppliers move contractual relationships online. Now, e-Chemicals is in a good position to work alongside, rather than compete with, industry coalition marketplaces being built by several giant chemical companies and those marketplaces can get to market faster by partnering with e-Chemicals.

8. Internet-Application Services, Vendor-Owned Software

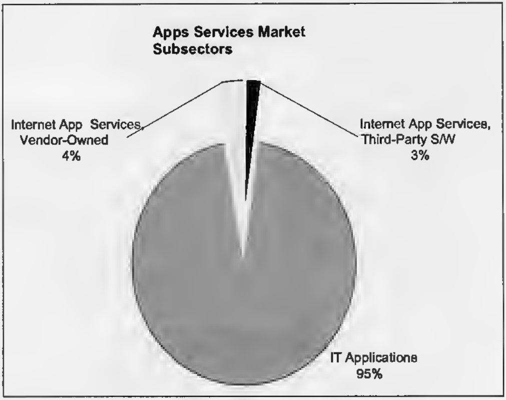
Competing with ASP vendors that re-sell third-party software (*i.e.*, not owned or developed by either the ASP or its customer) is a fast-growing list of software developers which are attempting to bypass re-sellers and offer their product directly to smaller end-users on a rental rather than license basis.

Some, like Oracle, have even proposed giving away software without charge. Oracle's customer relationship management (CRM) software has been trying to slow Siebel Systems' more rapid growth as well as demonstrate that Oracle is an innovative leader in the CRM market. The announcement of OracleSalesOnline.com, a free online sales automation system that is a part of the Oracle E-Business Suite 11i, was seen as an audacious move because no associated, identified revenue stream exists for the next 12 months. Yet, this initiative could help Oracle jumpstart its ASP business, or boost potential sales of Oracle *BackOffice*. Oracle expects to make money off of this free service in two ways. First, the company hopes the service will drive sales of its other e-business software, and secondly, it expects that it will eventually make money off of the fee-based services.

Exhibit V-4 portrays the relative sizes of the three, constituent components of the forecast Applications Services market for 2000.

Exhibit V-4

Relative Sizes of Forecast Applications Services Market, U.S. – 2000



Source: INPUT

9. Business Process Operations' Fast Growth Linked to Changing Business Models

The electronic business, electronic commerce-related stream of the BPO category is among the fastest growing segments of the outsourcing market, rising from $1.5 billion in 2000 to a projected $12.5 billion in 2005, representing a CAGR of 54%. In contrast, the Non-EB/EC-related stream of the BPO market is forecast to grow at a slower CAGR of 24%. The overall BPO market is expected to grow at CAGR of 29% from $12.5 billion in 2000 to $45 billion in 2005.

10. Vertical Industry Markets

Exhibit V-5 provides a forecast for the U.S. outsourcing market by industry sector over the period 2000-2005

This Operational Services forecast includes IT outsourcing, Transaction Processing and Business Process Operations outsourcing. The vertical industry breakout of this total market has been separated into two broad categories, outsourcing (including BPO) and processing services in order to better identify growth trends that differ by industry and type of operational service. Certain industries represent a significantly higher proportion of the total processing services market than they do of the outsourcing market.

Exhibit V-5

U.S. Outsourcing Market Forecast by Vertical Industry, 2000-2005

	US $m 1999	Growth 99-00	2000	Growth 00-05	2005
Total US Outsourcing Market Market (excl. BPO)					
	40,010	*19%*	**47,700**	*19%*	**115,900**
Banking & Finance	10,418	*18%*	12,341	*22%*	33,789
Business Services	6,006	*15%*	6,923	*20%*	17,377
Discrete Manufacturing	3,229	*32%*	4,274	*21%*	10,941
Education	741	*6%*	783	*43%*	4,666
Federal Government	2,481	*21%*	3,010	*17%*	6,597
Health Services	4,073	*17%*	4,756	*18%*	10,780
Insurance	6,945	*21%*	8,428	*21%*	21,641
Miscellaneous Industries	1,642	*17%*	1,926	*22%*	5,310
Process Manufacturing	2,406	*33%*	3,191	*24%*	9,171
Retail Distribution	2,253	*34%*	3,010	*24%*	8,689
State & Local Government	893	*45%*	1,294	*38%*	6,436
Telecommunications	3,616	*17%*	4,214	*21%*	11,102
Transportation	2,728	*13%*	3,070	*21%*	8,045
Utilities	1,355	*29%*	1,746	*21%*	4,505
Wholesale Distribution	893	*35%*	1,204	*9%*	1,834

Source: INPUT

11. Banking & Finance Industry Market, 2000-2005

Banking and finance companies continue to be more receptive to outsourcing than any other industry, despite their misgivings about confidentiality of data and competitive position. However, a higher proportion of banking and finance companies decline to permit vendors to disclose contracts awarded than in other industries.

One fast-growing sub-segment of the banking market for outsourcing and processing services calls for vendors to serve as the tangible back office for virtual banks that exist only on the Internet. Some ventures, such as

Bank One's Wingspan have struggled. Others, such as Prudential's Egg in the U.K. have thrived.

This sector remains one of the largest segments of the outsourcing market, representing over 20% of the total U.S. outsourcing market in 1999 and 2000.

Worth noting, although banking and finance enterprises are typically <u>buyers</u> of operational and processing services, there are some significant exceptions. In some cases, as in the example of Chase Manhattan bank, banks are themselves important <u>vendors</u> of such services. Scrutiny of Chase Manhattan's proposed acquisition of J.P. Morgan in September 2000 highlighted the fact that, in 1999, the bank had derived $3.1 billion of operating revenues (almost 10% of total revenues) from "global services," i.e., transaction processing for third-parties. Significantly, this amount was higher than global investment banking revenue, and almost double the revenue derived from corporate lending. In fact, it was higher than all but two bank businesses; global trading at $4.1 billion and cardmember services at $4 billion.

If Chase Manhattan were considered a **vendor** *of processing services rather than a buyer, it would take the third rank in the U.S. market, just under First Data and ADP, with $4.7 billion and $4.5 billion in revenues, respectively (assuming that all of Chase's revenues were generated in the U.S. market.)*

INPUT expects the banking and finance sector to exhibit growth rates consistent with the overall outsourcing market, growing from about $12.3 billion in 2000 to $33.8 billion in 2005.

12. Discrete Manufacturing Industry Market, 2000-2005

The Discrete Manufacturing industry includes a variety of manufacturers, including food, apparel and machinery manufacturing as well as computer and electronic product manufacturing. From the point of view of operational services, all segments of the market are expected to show strong demand for IT outsourcing, Business Process Operations and processing services as they transform themselves from doing business along traditional lines to the new, electronic business model.

Manufacturers are scrambling to put themselves in electronic connection with their customers and their suppliers of raw materials, as well as with their logistics support partners, regulatory authorities and high-potential electronic exchanges. All of these initiatives will require substantial spending on operational services.

INPUT projects that the discrete manufacturing market will grow at a 23% CAGR over the forecast period, increasing from $4.2 billion in 2000 to $10.9 billion in 2005.

13. Education Market, 2000-2005

INPUT projects that the education sector will grow only 6% between 1999 and 2000, but accelerate rapidly at CAGR of 43% for the period 2000-2005, significantly higher than the outsourcing market as a whole. Forecast market size is expected to rise from $783 million in 2000 to $4.7 billion in 2005 based on a convergence of the following, favorable trends:

- Highly politicized initiatives to wire all U.S. classrooms for the Internet.
- Rapidly proliferating Internet-enabled, interactive distance learning ventures on the secondary and professional levels.
- Demographic trends favor the extension of academic and professional education market to ever older constituencies.
- As the price of broadband connectivity drops and the price of business travel rises, an increasing number of companies will choose to outsource their corporate training to vendors able to deliver educational services independent of geography.
- Improvements beyond the PC in technology designed specifically for the education market (such as electronic books and Internet-enabled, hand-held devices) will serve as the catalyst for rapid growth among outsourcing service vendors positioned to provide, manage and render cost-effective use of this new technology.

INPUT forecasts a rapid acceleration of spending by the education industry after 2000 as new products are brought to market and they gain acceptance. Private companies, public and private educational institutions as well as a wide range of commercial training providers are expected to spend large amounts to enable a wide variety of Internet-enabled, new services.

While many educational institutions are turning to IT outsourcing for reasons similar to those of commercial organizations, their unique characteristics and growing size in the overall economy is attracting a wide range of IT outsourcers and providers of processing services.

As an example of the type of educational spending anticipated by state & local governments, consider the Pennsylvania Launches competition for 'digital school district' funding.

In an effort to spur innovation, maximize buying power and concentrate technology resources, officials in Pennsylvania launched a statewide competition to create two cutting-edge digital school districts. State officials have said that, "We're looking for new ideas."

State officials want schools to develop innovative plans that move beyond traditional uses of technology in education. Education officials, striving to look beyond what is currently being offered, insist that "There are a lot of virtual schools out there, or distance learning...We're trying to do more than that, where everything in the school is digitized. How can we think completely differently?"

The state plans to spend $200 million over a five-year period on education technology, based on proposals submitted by schools. A panel of nationwide experts, being selected by state officials, will help choose the winning districts. Reason: "You want to make sure you're not giving $2 million to someone who has hired a good grant writer." Most companies contract directly with school districts, or their philanthropic arms donate to universities or groups of school districts. They rarely contract with state education departments.

14. Federal Government Market, 2000-2005

Overall, the professional services segment will exhibit the most growth over the next five years. As agencies re-engineer their business processes, distribute their operating environments and consider, implement and web-enable their enterprise applications, professional services will be increasingly required. Outsourcing is also expected to play an increasingly significant role in the market. As contracts for desktop services, such as Seat Management, ODIN and N/MCI take hold, outsourcing will become key to supporting the organization and allowing it to focus on accomplishing mission objectives.

Government agencies are encouraged to rely more on outsourcing services, even in the area of acquisition support, despite increasing anti-outsourcing political maneuvers on Congress by government-employee unions and other constituencies. The Federal Activities Inventory Reporting (FAIR) Act, as a further example of the willingness of the Administration and the Congress to consider outsourcing functions previously performed only by government employees, promotes the use of outsourced services.

Processing services includes transaction processing with some batch-mode workloads. It previously included systems operations on contractor-owned equipment (COCO), now part of a separate delivery mode (systems operations) discussed later.

For the last half of the decade of the 1980s, this delivery mode continued to decline in real dollars as installation of new distributed processing systems and desktop processors depressed the need for outside processing support.

Transaction processing, previously called remote computing services (RCS) and until 1998 was identified as ADPE time in the federal IT budget, has continued to decline since FY1984, when growth was projected at 13%. Transaction processing is lower now than in the 1980s, but remains active for agencies still waiting for new facilities. Many of the larger federal data centers continue to add capacity and take on processing for other agencies to partially justify their own operating expense.

The level of $131 million in FY2000 is a further decline from $160 million reported in FY1996. This category will continue to decline for the foreseeable future.

Small amounts of utility and batch processing continue to appear in agency IT expenditures, but have declined to about $33 million per year. The bulk of this work appears in DOD budgets. FY1998 saw a decline, but slight increases are expected over the next five years to $40 million.

Continued budget-deficit reduction actions that delay implementation of upgraded systems stimulate this market beyond levels previously predicted, to meet agency productivity goals and mission objectives. This could support vendor-supplied disaster recovery and security backup systems, if the agencies cannot install equipment to satisfy their needs. Utilities are also a form of ADP insurance for agencies with marginal processing capacity.

Based on expected, positive political developments, federal outsourcing expenditures are forecast at $3 billion in FY2000 and are expected to grow to $6.6 billion in 2005.

Based on the more conservative criteria used by INPUT's federal sector forecast report, spending for outsourcing would rise to only $3.6 billion in FY2005. This represents a compound annual growth rate of 7.5%, which shows no increase since the FY1994 forecast. It was not expected to return to the 15% (or greater) level predicted in 1989, unless applications are outsourced at greater levels than currently identified by agencies—which is the basis of the more aggressive estimate used in this forecast report. If so, outsourcing would have to be accompanied by a significant increase in overall IT spending levels.

The federal outsourcing market is currently one of the fastest growing services segments of the overall federal IT market. Many factors are influencing this growth but the most influential is the Administration's mandate that all functions that cannot be cost- and time-effectively performed by in-house personnel should be outsourced. This has led to some controversy over the last few years about the actual entities to which the government should outsource.

Most logically, the government would outsource nonmission-critical functions to private-sector vendors. However, some agencies have the capability to perform the same work that a vendor could perform. In its award of the ICEMAN contract, the Federal Aviation Administration set a precedent by awarding its data center operations contract to another government agency, the Department of Agriculture. USDA had the excess capacity to be able to take on the operation of the data center without impacting its own mission requirements. Critics argue, to this day, that agencies with excess capacity should be downsized. This would leave no room for external projects, such as those at other agencies. Vendors believe that this causes unfair advantage because the government is not subject to the same rules of competition and may also offer a naturally lower price.

While the legislative controversy sparked by this action has not entirely vanished and continues to attract attention by government employee unions, it is safe to expect the outsourcing of IT functions to continue to play a major part in the federal marketplace. Historically, all efforts to reduce the size of the federal civil service have resulted ultimately in raising the demand for contractors, consultants and outsourcers.

One of the questions unanswered today is whether agencies will move more aggressively to identify government IT positions as part of their Federal Activities Inventory Report. In the first annual reporting there were very few IT positions identified. Following some appeals by industry groups to the Congress, agencies were put on notice to improve their reporting intentions. The next reporting is due at the end of June 2000.

As is normally the case in the federal IT services markets, the civilian sector is expected to experience more rapid growth than the defense sector. This is also influenced by some of the large-scale outsourcing projects currently under way at civilian agencies such as GSA's Seat Management program, NASA's ODIN project, and NASA's CSOC initiative. The civilian sector is expected to grow from $1.6 billion in FY 2000 to $2.4 billion in FY 2005 at a CAGR of 7.3% over the five-year period. On the defense side, the outsourcing market will grow at a 3.8% CAGR from $0.9 billion in FY 2000 to $1.1 billion in FY 2005. Outsourcing still represents one of the fastest growing IT market segments on the Defense side.

Federal outsourcing began to grow again in FY1990, after experiencing lower CAGRs of 6% to 8% since the cutbacks of FY1983, when a number of new systems were implemented. The turnaround began with staffing restrictions, a slowdown of new system acquisitions imposed by the Gramm-Rudman-Hollings Budget Control Act and a slowdown in Defense spending.

15. Health Services Market, 2000-2005

Although it has been slower than other industries to accept IT outsourcing due to legitimate concerns over privacy and regulatory issues, the U.S. health care services market is set for rapid growth over the next five years. Average annual growth of 18% is projected to reflect contracts covering a wide range of functions from front-office automation to medical records, diagnostic databases and telemedicine.

Results of a recent industry survey of 1,400 outsourcing contracts with 38 business partners on behalf of 860 health care organizations confirm INPUT's industry growth forecasts. Survey results show that, while hospitals have been slower to adopt outsourcing than their general industry counterparts, the strategy of outsourcing is growing rapidly in health care organizations. Health care organizations are increasingly using outsourcing to help achieve their business and financial goals. As is the case in other industries, strategic use of outsourcing services means the hospitals can focus on their core business-providing quality care.

Health care executives continue to externalize their spending, although they still lag general industry. Health care organizations now spend about 22% of their budgets on all forms of external sourcing options, compared to 33% in general industry. These external sourcing options include supplemental staffing with non-company personnel, outsourcing, and strategic alliance and joint ventures with one or more business partners.

Outsourcing spending in health care increased 20% from 1999 to 2000. There was a large increase in the use of outsourcing among health care executives. Average expenditures on outsourcing by health care executives now amount to 16 percent of their overall budget. At the same time the use of supplemental staffing declined significantly. Long-term strategic relationships with specialized service providers are clearly replacing the use of supplement staff within health care.

Outsourcing is projected to constitute 20% of health care budgets by 2002. Outsourcing spending is on a trajectory to constitute 20% of the average health care executive's budget by 2002, with an average annual growth rate of 15% during the period.

Smaller health care organizations (less than $100 million in revenue) are now using external sourcing at the same rate as large organizations. In 1999, larger health care organizations (greater than $500 million in revenue) were taking greater advantage of outsourcing and external sourcing options, but outsourcing has now become equally attractive among smaller health care organizations.

Outsourcing in finance, support services and clinical operations is poised to expand. In both general industry and health care, external sourcing expenditures differ by function. Information technology currently has the largest portion of the external sourcing budget (19%). In 1999, clinical operations was the *least* externally sourced area of the four surveyed (clinical, support services, information technology and finance). However, clinical outsourcing spending grew 13% between 1999-2000, the highest growth rate of any functional area, and now represents more than 12% of total external spending. Over the next two years, finance and support services show the greatest potential for growth in external spending.

Experience with outsourcing is a key factor in its acceptance. The findings suggest that health care executives who are experienced with outsourcing have a more positive perception of outsourcing's ability to deliver low-cost, high-quality innovation and speed to market.

16. Insurance Industry Market, 2000-2005

Insurance companies generate an enormous volume of paperwork, transactions that need processing and costs. Accordingly, it benefits from all types of operational services, including IT outsourcing, Business Process Outsourcing and processing services. Similar to the painful transition of the securities brokerage industry from a high-margin, high-cost broker delivery model to a low-margin, low-cost online brokerage model, insurance companies are learning how to live with, and benefit from the Internet. For better or worse, insurance products remain sufficiently complex and resistant to comparison to make them less amenable than securities trading to any quick move to online channel distribution.

Nevertheless, even if the sales front-end of the industry lags other industries in the use of operational services, internal and back-end processes are being moved to an electronic business model more rapidly. This process is being fueled—as is the case elsewhere—by the desire to cut costs and improve competitive position, as well as by a strong need to comply efficiently with regulatory authorities and provide improved customer service.

INPUT projects that this market will grow at an average annual growth rate of 21% over the next five years, expanding this market from $8.4

billion in 2000 to $21.6 billion in 2005, and making it the second-largest sector in the overall U.S. outsourcing market.

17. Process Manufacturing Industry Market, 2000-2005

The diverse segments of the Process Manufacturing industry show no single pattern of activity in regard to operational services. Ranging from oil & gas producers, to mining operations, food and beverage manufacturers, textiles, chemicals, paper and plastics manufacturers, each segment has a differing profile of needs in regard to IT outsourcing, Business Process Outsourcing and processing services. Yet, overall, INPUT expects continuing, high relative demand for operational services support in every IT delivery category from Infrastructure Operations to Application Management.

In general, this industry comprises large, traditional, well-established enterprises that are making a transition from legacy business systems and processes to the new electronic business model. This transition will, of necessity, proceed rather slowly, but the urgency of the process will serve as the catalyst for significant growth of spending for operational services due to the IT skills shortage, high turnover and the need for highly specialized skills sets that cannot easily be acquired and retained (cost-effectively) by companies in this industry.

Average annual growth of 24% reflects the continuing strength of the U.S. economy, competitive pressures resulting from globalization of markets and the urgent need for manufacturers to improve efficiency and cut costs when they are unable to raise prices in a low-inflation environment.

VI

Analysis of Select Outsourcing Vendors

In an attempt to identify potential correlations between a vendor's financial performance and its market positioning, INPUT selected the following companies as representative of both the commercial and federal IT outsourcing markets.

They are:

ACS, AMS, CSC, EDS, Fed Data/Logicon, Getronics, Raytheon, SAIC, UNISYS, CACI, Exult, Bisys, Compaq, Convergys, Entex, Fiserv, Keane, OAOT, Perot Systems, USInternetworking.

Some of these vendors are active primarily in the federal market, such as CACI; some are active entirely in the commercial market, such as Convergys. Some are entirely IT outsourcers, such as Exult. For others, IT outsourcing comprises only a small part of total revenues, as is the case with Raytheon. A few, such as Bisys and Fiserv, are entirely specialized in a particular vertical industry—here banking and other financial services.

Some are independent, such as ACS; others are operating units of larger, global organizations, as is the case with the Wang federal market unit within Getronics or the Entex unit within Siemens.

These differing company characteristics make it impossible to draw definitive conclusions from the data, because multiple variables preclude entirely accurate comparisons. Nevertheless, as can be seen in the exhibits that follow, some trends are visible.

Overall, INPUT ranks this select list of companies as follows in regard to their:

- Participation in the U.S. market;

- Proportion of revenues derived from IT outsourcing;
- Orientation in regard to federal versus commercial business.

Exhibit VI-1

Vendor Ranking

Primarily U.S. Commercial IT outsourcing

- Exult
- Entex [Siemens]
- Fiserv
- Bisys
- Convergys
- OAOT
- USInternetworking
- ACS
- Keane
- CSC
- Perot Systems
- EDS
- UNISYS
- Compaq
- SAIC
- AMS
- Getronics [Wang]
- CACI
- Raytheon
- Fed Data/Logicon [Northrup Grumman]

Primarily federal market, less IT outsourcing

Source: INPUT

A
Market Positioning and Strategy

Underlying the decision regarding whether to increase a company's level of business in the area of IT outsourcing, particularly outside of the federal market, is the assumption that this market segment is more profitable. The challenge is to determine whether this assumption is true and, if so, what extent.

Unfortunately, the ability to test this assumption accurately depends on being able to assemble a significantly large amount of data for a representative sample of vendors—and both aspects of this effort are problematic.

INPUT began with a representative sample of vendors that are active in varying degrees in both the U.S. commercial and U.S. federal IT outsourcing markets. However, because of the substantial differences in their market positioning (and difficulties in gathering comparable financial data), potential conclusions were weakened by an excessive number of variables.

In an effort to reduce, or normalize these variables, INPUT ranked vendors according to weighted factors that included the extent to which the vendor:

- Derives revenues from the U.S. market
- Derives revenues from IT outsourcing
- Participates in the commercial IT outsourcing market.

For example, as shown in Exhibit VI-2, vendors vary substantially in regard to the proportion of their revenues generated by the U.S. market.

Even so, they display great variation depending on their specific characteristics. While USInternetworking, a leading Annapolis, Maryland-based ASP, is not active outside of the U.S., its revenues are small ($5-40 million) and it is not profitable. In contrast, Raytheon is also active entirely in the U.S. market, but has revenues of about $20 billion.

Most vendors analyzed here are public enterprises, but not all: SAIC is an employee-owned organization; Fed Data, Logicon and Litton/PRC are well-defined, but wholly owned operating units of Northrup Grumman. Germany's Siemens AG recently acquired Entex, which has a prominent position in the desktop services market segment. Similarly, Wang Global, which has been prominent in the U.S. federal market, was recently acquired by Amsterdam-based Getronics, a global organization that (with

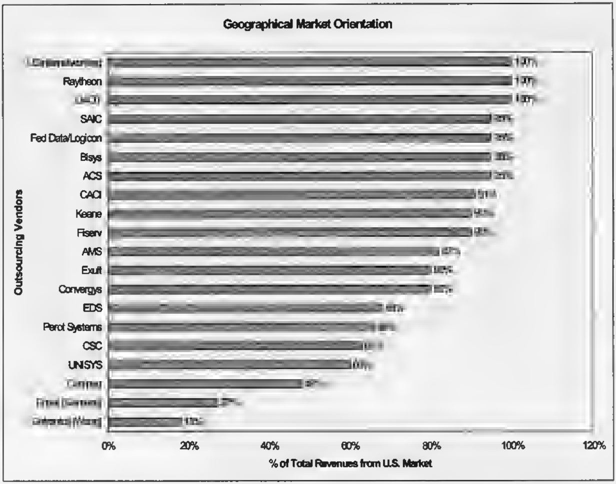
Wang) derives less than 20% of its revenues from the U.S. market. OAOT is a publicly held company that is active in the commercial market, buy affiliated indirectly with privately held OAO Corp, which is a federal market vendor (the CEO of OAO Corp is on the Board of Directors of OAOT).

Ideally, analysis would have been limited to comparable, publicly held vendors. Yet, that approach, too, would have posed analytic problems because it would have excluded organizations that are important, prominent and informative.

Therefore, the exhibits that follow and the modest conclusions associated with them, at best, suggest directions for further research based on additional data and/or a consideration of additional vendors. The data presented here should be considered preliminary. As such, they do provide a strong underpinning for a decision for a decision to enter the U.S. commercial IT outsourcing market—at best, they illustrate the variety of results possible.

Exhibit VI-2

Select Vendors' Market Orientation



Source: INPUT

Exhibit VI-3 demonstrates the extent to which the largest IT vendors have advanced the global diversification of their sources of revenues. For example, although EDS holds a prominent position in both the U.S. federal and commercial IT outsourcing markets, the U.S. generates only two-thirds of its total revenues. CSC derives even less than two-thirds of its total revenues from the U.S. market.

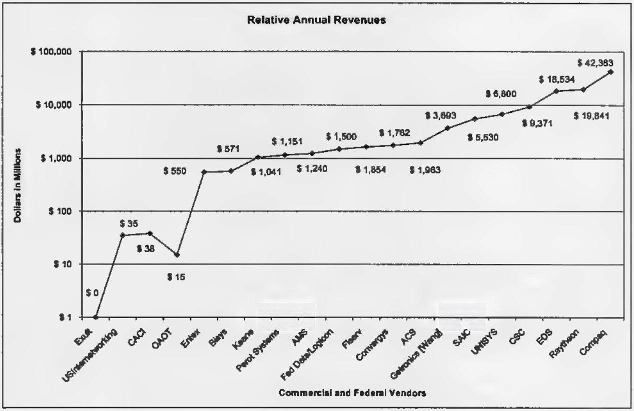
At the bottom, as an operating unit Wang derives all of its revenues from the U.S. market, but these represent less than 20% of parent Getronics' global revenues.

From another point of view, Raytheon may be a totally U.S. market vendor, but—as can be seen in Exhibit VI-3—it is only marginally active in IT outsourcing.

AMS derives most of its revenue from the U.S. market and is these are generated almost equally from public sector and commercial markets, making it one of the most representative vendors analyzed.

Exhibit VI-3

Relative Vendor Size by 1999 Revenues



Source: INPUT

The logarithmic scale of Exhibit VI-4 portrays, but masks, the tremendous variation in size between the vendors under consideration.

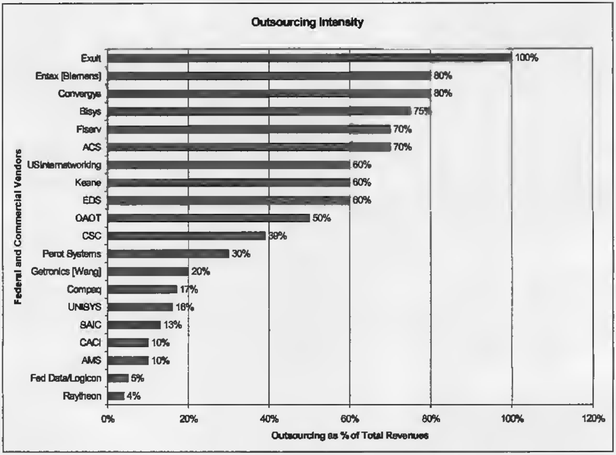
At one extreme, Exult is newly operational and had virtually no revenues in 1999, the base year. In 2000, it gained prominence by signing an impressive, $1 billion outsourcing contract, which will generate significant revenues in subsequent years.

USInternetworking is growing revenues rather impressively, but, as can be seen elsewhere, continues to spend even greater amounts on capital investments as well as sales and marketing, so that it remains dependent on the capital markets for survival.

At the other end of the spectrum, while Compaq has revenues in excess of $42 billion, it derives less than 20% from services and even less than that from IT outsourcing.

Exhibit VI-4

Comparative Proportion of Revenues Derived from IT Outsourcing



Source: INPUT

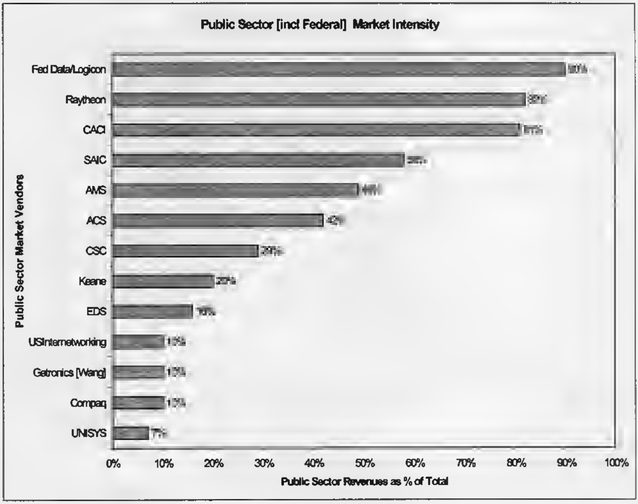
Considering only the proportion of revenues a vendor derives from outsourcing, Exult, Entex and Convergys rise to the top of the list. However, this ranking is misleading for several reasons.

As indicated earlier, Entex is now an operating unit of Siemens AG, which is a highly diversified, global organization that derives a relatively small proportion of its total revenues either from IT outsourcing, or from the U.S. market. Entex, despite having achieved a position as a prominent vendor in the U.S. desktop services market was not profitable at the time of its acquisition.

The next tier of vendors, Convergys, Bisys, Fiserv and ACS, which are very active in the U.S. outsourcing market, are profitable, but—worth noting—only one of them (ACS) is in the public sector market. Convergys and BISYS both insist that they are "agnostic" regarding whether customers purchase on a "product" or "service" (outsourced) basis, believing that customers benefit from having such flexibility.

Exhibit VI-5

Public Sector Market Intensity



Source: INPUT

Some vendors include their public sector work in the "commercial" market; others include as part of their "federal" market business. For that reason, Exhibit VI-6 normalizes the data in order to portray accurate, comparable rankings.

Subsequent exhibits portray relative vendor profitability correlated to the intensity of their participation in IT outsourcing. These data are then compared to other factors. Note that the 10% figure for Getronics represents the parent organization, which obscures the federal market orientation of its Wang unit. Worth noting, the top half of vendors shown here as active in public-sector markets are NOT primarily IT outsourcers.

Exhibit VI-6

U.S. Commercial Intensity

Source: INPUT

Seen from the opposite point of view, Exhibit VI-6 portrays vendors based on their commercial market activity. As indicated earlier, Getronics is primarily in the commercial market—but outside of the U.S.

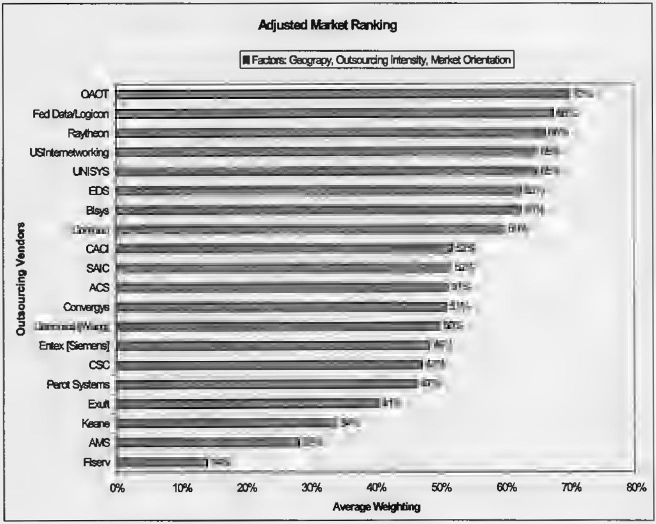
UNISYS ranks in the middle in regard to commercial versus federal orientation, but, as noted earlier, outsourcing accounts for only 16% of revenues, of which 40% are generated outside of the U.S.

Similarly, Compaq ranks near the bottom of all vendors here because a high proportion of its total revenues are generated outside of the U.S.

ACS and SAIC , which rank in the middle, are most representative of the medians, being active in outsourcing, in both the federal and commercial markets, and primarily in the U.S.

Exhibit VI-7

Market Ranking by Factors



Source: INPUT

Exhibit VI-7 portrays a composite, weighted ranking of vendors that considers multiple factors, including geography, extent of outsourcing activities, and extent of orientation toward the U.S. commercial market.

Of the top four ranked vendors, two (OAOT and USI) are small and relatively newly formed organizations. Fed Data/Logicon's parent Northup Grumman and Raytheon are very large DoD vendors with high exposure to the commercial market, but with less experience in IT outsourcing.

B

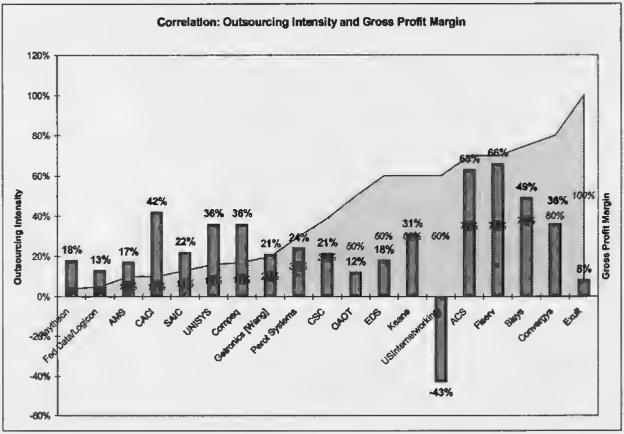
Financial Performance

Because of the wide disparities between the market profiles of the vendors under analysis, there is no obvious correlation between their respective levels of participation outsourcing and their respective levels of net profit.

Exhibit VI-8, below, plots vendors' increasing proportion of revenues generated by outsourcing to their most recent gross profit margin percentage. (Gross profit provides a better basis for comparison than net profit because net figures can reflect a number of nonoperating influences.)

Exhibit VI-8

Outsourcing Intensity and Gross Profit Margin



Source: INPUT

Excluding Exult and OAOT (with minimal profit) and USI with losses), vendors that are relatively more active in the outsourcing market appear marginally more profitable than those, such as Raytheon and Fed

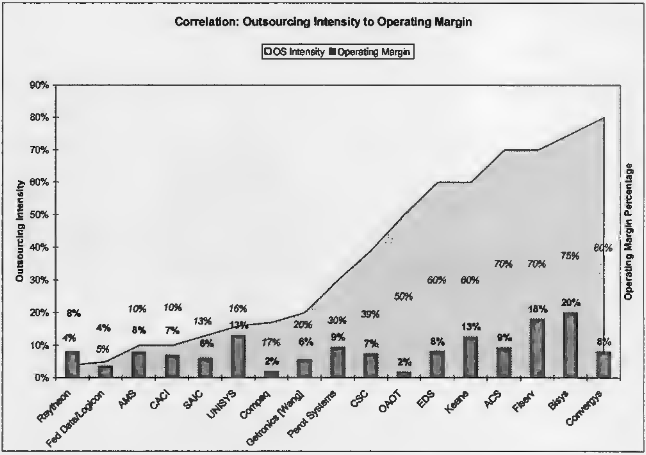
Data/Logicon, which are both minimally active in outsourcing and commercial markets. CACI stands out as an exception, being very profitable despite a low level of outsourcing activity.

Mid-tier companies, such as CSC, EDS, Getronics and Perot Systems, show a convergent level of profitability that reflects their larger size, geographical and business-line diversification.

Exhibit VI-9 plots vendors' levels of outsourcing activity to their operating margins.

Exhibit VI-9

Outsourcing Intensity to Operating Margin



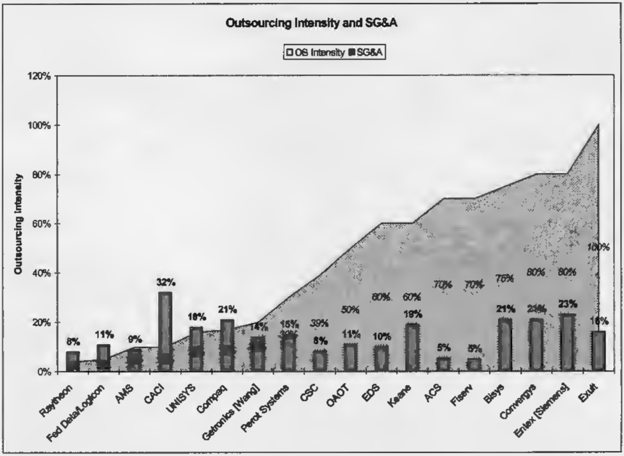
Source: INPUT

Operating margins show a substantially different profile from that of gross profit margins. This series of data is one of the most relevant on which to compare the relative attractiveness of the commercial IT outsourcing market compared to all other alternatives.

Here, the top-five outsourcers show an average operating margin of 13.6% compared to an average of 6.6% and 6.7% for the bottom five and the center-tier vendors, respectively. UNISYS stands as exceptional based on the achievement of an equal operating margin percentage as Keane, despite a much lower level of outsourcing activity, 16% versus 60%.

Exhibit VI-10

Correlation of SG&A to Outsourcing Intensity



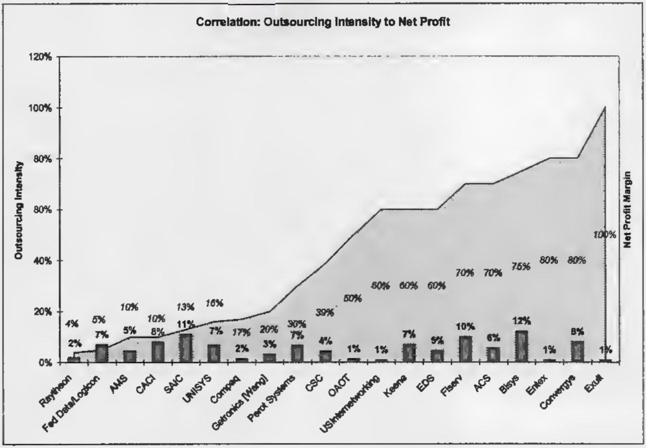
Source: INPUT

Because survey respondents were asked whether they believed that sales and marketing costs were higher in the commercial market than the federal market, INPUT examined whether outsourcers as a group had higher levels of SG&A.

In fact, with the exception of CACI as an obvious outlier at 32%, the top tier of outsourcers does appear to have a somewhat higher level of costs than the mid-tier that includes CSC, EDS, Perot and OAOT.

Exhibit VI-11

Outsourcing Intensity to Net Profit



Source: INPUT

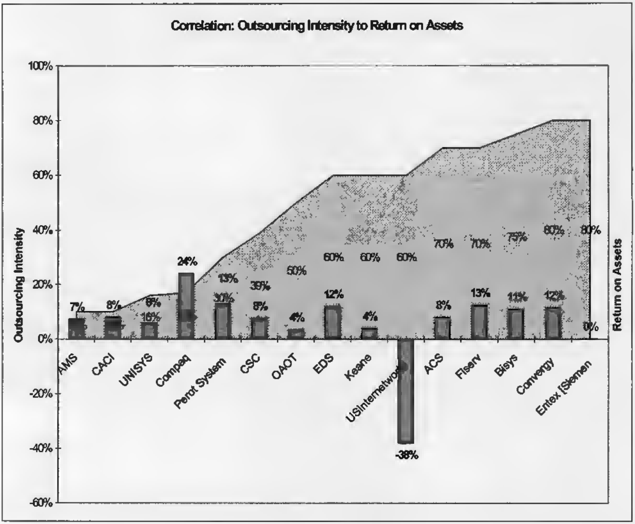
As indicated earlier, net profit margins are subject to a variety of nonoperating influences that make them less indicative of outsourcing profitability than operating margins.

USI, Exult, Entex and OAOT, in fact, are unprofitable enterprises, but have been shown in Exhibit VI-12 as negligibly profitable in order to facilitate the display of data.

On average, the top six vendors (excluding Exult and Entex) have a net profit margin of 6.9% compared to an average of 5% for the remaining vendors that are less active in outsourcing (excluding USI).

Exhibit VI-12

Outsourcing Intensity to Return on Assets



Source: INPUT

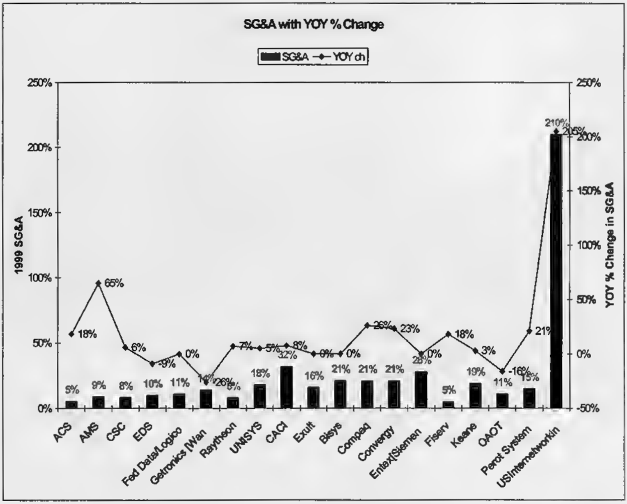
Survey participants were asked whether they believed that access to capital was a barrier to participation in new markets for IT outsourcing. Few respondents believed this was a factor in winning new business (but many admitted that size mattered).

As another way of approaching the same issue, INPUT plotted vendors' outsourcing activity to their ROA levels on the theory that, were outsourcing to require less profitable allocations of capital, their ROA levels would look comparatively weak.

In fact, the data show no clear trend. Excluding Entex and USI, the top tier of outsourcers do not show financial performance that differs markedly from the remaining vendors. Worth noting, Compaq shows the highest ROA even though it is in the bottom tier of vendors in regard to outsourcing intensity. Excluding Compaq, the remaining vendors' performance is similar to that of the top-tier outsourcers.

Exhibit VI-13

Level of 1999 SG&A Expense Correlated with Year-over-Year Change



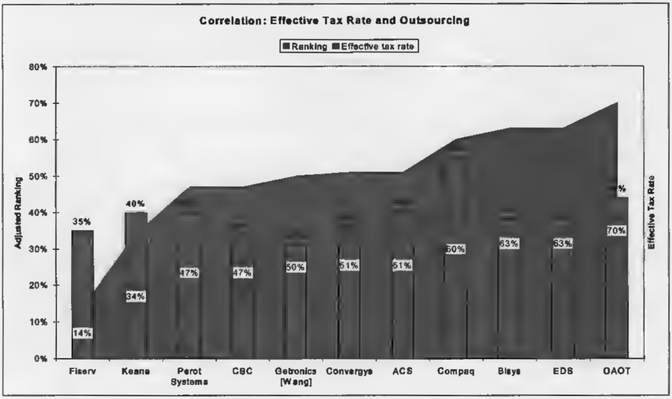
Source: INPUT

Exhibit VI-13 plots vendors' nominal level of SG&A against the year-over-year change in SG&A in order to determine whether, or not, any trends are discernible between vendors with higher and lower levels of outsourcing activity.

Even dismissing USI and AMS as outliers, no such trend is evident. In fact, SG&A declined sharply at OAOT, Getronics and EDS, while rising markedly at Compaq, Convergys and Perot Systems. Without additional data, it is impossible to say how much of these fluctuations is attributable to outsourcing activity and how much to other businesses.

Exhibit VI-14

Effective Tax Rates Correlated to Adjusted Ranking as Outsourcers



Source: INPUT

Exhibit VI-14 portrays the relationship between vendors' effective tax rates and their levels of outsourcing activity (tax rates are at the tops of the columns; levels of outsourcing are indicated inside each column).

Although there are significant discrepancies between vendors' levels of taxation, the trendline for effective tax rates dips only slightly to the left in favor of the less active outsourcers.

C
Financial Trends

1. Federal Market

A cross-section of federal market vendors (but not primarily outsourcers), ranging in size (annual revenue) from $10 million to $1 billion, or more, show shows a high level of consistency over the past decade. Based on by a series performance metrics data, a leading trade publication reached the following conclusions:

- Several important performance measures are improving, including revenue growth rates, operating profit performance (earnings before interest and taxes) and net income return on shareholders equity.
- A representative group of private federal vendors showed a significant increase in year-over-year revenue growth during 1998-1999, relative to previous periods.
- On average, the federal vendor group grew revenue 18-20% annually compared to 10-12% in each of the previous five years. Acquisitions by several active private companies contributed to this result.
- Also, since the 1994-1996 period, the cost of interest-bearing debt increased about 230 basis points, or about 25% above the 9% level prevailing in the earlier period.
- On a percentage of revenue basis, during the 1996-1999 period, total invested capital ranged from 17-22% of sales, with about one-third in interest-bearing debt and two-thirds in equity.
- Effective net working capital (current assets, less cash, minus current liabilities, less interest-bearing debt) ranged from 10-12% of sales. Typically, net fixed assets fall in the range of 3-5% percent of sales.
- Assuming margin improvement of one-quarter to one-half percent annually and compounded annual revenue growth of 10%, over the next five years, public company per-share values could grow by 85%.
- A capable industry competitor could triple its share value over five years either by increasing revenue growth to 25% compounded annually, at a steady 5% EBIT margin, or increasing the EBIT margin by one-half percent per year, while retaining a 10% annual revenue growth rate.

2. Commercial Market

While there is some concern that corporate IT budgets may shrink significantly in 2001, spending for outsourcing projects will not likely be affected directly. Reason: a growing amount of spending for IT outsourcing is expanding beyond the traditional IT budget.

While pre-recession alarm bells have been ringing for the U.S. macroeconomy, customer demand for a variety of services to support Web site development, networking and—overall—the transition to e-business, continues to be strong. Managements believe that they must take advantage of any temporary weakness in the market insofar as possible to reinforce their own capabilities. Accordingly, none of the users who responded to INPUT's survey reported any intention to reduce spending on IT outsourcing.

On the contrary, financial pressures may induce smaller companies to outsource as a means of coping with multiple inabilities to meet their needs internally.

Vendors are coping with margin pressure by attempting to streamline their own cost structures (which promotes the growing trend of IT vendors outsourcing noncore functions to other IT vendors, such as Microsoft's award of a desktop services contract to Entext, or EDS's award to Pinacor for contract fulfillment for equipment). Also, vendors are continually striving to enhance their value proposition with customers so that price retains a lower priority in customer decision-making.

In that spirit, vendors are taking an increasingly hard look at the types of outsourcing services that it can provide profitably. For example, formerly "pure" ASPs such as USI have come to the realization that the only way to achieve profitability is to assure that at least 20% of revenues can be generated by higher-margin consulting business. Inspired by IBM's success in offsetting declining profits from sales of hardware with services income, Compaq is attempting (with difficulty) to do the same.

Overall, vendors want to be able to offer customers a mix of custom consulting, IT outsourcing and non-IT services, such as BPO, facilities management, equipment, or contract staffing services. As noted earlier, critical all of these efforts is having good knowledge of specific vertical industries. Without that expertise, penetrating new accounts will remain very difficult to accomplish profitably. There will always be a demand for low-margin, commodity services, but vendors tempted into this market will find success very difficult to achieve and maintain.

As numerous vendors have demonstrated over the past year—and continue to demonstrate—building revenues while losing money is an unsustainable and unappreciated feat under today's market conditions, even if defensible in theory.

D Outlook

1. Federal Market Vendors

Overall, the federal market continues to be attractive based on the following favorable developments:

- Nearly one-half of civilian jobs in the federal government could be outsourced to private firms under the 1998 Federal Activities Inventory Reform (FAIR) Act, according to the final year 2000 list of jobs released by the Office of Management and Budget recently.
- Overall, 115 federal agencies submitted lists of 1.7 million federal positions. Of those jobs, roughly 50% were identified as 'commercial in nature', meaning that the work could be performed in the private sector. (The list was relatively unchanged from last year.)
- The Defense Department listed 452,807 civilian jobs that could be performed in the private sector on its FAIR Act inventory, but only 178,771 of those jobs are truly candidates to be contracted out. Most of the other positions are exempt from commercial competition for various reasons.
- The Energy Department listed 9,941 jobs that could be contracted out, while the Interior Department identified about 18,000. Over the next few years, these numbers are likely to rise at all agencies.
- Federal budget surpluses provide both the Bush administration and Congress with the ability to fund priority programs, and many observers believe that incremental spending will increase.
- In particular, the Bush administration has prioritized, among other things, national defense and intelligence agencies for increased funding. The pending Quadrennial Defense Review will likely continue to emphasize increased government spending on technology as a response to projected threats.
- Bush's budget is expected to include a $100 million fund that would run IT programs across government, similar to one he created in Texas, where he had experience working with technology. As governor, he called for giving all Texans easy, direct access to information on state programs and services, and the "e-Texas plan" has been called one of the most advanced in the nation. He cut the state Internet-access and data-processing taxes and signed legislation increasing salaries for many IT positions in Texas.

- The contradictory desire to reduce headcount in the federal civil service while increasing services provided make higher levels of outsourcing inevitable.

This will require identifying operating units that can and should be outsourced (in the face of continued resistance by government employee unions), followed by completion of an A-76 review, and on through contractor proposal solicitation and selection.

There has been much speculation regarding the extent to which IT vendors may benefit from a renewed effort by the Bush administration to appoint a federal CIO with a broad mandate.

One likely result of this broad view will likely be an expansion of interest in BPO contracts that incorporate IT functions along with a variety of non-IT responsibilities. PricewaterhouseCoopers has had much success in this market segment on the commercial side. CSC and Lockheed Martin have received a number of large contracts in the federal segment of this market.

For example, in January 2001, Lockheed Martin Aircraft & Logistics Centers' was chosen by the Defense Logistics Agency (DLA) to manage aircraft parts support for the C-5 Galaxy aircraft under a $1.1billion, three-year contract that has options for extension. Under terms, Lockheed will function as a supply and distribution manager to dept maintenance facilities and worldwide customers. Aircraft and logistics centers will also establish information systems that will enable DLA's supply centers to place and track electronic orders, giving customers total asset visibility through the Internet.

According to the Office of Management and Budget, agencies already spend $114 billion a year on five categories of services:

- R&D
- Construction,
- ADP
- Architecture/engineering tasks; and
- Miscellaneous work, including everything from janitorial services to consulting.

Outsourcing will likely continue to grow as agencies respond to pressures to reduce headcount. Austerity will prevail while Congress and the White House strive to cut more than $900 billion in projected government spending over the next seven in a continuing effort to eliminate the federal debt.

Because future DoD budgets are expected to decline in absolute terms (barring a dramatic change in priorities by the Bush Administration), funding for modernization efforts will have to come from savings in support operations such as depot maintenance, base services and health care-areas (defined by some as ideal for privatization). From a contrarian point of view, the Electronic Industries Association expects DoD's procurement budget actually will actually increase in the next decade while the overall defense budget continues to fall. EIA attributes the predicted rise to privatization of support operations.

Some would go farther. The Reason Foundation insists that an aggressive, governmentwide privatization campaign could lower federal spending by as much as 40% and yield more than $350 billion in one-time proceeds from the sale of federal assets. The Defense Department reported to Congress that in programs it managed to outsource last year, operating costs were cut by an average of 31%. One explanation: "In-house support staffs have little incentive to improve productivity levels, but an outside contractor knows that it will be tossed out and replaced by a better performing competitor unless quality is improved and costs are cut," (Peter Drucker).

2. Commercial Market

Three primary trends will have the greatest impact on the development of the U.S. commercial IT outsourcing market and on the profitability of vendors serving that market. These include:

- The continuing transition from traditional business to e-business (see Lou Gerstner's keynote address in the Appendix for insights into this process);
- The proliferation of mobile computing together with the development of e-commerce, or "m-commerce," and the challenges that this poses to both providers of infrastructure, network and distributed services;
- The growing willingness of U.S.-based customers and vendors to use offshore service providers.

a. The Transition to E-Business

INPUT believes that a real e-business revolution is underway and the signs are everywhere, but there is a clear danger that unwise managements will convince themselves that launching a Web site and stocking it with pages of brochures puts them well on the way.

Unfortunately, this "library" approach to e-business resembles the deception achieved by Hollywood sets that may be very impressive and convincing when seen head on, but whose credibility vanishes when seen from the edge—which reveals them to be thin, one-dimensional imitations of reality.

As the number and type of Internet-enabled devices proliferate, especially wireless formats, B2B customers and consumers alike demand both instantaneous execution and access to data.

Ever rising expectations favor "best-of-breed" vendors; due to the scale and immediacy of e-business and e-commerce, failure can mean huge losses within minutes or hours.

For these reasons (and others), there has been a tremendous proliferation of all types of electronic trading communities, net auctions, portals, vortals (vertical industry portals), and other net infomediaries as enterprises seek to establish contact with sources of supply and services.

What they have in common is the goal of bringing together buyers and sellers who otherwise would likely never have found each other, eliminating middlemen, and permitting buyers, whether consumers or businesses, to locate critical products, services and information.

The end goal of the transformation required by the dynamics and technology of e-business is the seamless interconnectivity of all business processes. For this, a fully functional Web site plays an integral role, directing traffic to and through an enterprise to its own suppliers and business partners. Therefore, the achievement of launching a Web site that is no more than an electronic library represents a very Pyrric victory.

Electronic business comprises only a relatively small portion of the operational services market today—and not necessarily the portion identified as "Internet-centric." Some elements of e-business can be conducted without the Internet by using VPN and other traditional network solutions. Conversely, some Internet-enabled services do not necessarily constitute "e-business." For example, an ASP that uses the Internet merely to link a customer to a remotely-hosted software application would typically be considered part of the outsourced, transaction processing market. Beyond that, many aspects of e-business are being implemented directly and without recourse to outsourcing.

(See Lou Gerstner's summary in Appendix E of the challenges of the transition to e-business from a top-tier vendor's point of view.)

b. The Advent of Mobile Computing and "M-Commerce"

Although PC-based e- commerce remains the preferred mode in the U.S., elsewhere Internet-enabled mobile phones are customers' preferred medium for getting information, making transactions, and checking on the status of their affairs. While the migration of American consumers and business to m-commerce based on IP telephony has been slower than many expected, there is little doubt but that it is on the way. Vendors need to prepare for the challenges of providing network and infrastructure services in a wireless environment, along with CRM applications and ERP support.

Expect the complexities involved in providing customized, targeted content and offers will increase exponentially. The job of organizing, managing, and targeting your content and transactions for different market segments becomes much more challenging. In a wireless environment. Both business and consumer customers will be expecting vendors to provide a seamless set of Internet-enabled applications and content that they can interact with throughout the day as they move from place to place.

Few top executives have been more bullish on this trend and its importance for vendors than Michael Capellas, CEO of Compaq.

Speaking at the company's annual analyst meeting, Capellas outlined his vision of a world in which "all kinds of devices" will access the Internet over an expanding grid of servers." With the rise of wireless handhelds, phones and pagers that can access the Internet and interface with multiple servers, he sees a profound change is taking place in the IT industry.

Capellas agrees with Lou Gerstner's (CEO of IBM) view that the post-PC age will be one of "pervasive computing." In the new distributed computing age, PCs won't remain the primary devices accessing servers. Instead, servers will distribute data to a wide range of machines, including PCs, handheld computers, mobile phones, pagers and Internet appliances via wired and wireless connections—some would include wearable computers that are embedding into clothing and furnishings. Beyond that, Capellas believes that Internet connections inside cars will become prevalent as well: "The wireless Internet will continue to make things change very rapidly. It won't be more than a couple of years before virtually every car has Internet access built in."

If so, vendors wanting to survive and prosper must begin now to meet the challenges of his new environment for both businesses and consumers.

c. The Growing Lure of Offshore IT Services—a Challenge as Well as a Threat

The number of companies that are leveraging global resources and looking beyond national boundaries to meet their IT service needs is growing, just as the number of companies that are expanding to address global markets is on the rise.

Increasingly, U.S. companies are taking advantage of resources located outside the country in addressing their information technology (IT) services needs. This growth, projected at a compound annual growth rate of 45% through to 2003, is being fuelled by a combination of better services and capabilities from overseas resources combined with new technologies. The Internet is also helping to eliminate distance as a barrier to providing services.

The trend towards using offshore services and resources in India, Israel, the Philippines and elsewhere, has been fuelled in recent years by the significantly improved depth and quality of services offered, combined with new technologies and the Internet.

Key areas of opportunity for offshore IT services vendors are: Web/E-Business services, IT-enabled services, industry-specific services, quick time-to-market. Key areas of concern regarding offshore IT services on the part of buyers of such services include control, risk, language and culture.

One key finding from a recent study by INPUT is that perception lags reality.

There is lack of awareness among senior executives as to what is available today from vendors offering offshore services or resources, or even who the key players are in offering such services. The perception of most of the senior IT management interviewed, particularly those that have never used offshore services, was that offshore services providers offer low-cost -- and often low-quality -- programming capabilities. In fact, the offshore services providers at the forefront of the market are focused on selling leading-edge services rather than low-cost services.

Historically, U.S. companies have relied on local, American resources to meet their need for professional information technology (IT) services. However, this is changing and the pace of change is expected to increase significantly over the next few years.

<u>More and more organizations are turning to IT services providers that use resources outside the U.S.</u> Indeed, a significant percentage are already using offshore IT services. In some cases, these services are purchased

and managed through vendors headquartered in the U.S.; in other cases, it is through foreign companies selling through local branch offices.

There are two key trends driving this growing use of offshore IT services:

1. The world is getting smaller. Whether the resources of a services supplier are located next door or on the other side of the globe is becoming increasingly transparent to the users of IT services. On the one hand, technology -- particularly the Internet -- is making it easier, cheaper and faster to communicate across vast distances. Distance is becoming less of a factor in delivering any kind of service.

   At the same time, experience, contact and awareness have helped to make language and culture less of an issue in delivering offshore services.

2. The depth and quality of offshore services have advanced significantly. Offshore IT services providers have come a long way over the past few years. The range and quality of services offered are comparable with, and in some cases exceed, those available from American suppliers. More significantly, some offer services, products or capabilities that are unique and simply not available elsewhere. Examples include firms with skills in combining Web-enablement with industry-specific competencies.

Contrary to popular opinion, cost alone is not one of the more significant factors driving the growth of offshore services. While offshore services providers are helping to lower the cost of IT services, particularly in applications development and maintenance, American executives are looking beyond cost alone for value and quality solutions to meet their needs.

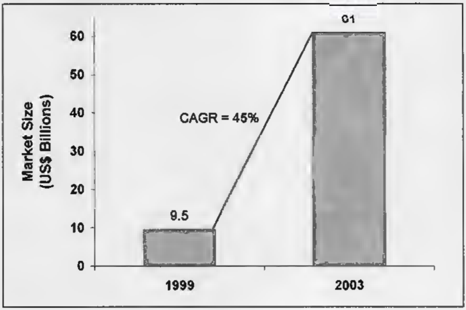
The use of offshore services and resources in the U.S. is on the rise. Most offshore vendors are seeing revenue growth of 40-80%, and some are even experiencing triple-digit growth.

In 1999, INPUT estimates that U.S. and Canadian companies spent US$9.5 billion on offshore services. By 2003, this is expected to reach US$61 billion, representing a 45% compound annual growth rate.

Exhibit VI-15 summarizes INPUT's projections for growth in this market segment.

Exhibit VI-15

North American Market for Offshore IT Services (1999 - 2003)



Source: INPUT

A growing awareness and acceptance of offshore vendors by American executives is helping that growth. Unexpectedly, one of the biggest factors that helped to drive the use of offshore services providers in the U.S. was the Year 2000 issue.

Over the past few years, companies had been turning to offshore vendors to help them with their Y2K compliance work. Those offshore vendors appear to be turning most of those short term, one-time projects into long-term business, which says a lot about the capabilities of these services providers and the value of a strategic partnership with offshore services providers.

A factor helping to spur the growth of offshore services is the importance of choice for IT decision-makers. IT management has always been attracted to market changes that provide greater choice, more options and the opportunity to gain better leverage with existing suppliers.

Table of Contents

APPENDIX A 104

Summary Vendor Profiles 104

APPENDIX B 112

User and Vendor Survey Questionnaires 112

APPENDIX C 122

User and Vendor Survey Results 122

APPENDIX D 227

Operational Services Market Forecast Summary 227

APPENDIX E 233

IBM CEO Lou Gerstner's keynote address: "Next Generation E-business, " at the eBusiness Conference and Expo in New York City on December 12, 2000. 233

List of Exhibits

Exhibit C-1 Tabulation of Vendor Interview Survey Responses by Question 122

Exhibit C-2 Tabulation of Vendor Interview Survey Responses by Respondent 159

Exhibit C-3 Tabulation of User Interview Survey Responses by Respondent 197

Exhibit C-4 Tabulation of User Interview Survey Responses by Question 214

Exhibit D-1 U.S. Operational Services Market, 2000-2005 227

Exhibit D-2 U.S. Outsourcing Services Market (incl BPO), 2000-2005 230

Exhibit D-3 U.S. Processing Services Market, 2000-2005 231

Exhibit D-4 Vertical Industry Market Breakdown, U.S. Outsourcing Market, including BPO 2000-2005 231

A

Appendix

A
Summary Vendor Profiles

Following are annotations on the principal IT outsourcing vendors discussed in this report.

Vendor	Year	Comment
ACS	2000	Divested commercial staffing business, recorded charge of $44 million. Wages & benefits = 43% of revenues; during FY2000, acquired Intellisource Group, Inc., provider of IT solutions to public-sector and utilities markets.
AMS	2000	Founded in 1970, AMS is headquartered in Fairfax, Virginia. The firm has more than 9,000 employees and 59 offices worldwide. Its 1999 revenues were $1.24 billion. AMS is traded in the NASDAQ over-the-counter market under the symbol AMSY. AMS' core strengths are its expertise in systems development and implementation, large-scale technology integration, change management, and e-Business transformation.
BISYS	2000	An outsourcing company for more than 11,000 financial institutions and corporations, BISYS's TotalPlus products and services offer transaction processing and document imaging (it is a leading provider). The company also offers mutual fund and retirement plan distribution, administration, and fund accounting services. BISYS is also a major distributor of life insurance, annuities, group health, and long-term care products; Eighth year as a public company; fastest growth = Insur & Educ Serv, nation's largest independent distributor of life ins and industry service provider—supports 100,000 ins agents BISYS is the premier single-source integrator of banking, investment, and insurance solutions, uniquely positioned to leverage its outsourcing platforms across these business lines.
CACI	2000	CACI International has all sorts of cures for high-tech ills. The Arlington, Virginia-based company provides a host of information technology (IT) services and products in areas such as systems integration, e-commerce, debt management, and simulation. It also makes software and database products for use in marketing. The US government accounts for 80% of sales; the Defense Department accounts for 51%. The company also serves local and state governments and commercial clients. It has more than 70 offices in the UK and the US. In 2000 CACI acquired government services specialist XEN Corporation (systems engineering and IT services) and CENTECH (network services and e-commerce) as well as the network services and related assets (Federal Services Business) of net.com.

COMPAQ	2001	**Bullish on Mobile Computing** Speaking at Compaq's annual meeting for analysts, CEO Michael Capellas outlined his vision of a world in which "all kinds of devices" will access the Internet over an expanding grid of servers. With the rise of wireless handhelds, phones and pagers that can access the Internet and interface with multiple servers, a change is taking place. According to Capellas, in the new distributed computing age, PCs won't remain the primary devices accessing servers. Instead, servers will make data available to a wide range of machines, including PCs, handheld computers, mobile phones, pagers and Internet appliances via wired and wireless connections. "The world is going back to distributed computing," he said. "I really do believe this is the foundation of how the world will look." Internet connections inside cars will become prevalent as well, he said. "The wireless Internet will continue to make things change very rapidly. It won't be more than a couple of years before virtually every car has Internet access built in." As a result of the changing environment, Compaq sees opportunity in storage, Web-content serving, home networks and home entertainment.
Convergys	2000	In February 2001, Convergys acquired Keane's technical support centers in Tucson, Arizona, and Kirkland, Washington, which together employ approximately 1,000 people. These two technical support centers currently provide world-class, integrated, technical help desk support services for leading global firms in high tech software and hardware as well as financial services. Both the Kirkland and Tucson centers became part of Convergys Corporation.
CSC	2000	Nichols Research acquisition (Nov 99); multibillion IRS contract [PRIME, dec 98] not called OS, not included; 32% of accts receivable were from fed customers; no single commercial customer accounts for more than 10% of revenues
EDS	2000	EDS reported all-time high contract signings for 4Q 2000 and the full year. For the quarter, the company won contracts totaling $15.8 billion, up 41% from $11.2 billion a year ago and a record for the eighth consecutive quarter. For 2000, the total value of EDS' contract signings increasad 31 percent to $32.6 billion from $24.9 billion in 1999. EDS enters 2001 with a backlog of signed business now approaching $80 billion. Fourth quarter operating margin increased to 10.5% from 9.6% a year ago, positioning the company to achieve its target of a 10% operating margin for 2001. ROA improved to 16% from 13.8% a year ago. In the government sector, where the total value of contract signings was up 622% globally in the quarter and 380% for the year. EDS won the $6.9 billion Navy and Marine Corps Intranet contract, the largest IT services award ever by the U.S. federal government as well as a $713 million contract expansion with the UK government's Employment Service to provide an E-enabled system to link employers with available jobs to citizens seeking employment.
ENTEX	2000	Acquisition in March 2000: the combination of Siemens IT Service and ENTEX will generate nearly $2.2 Billion annually and employ approximately 13,000 people. Siemens: 152 years old; 443,000 employees in 193 countries; $75 billion sales worldwide (FY99); 7th largest private sector employer worldwide. Siemens USA = $14.8 billion in revenue; 63,900 employees; 26+ operating companies; HQ in NYC, NY Siemens IT services worldwide: $1.7 billion revenue; 8,000 employees; Provide services in over 100 countries; HQ Munich, Germany;#2 in Europe Goal: to become pre-eminent Managed Services Provider ENTEX offer today: Outsourcing; Network & Distributed; Computing Services; Desktop Support In 1998, ENTEX had total rev of $8.5 billion + 18,000 employees; primary offer: desktop services

Exult	2000	"Exult is the first company to offer comprehensive human resources (HR) business process management services for Global 500 corporations." IPO on 2 June 2000 yielding proceeds of $60 million. EXULT's Web-enabled human resources services include offerings such as employee communications, employee development, organization, payroll, and recruiting. Although BP Amoco became EXULT's first client in 1999, EXULT since has agreed to provide services to Tenneco and Pactiv. Top Competitors: Administaff, ADP,HR Logic. Nov 21, 2000 --Exult lands $1 billion BofA deal--In a contract believed to be worth about $1 billion over ten years, Exult Inc. finalized a deal Tuesday to provide online services to Bank of Americe Corp. employees around the globe. As part of the agreement, first announced in October, Charlotte, N.C.-based Bank of America is acquiring 5 million shares of Exult (Nasdaq: EXLT) common stock and a warrant to purchase an additional 5 million shares. The deal was to bring in about $55 million to Irvine, Calif.-based Exult. Exult has only four clients under contract for its HR business process management services and it is still implementing the largest two of our process management contracts. Executive officers, directors and their respective affiliates beneficially own approximately three-quarters of our outstanding Common Stock. As a result, these stockholders, acting together, have the ability to control matters requiring stockholder approval, including the election of directors, and mergers, consolidations and sales of all or substantially all of our assets. These stockholders may have interests that differ from other investors and they may approve actions that other investors vote against or reject actions that other investors have voted to approve. In addition, this concentration of ownership may also have the effect of preventing or discouraging or deferring a change in control of Exult, which, in turn, could depress the market price of our Common Stock.
Fed Data / Logicon [see Northrup Grumman]	2000	Oct. 31, 2000 – Northrop Grumman Corporation completed the acquisition of Sterling Software (U.S.) Inc., known as the Federal Systems Group, for $150 million in cash. The company provides IT services primarily to the federal government's defense and intelligence agencies. Feb. 1, 2001– Northrop Grumman Corporation extended pending tender offer for Litton Industries Inc. (including Litton / PRC) from Feb. 2, 2001, to March 1, 2001.The offer is being modified and extended in accordance with the terms of the merger agreement announced on Jan. 24, 2001. Logicon, a wholly owned subsidiary of Northrop Grumman, plays a leading role in providing information technology services to the Federal government through its ANSWER and Millennia programs with the General Services Administration. It is also part of a team working with the Internal Revenue Service to modernize the nation's tax system.
Fiserv	2000	The US's #3 processor of financial data (Electronic Data Systems and First Data are first and second), Fiserv provides check processing, software development, and securities clearing services to some 10,000 banks and thrifts, credit unions, and mortgage banks
Getronics	2000	With its purchase of the US' Wang Laboratories, Amsterdam-based Getronics has become one of Europe's largest international information technology (IT) providers (IBM and EDS lead the pack). Getronics' operations are divided into Business Solutions & Consulting (consulting, software services, and IT products and services for finance and industry) and Systems Integration & Networked Technology Services (network installation and management, systems integration). The company also distributes third-party computer and networking products. Finance is Getronics' largest market, accounting for about a third of sales. About three-quarters of the company's sales come from Europe, the Middle East, and Africe. Acquisitions, the largest of which was Wang Laboratories at nearly $2 billion, propelled Getronics beyond its European roots. The company continues to globalize its services revenue base while lowering product sales. By 2002, mgmt aims at deriving 25% of revenues from Business Solutions and Consulting (including Wang). 6 Feb 2000 - Shell Services International (SSI), the IT-services arm of the global energy company, has awarded Getronics a multi- million Euro partnership to create and

		maintain a common unified desktop computer and server environment across the world wide operations of the Royal Dutch /Shell Group (Shell). Shell's Global Infrastructure (GI) project covers 90,000 workstations at over 1,000 sites in over 135 countries. Shell's IT-infrastructure is one of the broadest in the world. Getronics has been contracted to install the new common environment and provide the necessary maintenance and support. The three-year contract is worth initially approx. € 75 million.
Keane	2000	Keane's services include custom software application development, system design and implementation, and e-commerce application integration. Planning services, such as organizational design and IT consulting, are offered through its Keane Consulting unit (formerly the separate divisions of Bricker & Associates and Amherst Consulting). The manufacturing industry accounts for 21% of sales. Keane also operates a unit dedicated to health care services. The company's client list includes IBM, General Electric, AT&T, J.P. Morgan Chase & Co., BMW, and Ford. Upbeat Keane To Sell Help Desk, Restructures - At a time when many IT services firms are releasing low-revenue expectations, IT consulting firm Keane is deploying a restructuring plan that it estimates will let it achieve fourth-quarter 2000 revenue of about $219 million, which is on target with analyst expectations. Without disclosing many details, president and CEO Brian Keane said Monday during a teleconference with analysts that the company is selling its help-desk business and has closed three of 10 slow-growing branch offices and consolidated the rest into six offices. "Help desk is a capital-intensive, low-margin business that requires volume and scale to be profitable," Keane said. The help-desk operations performed "just above breakeven in 2000," he added. Through the sale of its help-desk business, which is expected to close by the end of February and is subject to customary approvals, Keane expects to achieve a one-time gain during its first quarter of 2001, but the company didn't specify how much. Securities analysts applauded the move, saying the staffing operation was a slow-growth, low-margin and capital-intensive business. The company is expected to incur a one-time charge of $13 million to $15 million during 4Q 2000, which closed Dec. 31, because of the consolidation of its branch offices. Once help-desk and other underperforming businesses have been eliminated, Keane estimates it will achieve revenue of $880-920 million for FY2001. The consulting firm plans to concentrate its efforts on application development and management outsourcing, consulting, and enterprise-systems integration.
Northrop Grumman	2000	In 1999, strong federal wins pushed Northrop Grumman a top-ten spot among federal IT vendors, based on about $621 million in IT-related contract obligations. During 1998, Northrop Grumman integrated its Data Systems and Services Division with Logicon, which it purchased in 1997. The integration included the re-engineering of the unit's business development processes. As the IT division for Northrop Grumman, Logicon pulled in $1.44 billion in 1999 revenue compared with $1.08 billion in 1998. Among the 1999 highlights for Logicon was the beginning of work on the five-year, $2.2 billion Joint Base Operations Support Contract that a Logicon-led team won from NASA and the Air Force to provide base operations and launch support functions at the Kennedy Space Center and Patrick Air Force Base in Florida. The acquisition of Data Procurement Corporation Inc. of Laurel, Md., added another 7 percentage points to Logicon's growth rate. DPC primarily provided IT outsourcing services to Department of Defense and intelligence agencies. The acquisition brought $60 million in annual revenue to Logicon and another 180 employees, bringing Logicon to 12,000 employees overall. Both the DPC and Inter-National Research Institute acquisitions strengthened Logicon's position in the defense and intelligence areas, which will encompass bigger markets in the coming years as agencies in those areas look to outsource more of their information technology needs. In 1999, 58% of Logicon's business was with the Defense Department, 9% with federal civilian agencies, 10z5 with commercial customers, 2% with state and local governments and 0.4% with international governments. The target business mix in 2006 should be 49% Department of Defense, 26% federal civilian, 11% commercial, 11% state and local and 3% international governments.

OAOT	2000	Founded as a privately held company in 1993, OAO Technology Solutions, Inc. became a publicly traded company in 1997, trading on NASDAQ under the symbol OAOT. The information technology (IT) company provides services and staff to large companies that outsource portions of their operations. IBM accounts for three-fourths of sales; Compaq for 16%. Through its four business lines, the company operates service centers, manages distributed systems, develops and maintains software applications, and provides enterprise applications, e-business consulting, training, and proprietary software for managed-healthcare providers. CEO of OAT Corporation (private) is on the Board of Directors of OAOT. [See November 2000 letter to shareholders from Greg Pratt, CEO of OAOT. In 1Q 2000, OAOT reported 150% revenue growth in its new business sector, inclusive of Application Service Provider (ASP) services, a healthcare proprietary software solution, custom software application and maintenance, eBusiness systems integration, and IT consulting.
	Prior	OAO Technology Solutions had its beginnings as the Commmercial Systems Group, a division of OAO Corporation. Founded by Cecile D. Barker in 1973, OAO Corporation initially provided aerospace engineering services in support of an early NASA program, The Orbiting Astronomical Observatory, from which OAO derived its name. After years of demonstrated excellence in providing information technology services to the U.S. Government, OAO Corporation extended its services to the commercial sector in 1993 with the establishment of its Commercial Systems Group. In 1996, the group spun off and became incorporated under the name OAO International Corporation, and later changed to its current name, OAO Technology Solutions, Inc. OAO Corporation continues separately as a successful corporation providing quality service to the government. In 1997 with its own board and leedership, OAOT went public, becoming a Safeguard Scientifics, Inc. (NYSE: SFE) partnership company, and currently trades on NASDAO under the trading symbol, "OAOT".
Perot Systems	2000	Perot Systems is primarily focused on four industries: financial services, healthcare, energy, and travel & transportation. Perot Systems also serves the communications and media and manufacturing industries. Perot Systems' growing list of services include consulting, systems integration, data center management, and digital marketplace design. It focuses its support on specific markets, including energy, financial services, health care, and travel. Instead of fixed fees, the company is compensated for services based on customers' results. Clients include Swiss bank UBS (30% of sales), medical supplies distributor Owens & Minor, and Bank of Ireland. Founder Ross Perot returned as CEO in 1998. Among his changes: revoked health benefits for same-sex partners (a policy instituted in his absence) and reinstated drug tests. Perot's decision to transfer back-office operations onto the Web cut costs and significantly improved net income. Perot Systems went public in 1999; 90% of amployees (known as "associates") own stock. Ross Perot, Sr. owns 35% of the company. Meyerson owns 6%. Founder Ross Perot passed the CEO position to his son Ross Perot Jr. in 2000. Perot Jr is chairman of HCL Perot Systems (HPS), a joint venture formed in March 1996 between HCL Technologies, one of India's largest information technology groups, and Perot Systems. In January 2000, Perot Systems sold its 40% interest in Systor to a subsidiary of UBS. The ten-largest clients represented 65% of revenue at year-end 1999, of which UBS represented 30%. July 2000 - KPN Royal Dutch Telecom and Perot Systems announced the formation of a company to develop telecommunications industry-focused applications. The strategic objective is to develop, implement and integrate front-end applications and customer service technology for KPN, its subsidiaries and major organizations within Europe. The new company will focus on using the Internet, Wireless Application Protocol (WAP) and call center applications to develop applications for both Business-to-Business and Business-to-Consumer markets. With customers reducing spending, the company said it now believes revenue from existing contracts will shrink beginning in F2Q 2001. Management expects sales for

		2001 to expand just 8% to 15% above last year's $1.11 billion. Operating profit, excluding charges, is expected to increase 20%. The company struggled last year after two large customers either canceled or reduced computer-outsourcing projects. In its current quarter, Perot will take a charge to earnings of about $20 million in F1Q 2001 to complete its restructuring. Perot is laying off more than 200 employees and consolidating six marketing groups into four.
Raytheon		Raytheon's IT outsourcing business is peripheral to is aviation-related work. The facilities management unit, Raytheon Technical Services Company (RTSC) provides a variety of support services for defense, federal, and commercial customers worldwide. It specializes in the management, operation, and maintenance of customer facilities, equipment, and systems; logistics and life-cycle support; overhaul and repair depot operations; engineering, logistics, and personnel support; space and earth sciences; test range support; and privatization of government services. RTSC is a primary operator of Department of Defense ranges and provider of technical support services to the Federal Aviation Administration. Raytheon's Outsourcing Services organization provides large-scale outsourcing and remote engineering services for Raytheon and other companies worldwide. With employees in 50 states and 31 countries, the Outsourcing Services organization works to identify a client's non-core tasks. Then it determines opportunities to redeploy the staff that supports those non-core tasks, allowing the client to concentrate on its core business. In recent years, Raytheon provided operational oversight for more than 20 major outsourcing activities, transitioning over 5,000 people from their former employers to the Raytheon family.
SAIC	2000	SAIC's acquired Boeing Information Services in July 1999. Which was second largest acquisition ever for SAIC. The Boeing unit brought with it strength in telecommunications and network management capabilities. The Boeing buy also included a large contract with the Defense Information Systems Agency, making SAIC a formidable network management vendor. Since SAIC acquired the unit, its revenue is running at an annual rate of about $280 million. On February 12, SAIC's Strategies Group acquired Bunyard Enterprises Inc. (BEI) of Alexandria, Va. BEI, a senior-level government and industry consulting firm, supports top defense, aerospace, engineering and research organizations worldwide in the public and private sectors. BEI will become a division of SAIC's National Security Studies/Strategies Group. During FY (Sept)1999, BEI had 15 employees and annual revenues of $2.8 million. SAIC's Strategies Group has been providing government, commercial and international clients with integrated solutions to pressing and complex problems for more than two decades. It provides strategic consulting services in three key areas: Analysis, Operations and System Analysis and Strategic Integration. Group staff members assist clients with program management, communications, systems integration, and logistical support and by electronic decision analysis, group problem solving and collaboration, legislative analysis, modeling and simulation, and war-gaming to increase understanding of critical global issues. The Broadway & Seymour Group of SAIC specializes in providing financial services institutions with systems integration, consulting and technology-based products for enterprise customer relationship management.
UNISYS	2000	A key to UNISYS' success has been the federal group's client satisfaction rating. With an overall rating of 4.35 out of 5, the federal group ranked the highest of any Unisys unit, according to a Washington Technology survey. As Unisys continues its private-sector focus on e-commerce, or "e-@ction" as the company calls it, it looks for additional government markets that can take advantege of the solutions it has developed.
USInternet-working	2000	About 60% of USI's sales come from its iMAP service, which provides hosted applications via the Internet for midsized companies that don't want to invest in their own software. iMAP offers applications from vendors in the areas of e-commerce (BroadVision, Ariba), sales force automation and customer support (Siebel Systems), human resources and financial management (PeopleSoft), messaging (Microsoft),

professional services automation (Niku), and decision support (Sagent Technology). USi also offers information technology services. Customers include U S WEST (which owns 7% of USi), Legg Mason, and Clarus.

USI reported 4Q 2000 revenue of $37.3 million, including one-time fees of $3.2 million primarily related to the early termination of a contract with U S WEST. Total revenue for fiscal year 2000 was $109.5 million, a 208% increase over 1999. EBITDA loss for the quarter improved to $11.9 million, and the net loss amounted to $45.6 million, or $0.44 per share. For the full fiscal year the Company reported a net loss of $175.0 million, or $1.80 per share.

Additional highlights during the quarter include:

- 33 new service contracts, including clients such as The Port Authority of New York and New Jersey, Barclays Global Investors, American Battle Monuments, Magellan Health Care, The Longaberger Company, and Polyclad Technologies, a Cookson Electronics Company.
- $49.3 million in new service contract value.
- Gross margin for 4Q improved to $7.0 million, up 19%.
- Capital expenditures for the quarter declined to $26.0 million.

Management expects 1Q 2001 revenue to be approximately $35.0 million, or slightly above 4Q 2000 revenues prior to termination fees. Revenue for 2001 is expected to be approximately $180.0 million, a 64% increase over 2000 revenues. Management also expects 1Q 2001's EBITDA loss to decline to approximately $11.0 million. For the full year 2001, management expects the EBITDA loss to be in the range of $10-11 million, down from a $71.2 million loss for 2000. Management expects to reach EBITDA breakeven in 3Q 2001 and 1Q gross margin to improve modestly over 4Q. Gross margin for 2001 is expected to be approxi-mately 33-34%.

On average, the company is reaping $47,000 a month per client, a figure chief executive Andrew A. Stern said the company expects to continue to hover between $46-50,000 each month.

USinternetworking, which typically charges companies a flat-rate monthly fee for use of the software it provides, reported $56.9 million cash on hand at the end of the quarter, compared with the $81.1 million it had on hand at the end of 1999. The latest figure does not include about $95 million the company received in financing in January from a financing deal that it announced in November.

At the close of 4Q, USInternetworking, which has been fully operational for just over two years, reported long-term debt and lease obligations of $193.4 million, a slight improvement from $199.7 million at the end of the previous quarter.

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B

Appendix

A
User and Vendor Survey Questionnaires

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ☐ **Vendor** ☐ **Telephone**
- ☐ User ☐ On-Site
- ☐ Other ☐ Mail

Company: ______________________

Address: ______________________

____

____

____

City/State: ______________________

Zip: ______________________

Telephone: ______________________

Fax #: ______________________

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐

Interviewer Initials ☐☐☐

Interview Date. ☐☐|☐☐|☐☐

QC Initials ☐☐☐

QC Date ☐☐|☐☐|☐☐

Data Entry Initials ☐☐

Data Entry Date ☐☐|☐☐|☐☐

Company Type: ______________________

Annual Revenue: ______________________

Employees: ______________________

Total IS Budget: ______________________

Total # IS Staff: ______________________

Respondent(s):Name ______________________ Title: ______________________
Phone/Ext. ______________________ Email: ______________________
Role in Project: ______________________

Referrals:

____

____

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

   ____

   Collect related demographics

2. What is your role?

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

   Comment______________________

3a. Also, what proportion of your company's business, if any, is the U.S. federal market.

   Comment______________________

B. Priority Questions

4. In which vertical industries do you see the best growth potential for IT outsourcing?

   Comment______________________

5. Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments____

____

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments____

____

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment ____

____

8. What important changes do you see at work in the outsourcing market today?

Comments ____

____

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments ____

____

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments ____

____

11. What process do you use for computing the cost of contract bidding?

Comments ____

____

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

Comments ____

____

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

Comments ____

____

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

Comments ____

____

15. What is your policy toward dealing with unions? (How important?)

Comment ____

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comments ____

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comments ____

____

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comments ____

____

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comments ______________________________

____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comments ______________________________

____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ______________________________

Phone #: ______________________________

Email Address: ______________________________

Thank you for your time and consideration.

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❐ Vendor ❐ **Telephone**
- ❐ **User** ❐ On-Site
- ❐ Other ❐ Mail

Company: ______________________

Address: ______________________

____

____

____

City/State: ______________________

Zip: ______________________

Telephone: ______________________

Fax #: ______________________

Project Code/Catalog No. □□|□□□|□□□□

Interviewer Initials □□□

Interview Date. □□|□□|□□

QC Initials □□□

QC Date □□|□□|□□

Data Entry Initials □□

Data Entry Date □□|□□|□□

Company Type: ______________________

Annual Revenue: ______________________

Employees: ______________________

Total IS Budget: ______________________

Total # IS Staff: ______________________

Respondent(s):Name ______________________	Title: ______________________
Phone/Ext. ______________________	Email: ______________________
Role in Project: ______________________	
Referrals:	
______________________	
______________________	
Industry (User Interviews Only)	

Introduction

The purpose of this survey is to determine how customer attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of customer attitudes and preferences in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

   ____

   Collect related demographics

2. What is your role?

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

   Comment ______________________________

B. Priority Questions

4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)

   Comment ______________________________

5 To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?

   Comments______________________________

   ____

6 How do you determine which outsourcing vendors to invite to bid?

   Comments______________________________

   ____

7 How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?

   Comments______________________________

   ____

8 How important is the outsourcer' ability to attract and acquire your targeted staff (as part of a proposed contract)?

Comments____

____

9 What important changes do you see at work in the outsourcing market today?

Comments____

____

C. Additional Questions

10. Which type of outsourcing fits best your company's needs? (and why)

Comments____

____

11. How is outsourcing affecting your industry? (Effect on growth? Profitability?)

Comments____

____

12. How has your attitude toward IT outsourcing changed over the past year?

Comments____

____

13. Are you as attracted by outsourcing entire business processes as by offloading commodity transaction processing?

Comments____

____

14. Have you computed the contribution made by outsourcing to your company's overall profitability? (To cost-reduction of IT depart

Comments____

____

15. Do you prefer longer or shorter contract durations? (Why?)

Comments ______________________________

____

16. Have you in mind a ranking regarding which types of outsourcing are the most costly? (Reasons?)

Comments ______________________________

____

17. In relation to outsourcing, how sensitive are you to the issue of control, in general, and control of proprietary data in particular?

Comments ______________________________

____

18. How strong is your relationship with incumbent outsourcers? (Probability of sole-sourcing new contracts?)

Comments ______________________________

____

19. To what extent, if any, have union relations affected your desire or ability to outsource?

Comments ______________________________

____

20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comments ______________________________

____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ______________________________

Phone #: ______________________________

Email Address: ______________________________

Thank you for your time and consideration.

C

Appendix

A
User and Vendor Survey Results

Exhibit D-1 through C-4 that follow present results of INPUT's Vendor and User surveys both by respondent and by question.

Exhibit D-1

Tabulation of Vendor Interview Survey Responses by Question

2. What is your role?	
ACS Government Solutions Group [#8]	The respondent has been at ACS for two years. Prior to that, he worked at Wang and was part of the capture team that won the ODIN seat managemant contract. Most of his professional experience is on the DoD side of the market, especially in electronic warfare.
Applicast [#9]	Respondent has a background in IT management and systems integration for the midmarket. Applicast wants to replace the customer's "back office" by offering required functionality on a service basis.
COMPAQ [#18]	Respondent has primary responsibility for development of the outsourcing offerings for Compaq Global Services. He has 20 years in the business selling, delivering and building different approaches.
Convergys [#19]	Respondent is VP for marketing strategy and has responsibilities for both planning and implementation of sales globally. Also, he has done corporate planning with a focus on strategy. He joined Convergys in 1991 prior to its spin-off from Cincinnati Bell. (Convergys was formed from the CIBIS and Matrix units of Cincinnati Bell, which were the IT operations and marketing units.) Initially, Respondent was co-located in Fairfax, Virginia, with CIBIS' federal market unit. This assignment lasted three years, after which Cincinnati Bell decided to leave the federal market and concentrate on its present areas of expertise: billing, call center and customer care solutions for the telecom (mainly wireless), technology and financial services markets.
CSC (1) [#3]	Respondent has a high-level position in CSC's federal group, with responsibility for both civilian and DoD business.
CSC (2) [#5]	Respondent represents the "capture" side of CSC's commercial outsourcing business. The vendor has centralized all contract capture activities in one place—including some federal outsourcing. CSC tries to bring its vertical industry expartise to bear on the capture process, including in particular the federal, health care and financial services markets.

EDS [#21]	Respondent was a senior VP of Sales with 24 years of experience at EDS. Previously, he was president of the banking and financial services division (eight years); he ran the transportation industry group and, for four years, was in charge of the GM relationship on location in Michigan. He has been heavily involved in sales and business development in both the governmental and commercial markets. He has both a CPA and MBA-Finance educational background.
Entex IT Services [#13]	Respondent is a SVP for strategy at Entex IT Services. He has responsibility for planning, marketing strategy and is directly involved with the development of outsourcing proposals. At Entex, federal and commercial businesses are treated as a single entity. Respondent came to work at Entex in the U.S. after the Siemens acquisition. He has substantial prior experience with Siemens in Europe.
Fed Data [#17]	Respondent is a VP for IT management services with responsibility for Fed Data's work on ODIN and GSA seat management contracts. He worked on the original proposal development. Prior to that, he had IT managerial positions at the Kennedy Space Center and the Johnson Space Center. Overall, he has 20 years of experience in IT, virtually all in the federal market. At Fed Data, he has project management responsibility for the Peace Corps and Wright Patterson AFB outsourcing contracts. Overall, Fed Data is working with agencies that are playing "catch up" with the NMCI/EDS contract. They want to roll up smaller projects into a similar, large contract vehicle, but this will take some time. To date, Fed Data has won only smaller, discrete task orders.
Getronics [#10]	The respondent worked previously for Wang. After Wang's acquisition by Getronics, he became head of outsourcing for the federal group. He has 16 years of experience in the federal market (mainly at PRC) and two years of experience in the commercial market. Significantly, he stressed that the federal and commercial market sales teams are in continual contact, at least weekly, even though they have separate missions. Specifically, respondent has hands-on experience with the ODIN seat management contract. Currently, he is head of that group's Center of Excellence in Seat Management, which has a staff of about ten technical specialists. Getronics has several such Centers of Excellence—including one for Network Security, and another for E-Commerce. For Getronics, "government" means federal. The commercial division handles the few state and local government contracts that have been booked. The Center of Excellence serves as a technicel (Best Practices) as well as sales resource. Accordingly, respondent does get involved in the proposal preparation process and consults with business development staff on "alignment" of effort by agency. For Getronics, federal marketing consists primarily of determining which agencies offer the best prospects for new seat management business.
Independent Consultant	Respondent worked for 20 years at Digital Equipment Corporation in application development before joining CSC initially as a director IT for a business unit and working later as an account executive. In that role, she gained experience in the federal market by working closely with a major CSC client that was a major federal contractor. She has experience with "full-service" IT outsourcing as well as application development. This exposure to federal business provided experience with large, comprehensive IT outsourcing programs (albeit without any classified software development). Subsequently, she joined ACS where she had responsibility for application management outsourcing for new clients as well as the installed base.
Keane [#15]	Respondent is a VP with responsibility for external communications, including industry analysts, investor relations and other.
Keane [#6]	Respondent has 20 years of experience in the IT industry, including consulting. His background includes work at Wang where he managed outsourcing projects prior to coming to Keane. At Keane, he works for both internal and external clients. His outsourcing responsibilities include sales and delivery.
Litton/PRC [#1]	This respondent has a high level position in the company's outsourcing organization. Project managers report to him. He has overall responsibility for contract "capture" and management.

Lockheed Martin [#4]	Respondent has responsibility for IT outsourcing strategy and business development in the commercial Integrated Business Solutions (IBS) division. He also manages alliances and partnering relationships. He began his career at PMS in the insurance industry. All of this division comprises commercial client work. It does no federal business. Federal outsourcing is done through the Information Support Systems division, which provides technical services to government agencies.
Perot Systems [#22]	Personally, the respondent manages client relationships. As a company, Perot assists customers with aligning, managing and applying technology toward client business objectives. Respondent has been in the IT outsourcing field for five years. He began his career at EDS where he achieved Inner Circle Status as one of the top sales people globally. He now represents Perot System's Integrated Solutions Group and is one of the top sales people representing this group.
Raytheon [#7]	The respondent has been an observer as well as a participant in the outsourcing initiatives of various government agencies. At Raytheon, he played a key role in preparing the company's bid for the NSA's Groundbreaker contract. All of his professional experience has been in the federal market. Currently, Raytheon does less than 5% of its business in commercial markets.
SAIC [#20]	Respondent has recently moved into a very high level executive position with responsibility for all commercial, and some federal outsourcing business. This new position is more senior than that held by its predecessor and signals a significant reorganization of the vendor's approach to outsourcing—primarily by piercing the stovepipes between the federal and commercial markets. Respondent believes that commercial and federal outsourcing operations should be operated separately—but the units should be able to leverage each other's assets. Respondent has 30 years of experience in outsourcing, beginning at the federal division at UNISYS. As indicated above, he does not believe that a vendor operating in both markets can use the same sales force, but he does believe that the same technical staff can work in both markets. Beyond that, vendors need to pay attention to the differing cost accounting systems used in federal and commercial markets
The Outsourcing Institute [#2]	The respondent has a broad background in IT outsourcing, having worked at UNISYS, AT&T Solutions, Cap Gemini and other firms prior to The Outsourcing Institute. Previously, he worked with Victor Millar, co-founder of Andersen Consulting, who is now CEO of VC Fund. He has been selling IT outsourcing deals since 1982.
UNISYS [#16]	Respondent is a Manager of Market Development & Planning. He has worked with leading providers of outsourcing to both commercial and public-sector marketplaces.
USInternet-working [#14]	Respondent is a VP for public sector sales. However, prior to assuming this position in spring 2000, he had extensive experience in the commercial IT outsourcing market, beginning with CSC in 1974. At USI, his role includes business development, sales, staffing, and new client capture in the public sector, which at USI includes all of higher education.
3. Please indicate the nature of your experience with outsourcing (IT or otherwise)	
ACS Government Solutions Group [#8]	ACS considers itself a "pure play" outsourcing vendor whose vendors derive virtually in their entirety from IT outsourcing. Overall, the company's $2 billion revenue mix is two-thirds commercial, one-third public sector, which includes federal (both civilian and DOD) as well as state & local. In the Government Solutions Group alone, revenues are split between IT solutions ($300-400 million annually), ACS Defense ($100 million annually) and Business Application Systems ($100-200 million annually). The state & local government division does about $600 million annually; another $100 million of state & local business is done outside of the Government Solutions Group.
Applicast [#9]	Menlo Park-California-based Applicast is an Application Service Provider that specializes in serving the midmarket, high-tech industry ("the premier, total-solution [ASP] for aggressive-growth companies"). Recently, it merged with Englewood, Colorado-based Agilera ("the first ASP to offer a combination of hosted solutions and value-added services"). Applicast defines "midmarket" loosely as comprising companies with $0-1 billion in revenues. In a crowded field, Applicast differentiates itself from its competitors by eschewing "legacy baggage," i.e., the high overhead resulting from established infrastructure, staff consultants, etc. It was formed as a new organization specifically to serve the new ASP market. One key element of success has been to partner effectively with complementary companies.

COMPAQ [#18]	Compaq Global Services has been providing outsourcing services since the late 1980s.
Convergys [#19]	Presently, Convergys is divided into two divisions, Information Management Group (IMG) and Customer Management Group (CMG). The IMG division represents about 60% of revenues, derived primarily from customers in the wireless telecom industry. Overall, Convergys believes that it is the dominant U.S., if not global, vendor of comprehensive customer care and billing solutions for the telecom industry. It also serves the "technology" industry, which it defines to include ISP and related computer HW vendors. In financial services, it serves banks and other institutions primarily in connection with the telecom industry and call center operations. Convergys also has a large share of cable and broadband provider billing operations. Company does business in Europe and Latin America and is now in the process of setting up several offshore IT centers (including in Israel) from which it will serve global clients. A Latin American center is being set up with a Brazilian partner on a Build Operate Transfer (BOT) model whereby Convergys will operate the center initially, but ownership will revert over time to the local partner. *Currently, Convergys does not do business at all in the U.S. federal market.* In the 1980s, CIBIS [predecessor to Convergys] made acquisitions in order to enter the federal market, especially in the facilities management segment. By the 1993-94 period, management decided to divest all federal market operations in order to focus entirely on providing billing and call center services to commercial customers. Currently, the company is divided into two divisions, IMB = Information Management Group [formerly CIBIS]; and CMG = Customer Management Group [formerly MATRIX]. These hed been part of Cincinnati Bell prior to the Convergys spin-off. Convergys offers both products and services. These can be bundled into large, comprehensive outsourcing contracts. Alternatively, customers can purchase specific business solutions that they implement themselves. Convergys has little proprietary. Rather, it markets value-added, proprietary packages of third-party software that has been "pre-integrated" to work together. This proprietary architecture is important because of the growing complexity in the telecom market of the "rating of events" problem. This refers to the difficulty of assembling disparate kinds of transaction data from around the world, applying the correct billing and rate information in order to assure a high level of customer service to client's customers.
CSC (1) [#3]	Federal market work comprises about 25% of CSC's total revenues. This has declined at times to 23%, but the target remains 25%. Another 3-5% of total revenues derives from work in the state and local levels of the public sector. Fifteen years ago, federal business comprised 70% of CSC's total revenues, including outsourcing and facilities management. Overall, outsourcing comprises 38%. Historically, CSC leveraged its work for General Dynamics to enter the federal market. The key to success in this market has been strong program management skills, good software development capability, and skill in dealing with complex systems and security environments. Another key to success: thorough knowledge of agencies and customer needs.
CSC (2) [#5]	CSC does a wide range of types of outsourcing, including Web-hosting, applications management (ex. health care and financial services) and is a leading provider for the insurance industry (ex. recent acquisition of Mynd, which only reinforced a prior position of strength). Last year, there was a noticeable trend toward "downmarket" outsourcing (transaction processing), but this was likely an anomaly.
EDS [#21]	Respondent explained that EDS has currently four operational divisions: Information Solutions (which includes traditional outsourcing and comprises 80% of EDS' total revenues); • A.T. Kearney, high-end management consultants; • E-solutions, which does Web development and related Internet work; • Business Process Management, which includes a large health care, claims-processing operation along with other commodity data processing.
Entex IT Services [#13]	Currently, public sector comprises only 10% of Entex's total revenues, commercial work represents 90%. Of public sector work, only 10% derives from the federal government—the rest, from work for state and local government clients. The company's primary products are desktop services and network management.

	Background of the Siemens Acquistion Last Year of Entex At present, Entex is a wholly owned subsidiary of Siemens Business Services (SBS), based in Germany. Entex operations are integrated fully into Siemens on a global basis. SBS is divided into SBS consulting and IT Services. Entex is part of the IT Services group.
Fed Data [#17]	Fed Data is now a part of Logicon, which is Northop Grumman's IT services division. (When the Litton/PRC acquisition is completed, part of it will join Logicon, and part will go directly to Northrop Grumann. While Fed Data and Logicon have a few commercial clients, 90% of their work is for federal clients. Of that, only 10% comprises IT outsourcing. According to respondent, commercial IT work at Fed Data is done by completely separate work groups. There is virtually no synergy between the federal and commercial market teams. The company's commercial work was described as "oddball" projects that included help desk and network management work—but no data center outsourcing. Currently, Fed Data has a backlog of about $20 million in annual revenue from signed contracts. By comparison, Logicon had $400 million in 1998 and has grown to $2.1 billion today. On the top level, Northrop Grumann has annual revenues of $10 billion; Logicon represents $2.5 billion of this (including Fed Data). Litton/PRC has annual revenues of $5.5 billion.
Getronics [#10]	Getronics does $3-4 billion in annual revenues worldwide. Of this, the Government Solutions Group in the U.S. contributes about $400 million, or 10% of the total. The corporate target is to grow this business to $1 billion over the next 5-6 years through organic growth and acquisitions. Seat management comprises about 10-15% of the Government Solutions Group's revenues; the remaining 85-90% consists of a variety of professional services (non-outsourcing). According to the respondent, the term "seat management" is essentially a federal-market-specific term. In the commercial market, "desktop services"—the nearest equivalent—usually includes network services, call center and other kinds of work. For some federal customers, seat management contracts are used as a back door vehicle to buy hardware when they can't access a capital expenditure budget. HW purchases are built into the seat management contract under the guise of periodic equipment "refresh" and using existing GSA schedules. Federal budget politics often requires agencies to spend money on a time & materials basis even when this is contrary to the best interest of both the government and the taxpayer. Partly for the reasons noted above, the government's concept of seat management is evolving and becoming increasingly comprehensive. Eventually, it will become something like BPO in the commercial market. This process will take 4-5 years. At present, they are putting out to bid increasingly extensive pieces of work.
Keane [#15]	Background on Keane As a percentage of total company revenue, Keane's public sector business represents about 15%. Overall, about 60% of the company's turnover derives from IT outsourcing of various kinds. Keane has four main business divisions: • Application development and management (9% is outsourcing) • E-solutions projects (9-10% is outsourcing) • Business innovation and consulting (1% is outsourcing) • Managed IT Keane earns about 38% of its revenues from "e-solutions projects." According to respondent, Keane has never lost an outsourcing customer based on poor performance: "[Outsourcing] is not a market for people who can't perform." Of Keane's total revenue, 60-70% derives from multiyear outsourcing contracts.
Keane [#6]	Outsourcing comprises about 50% of Keane's total revenues. Of that, work for commercial clients represents about 80% of outsourcing revenues; work in the federal market represents about 20% of total outsourcing revenues. Management believes that this is an optimal diversification for the company. Overall, the federal unit represents about 10-15% of total company revenues.
Litton/PRC [#1]	Depending on one's definition of outsourcing, Litton/PRC does about $175 million annually in outsourcing, representing about 95% in the federal sector and the remaining 5% in the non-

	federal public sector. On a dollar basis, outsourcing accounts for about 25-30% of total revenues. Parent Litton Industries does commercial outsourcing, but those activities are totally separate from the Litton/PRC unit. [A contract at Federal Data/Logicon speculated that—after the Northrop Grumman acquisition of Litton Industries, Litton/PRC would be folded into the Fed Data/Logicon unit. However, this respondent believed that the it would likely be joined directly to Northop. The matter is as yet unresolved.] Litton/PRC has been active in the staff augmentation and [physical] asset management. Currently, the company is most active in the following outsourcing markets: • Seat management • Network management • Help desk • Application management • Storage on demand (SAN - storage area networks) where Litton/PRC owns and operates the storage servers for clients *The company is attempting to diversify away from federal market seat management and into the state and local government markets, especially for data storage, which is experiencing huge growth.* In the area of asset "takeover" or management, company has only one contract for $15 million (a GSA seat management contract). The storage-on-demand business is still small, but Litton/PRC expects "tremendous" growth in this market.
Lockheed Martin [#4]	Of Lockheed Martin's total revenues, IT outsourcing plays a small role, comprising less than $1 billion annually. This is split about half federal, half commercial. The division does NO transaction processing. The company also does some business in the state and local government market segment, which amounts to about $400 million annually.
The Outsourcing Institute [#2]	**Background on The Outsourcing Institute** It is a private organization that was formed in 1993. It owns a Web site. The purpose of the organization is to become a primary resource for the outsourcing industry, along the lines of a professional association, but with practical benefits. The Institute hosts Forbes magazine events and co-sponsors publications. It aims to be a neutral clearinghouse for information on best practices, events, etc. It coordinates with DCI on participation in large, industry events. It has no paid membership, but has built a DB ("Accelerator") of 24,000 industry participants—including buyers, sellers and "influencers." The organization derives income from consulting fees and provision of various kinds of marketing assistance. In addition, the Institute receives income from finder's fees generated by helping vendors win new outsourcing business for vendors. (Typically, 8-15% of total contract value is spent on deal marketing.) Currently, the Institute maintains an Outsourcing Index, which is the core of its clearinghouse efforts. The organization has a staff of 18 people, headed by its founder, Frank Casale. Initially, Michael Corbett was a principal in the organization, but he subsequently founded his own company, Michael Corbett & Associates, which is an outsourcing consultant. At present, the Institute is seeking VC funding. In his opinion, generally, the federal and commercial outsourcing businesses of vendors are operated in complete independence. He regards this as unfortunate. *The Accelerator*—offered on the Institute Web site—was conceived as a start up portal for the exchange of data by all participants in the outsourcing process.

USInternet-working [#14]	At USI, the sales force is organized according to geographical territories. Within each territory, there are multiple VPs with differing responsibilities within the region. Within regions, there is some focus on specific vertical industries depending on which companies are prominent in the area, rather than on a corporate strategy for such diversification. In fact, USI wants to market to all vertical industries because it positions its offer as essentially a "horizontal" service that should be attractive to all companies that share certain non-industry characteristics. Beyond that, USI wants to come to market by highlighting the spacific applications that it offers, rather than its vertical industry expertise. Nevertheless, the company does enjoy some industry-specific advantages in regard to BroadVision for retailing and PeopleSoft in insurance. **Market Position** In respondent's view, the advent of the ASP model represents a significant evolution in the IT industry. He believes that vendors such as CSC, EDS and IBM Global, on the whole, target very comprehensive contracts that include data centers, networks, applications, etc. In contrast, USI targets ONLY the demand for specific apps.
3a. Also, what proportion of your company's business, if any, is the U.S. Federal market?	
ACS Government Solutions Group [#8]	Within the federal market, ACS targets specific agencies as their best sources of business growth, ranked according to the best match between ACS areas of expertise and agency requirements. • Other considerations include: • Where do we have the best technical solutions? • Where can we find a "level playing field"? (In some agencies, the incumbent is so well entrenched that it is virtually impossible to win new contracts.) ACS considers itself to be the top vendor in the network security market segment, as evidenced by work for NASA. Also, ACS considers itself to be the biggest factor in the imaging market where it does $400 million annually. In seat management, ACS has 300,000 seats under management.
Applicast [#9]	To date, Applicast does no business in the federal market. Management considers the public sector (including federal) market unattractive because of excessive bureaucracy and the slow pace of change. Applicast wants to work with customers that are ready to transform themselves, and quickly. Applicast management perceives the public market as lacking in opportunity to achieve innovative implementations in a short timeframe. Conversely, it is seeking to build a client base among fast-growing, innovative commercial companies. It would rather expand into complementary vertical industries. For this, success hinges on the ability to understand a customer's industry-specific requirements. It is not enough to propose generic, or standardized, horizontal software applications (such as plain-Vanilla PeopleSoft). Applicast sees the most profit and the best growth prospects in "upmarket" solutions that fall within the category of Business Process Management (BPO). Applicast has no proprietary software, but does have proprietary, industry-specific packages or templates that consist of pre-configured, complementary software applications. It is critically important to "speak the customer's language." Applicast is not a BPO vendor, but believes that it has a BPO focus, or orientation.
COMPAQ [#18]	From an outsourcing perspective, very little of Compaq's business is in the U.S. Federal.
Convergys [#19]	Convergys doesn't believe there is a place for it in the federal market because it specializes in mission-critical applications. Its customers prefer its solutions because they are field-tested. Respondent doesn't believe that the kind of work that the company does has a wide application in the federal market, except perhaps at the IRS. In his view, "the federal market is a world unto itself." He believes that sales staffs need to be different (it is more difficult to send federal salesmen into the commercial market). All parts of the organization, including technical, sales and office staffs need to adapt to the characteristics of each market—which differ significantly.

CSC (1) [#3]	Federal market work comprises about 25% of CSC's total revenues. This has declined at times to 23%, but the target remains 25%. Another 3-5% of total revenues derive from work in the state and local levels of the public sector. Fifteen years ago, federal business comprised 70% of CSC's total revenues, including outsourcing and facilities management. Overall, outsourcing comprises 38%. Historically, CSC leveraged its work for General Dynamics to entar the federal market. The key to success in this market has been strong program management skills, good software development capability, and skill in dealing with complex systems and security environments. Another key to success: thorough knowledge of agencies and customer needs.
EDS [#21]	Respondent confirmed that 14% of total EDS revenues derive from the U.S. federal market and 58% overall from the U.S. market. Of total global sales, 60% derives from IT outsourcing. An estimated 2% comes from the non-federal, U.S. state and local government market.
Entex IT Services [#13]	Entex participates in the federal market in both prime and subcontractor roles.
Fed Data [#17]	Respondent sees excellent long-term growth potential for increased desktop management business (task orders) from the DoD, Army and Air Force. These agencies are now trying to follow the example of the Navy's NMCI contract. While they don't anticipate any dramatic new budget allocations, the DoD appears increasingly willing to change existing budget allocations in order to roll up GSA task orders and other BPA contracts in to evermore comprehensive "bundled" large contracts for a wider range of work. In this context, respondent corroborated opinions expressed by other vendors to the effect that the federal government's entire IT infrastructure would be virtually obsolete in less than five years. This reality, along with the skills shortage, budget restrictions and pending retirements, would make IT outsourcing unavoidable.
Perot Systems [#22]	Perot Systems does no business at all in the U.S. federal market.
SAIC [#20]	Currently, 50% of SAIC's total revenues of $5.5 billion [2000; FYJan 31] derive from business in the federal sector, 50% from the commercial market. Of this,13% represents outsourcing. SAIC's primary vertical markets are: • The oil & gas industry (built around core, global contracts with BP an a large joint ventura, Entassa, with Petavesa, the Venezuelan oil company); • Utilities – built on core contracts with Entergy and the Scottish Power authority (SAIC's largest contract); • State and local government – built on the core contract shared with CSC for San Diego County, where SAIC is headquartered. (While the contract was announced as a CSC win, respondent commented that "SAIC brought CSC into the deal.") • Federal – built on core contracts with the FBI for data security and • SW engineering In addition, the financial services and manufacturing industries are also important to SAIC, but to a lesser degree.
USInternet-working [#14]	Commercial vs Public Sector Market To date, USI has only seven clients in the public sector, six in the federal market and one in state and local (the NY Port Authority). Currently, the company is focusing on potential business with the State of Maryland, which leverages its advantageous location in Maryland's state capital, Annapolis. Public sector business comprises only 5-10% of USI's total revenues. In the federal market, USI has chosen to partner with big SI vendors. Typically, these vendors do not want to make a large, new investment in hardware and find USI's remote app delivery an attractive alternative. From a marketing point of view, USI benefits from the extensive customer relationships of these top-tier vendors, e.g., PWC, EDS, IBM. USI believes that it is gaining valuable exposure through partnering. Regarding profitability, while it is true that federal contracts usually carry lower profit margins, their size tends to be larger, which serves as an off-setting factor. As a result, USI has taken no "profit haircut."

4. In which vertical industries do you see the greatest potential for IT outsourcing?	
ACS Government Solutions Group [#8]	ACS considers itself to be a "services company," which means that it wants to provide bodies and sell solutions. It wants to build on its experience with the ODIN contract. GSA seat management has not been very successful, but NASA's ODIN contract was structured differently. OAO and ACS each has responsibility for multiple NASA sites. Typically, seat management contracts are difficult because vendors must interact with a multiplicity of other vendors, as well as with civil servants. Respondent: "Give me an empty room, and would love to do seat management." Better are contracts where seat management is included along with networking and application services. The ACS Government Solutions Group works closely with its counterparts in commercial sales. Staff meets regularly, compares notes. Some prospects are marketed jointly and there has been much benefit from this close cooperation. The commercial culture provides depth of knowledge in the area of "best practicas." The federal market culture provides excellent depth of project management skills, technical discipline and rigor of methodology. In a few cases, commercial clients have been brought to see what is being done in the federal market. They have been so impressed that commercial deals were closed in the offices of the Government Solutions Group.
Convergys [#19]	As indicated earlier, respondent views the telecom, technology and financial services industries as the company's best growth prospects. Fully 80% of revenues are derived from the telecom sector. In the technology sector, customers include ISP, broadband providers, Dell and other IT hardware vendors. In financial services, the company works with banks primarily by providing call center services. It does no network or data center management. Respondent believes that the market for the kind of "end-to-end" solutions that Convergys offers is growing rapidly. Demand for customer service and billing solutions will only increase. Worth noting, Convergys also offers the third component of the billing/CRM-call center triad: CRM analytics, or knowledge management that converts the billing and transaction information into useful marketing data for customers.
CSC (2) [#5]	CSC sees the best opportunities for growth in its commercial IT outsourcing business in financial services (banking and insurance), manufacturing (esp. electrical) and other industries. Since mid-1998, the company has done relatively little work in accounting (other than Y2K-related). Overall, consolidation in the banking industry has been good for IT outsourcing, yet the end of Y2K spending depressed the volume of business. Now there is a powerful trend in play toward standardization, esp. in the areas of application management, or applications infrastructure. Customers want vendors to buy their data centers, run and operate them. In some cases, customer's want work done on their premises (whether they, or the vendor own the hardware); in other cases, customers either agree to having their work done remotely at the vendor's data center. Ultimately, customers become comfortable with the idea of vendors acquiring and running their hardware, located on the customer's premises, while the vendor does work for third parties. This kind of flexibility greatly enhances the cost-effectiveness of deals to customers and the profitability of them to vendors. While our financial service customers tend to be headquartered in the U.S., their operations are global. So far, we do all work for them in the U.S., however, we are exploring the possibility of using offshore IT vendors as partners in countries such as India. No initiatives in this area have yet been implemented.
EDS [#21]	EDS sees the best prospects in the financial services, telecom, manufacturing, energy, and health care industries. In addition, the company finds the federal and state public sectors attractive along with transportation—especially the "emerging" transportation segments of air, car rental, and freight.

Entex IT Services [#13]	**Most Attractive Markets** Financial services (including insurance) and health care [a stronghold of Siemens] appear to have the most potential for Entex. Nevertheless, the company is active in almost all vertical industries. Sales and marketing are not organized by vertical industry. Entex believes that its primary offer, desktop services, is a horizontal product that can be sold in every industry to organizations above a certain size (3-5,000 seats). Overall, the IT outsourcing market is clearly moving "upmarket" toward more comprehensive contracts. Customers want relief from the burden basic IT operations and they want to advance an agenda that includes a transition toward e-business—and lower headcount. Cost-savings are less important than streamlining management structure.
Independent Consultant	Respondent believes that ASPs have good growth potential. Top-tier, experienced IT vendors can thrive in all verticals because many facets of the services required are really generic. As a result, vendors can leverage experience in one vertical to another. Although clients do expect vendors to offer reference clients in their own industry, this need not be a barrier. Truth be told, customers ALWAYS believe that their needs are unique (and you don't dare contradict them). This customer misperception is based on a lack of technical background. From a technology point of view, there is little significant difference between verticals. Having said that, ASPs are most attractive when they specialize on offering very well chosen selection of applications that industry-specific.
Keane [#15]	We see the best potential for commercial outsourcing business in the financial vertical (banking and insurance), utilities (esp. natural gas companies), health care, entertainment. Most important, in the commercial market the customer must have confidence in the vendor as a partner. At the same time, the customer expects the vendor to be profitable. Therefore, as changes are made to the original contract agreement, customers understand that costs can rise and they are willing to pay. All of this is much more difficult in the federal market. Often, FAR is used as an excuse to deny changes in the contract, or to pay additional costs. In the end, it is more difficult to make money in the federal market.
Keane [#6]	Keane sees excellent potential for growth of its public sector business, federal as well as state and local government. Beyond that, it sees good opportunity in financial services, insurance, manufacturing and utilities—which is currently experiencing unfavorable market conditions. Telco is another market for good growth. Keane does a lot of what it calls "backfilling" gaps in customer resources by deploying contract staff either on site, or at a remote location. (Sometimes "remote" is only a few blocks away from the customer's premises.) In addition, Keane sends customer work to its own "remote" data center in Halifax, Nova Scotia. Keane has done some deals to provide HR solutions and is strong in system integration. These markets remain attractive.
Litton/PRC [#1]	Financial Services, Manufacturing and Healthcare

Lockheed Martin [#4]	Respondent sees the best potential for new IT outsourcing business in the financial services and utilities industries. Utilities are particularly attractive due to deregulation and the turmoil surrounding changing market relationships. In terms of types of outsourcing, respondent sees the best growth potential in BPO work. Nevertheless, he believes that the IT outsourcing market is moving in two directions simultaneously, toward increasingly comprehensive as well as toward "low-end," specific-application services and transaction processing. The answer depends on who is making business decisions. CEOs think in terms of BPO ("big picture") or ASP ("BPO by the drink"). The IBS division has chosen NOT to organize around vertical industries. Instead, it targets large multinational customers that went to buy services only. IBS has no interest in acquiring customer assets or managing facilities. IBS can build e-business canters, but would prefer to do remote application management for clients who don't want to own their own data canters. Also, IBS would like to sell special solutions such as supply chain management. IBS does not believe in "building ahead of the curve," i.e., running the risk of excess capacity in either equipment or staff. It strives to stay just slightly ahead of demand. In this, and other ways, IBS benefits from its experience in both the U.S. and South America.
Raytheon [#7]	Primarily the oil & gas industry, telecom / IT, energy (including the utilities). Respondent believes that the utilities and telecom markets globally are very attractive because of continuing deregulation—which is even a factor in the U.S., as evidenced by California. More important, the utilities and telecom industries have an established billing system in place that reaches all businesses and consumers. This puts them in a very unique position. Other growth areas—financial services and manufacturing, to a lesser extent. While there is great potential for growth in all segments of both the federal and commercial outsourcing market, Raytheon targets in particular the intelligence agencies—all of which are watching the development of the Groundbreaker contract in order to decide whether to follow.
SAIC [#20]	Respondent sees the best growth potential in financial services, manufacturing (particularly for supply-chain-related work, and for facilities management work for companies like Bechtel and Fluor). He believes that IT outsourcing only represents about half of the total outsourcing market. The next largest segment is facilities management, both pure real estate and a sophisticated mix of real estate and IT. The last segment is HR management. [This split ignores manufacturing outsourcing.] In respondent's view, it is unfortunate that the federal and commercial sides of outsourcing management are usually entirely separate.
UNISYS [#16]	The public sector.

USInternet-working [#14]	In respondent's view, the ASP offer will be even more attractive to the public sector than to the commercial sector due to the coming wave of retirements of federal IT workers. In his view, the problems created by these retirements will be exacerbated because it will severely handicap the government's independent ability to develop and manage critical sw applications. In addition to the public sector, USI views the financial services (including insurance) and healthcare industries as particularly good prospects. Also, retailing looks promising because retailers are now accepting the need for new e-commerce strategies (that require specialized apps). Far from suffering from fallout of the demise of the dotcoms, USI enjoys an increasingly prominent and positive market position: "USI is being wooed by big systems integration vendors." USI considers itself to be the number one ASP in the industry, with special expertise in ERP (including Lawson, SAP and Oracle). In fact, less than 10% of USI's clients are dotcoms. Major federal agencies want to use the outsourcing model (Justice, Transportation, Agriculture). USI sees no effect yet from the TRAC anti-outsourcing initiatives in Washington. There are many counterpressures. In the end, the federal government will realize that it has no viable alternative to outsourcing because it will soon be unable to operate its own IT infrastructure. Enterprise software, such as PeopleSoft is relatively labor-intensive, and the federal civil service cannot attract sufficient numbers of skilled staff required to operate such applications.
5. Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?	
ACS Government Solutions Group [#8]	Some barriers to entry on the federal side include the following: • A vendor must be an incumbent at an agency in order to get a foot in the door. • You need to have established personal relationships—and you can't walk the hallways to introduce yourself in secure environments. Access is a major issue. • The government doesn't really want full competition, which makes it difficult for a new vendor to break in. Because the federal procurement process is so onerous, despite recent efforts to streamline, there is an increasing tendency to make new awards to incumbents as an expediency. Consequently, it can be very difficult to unseat an incumbent. Some barriers to entry on the commercial side include: • Marketing must be undertaken in a totally different way, costs are higher. • You need new people for commercial work, or you must undertake a long, difficult re-training effort. • For ACS, the best way to enter a new market is to acquire an existing company with a good reputation and on-going business. This can provide a platform for further expansion.
Compaq	We are moving up-market to become a virtual support function to the CIO. Segments with the best growth potential for outsourcing: Telecom, Financial, Manufacturing, and Retail/Distribution. Goal: developing and delivering a creditable value proposition that the clients in the new market will buy.
EDS [#21]	EDS believes that the market is definitely moving toward more comprehensive outsourcing deals because company managements are looking for long-term, strategic business partners that are able to add value to their businesses. The vendor's role is clearly becoming more strategic than tactical—as it was in the past, i.e., a provider of short-term, clearly defined solutions. Fewer customers are opting to select a team of various service vendors that they need to manage themselves. However, customers do often prefer to outsource while retaining certainly specifically defined IT functions to do internally. Even EDS seldom wins ALL of a customer's IT budget.
Fed Data [#17]	Direction of Federal Market Fed Data wants to pull out of the facilities management segment of IT outsourcing. Because the potential for increased business in the federal seat management market is excellent, Fed

	Data is not actively pursuing commercial clients. However, when pressed, he said that he thought the following mix of business would be ideal: • 50% federal • 25% state & local • 25% commercial The federal market is clearly moving "upmarket," albeit slowly. For example, the SSA wants to outsource only 2,000 seats as a test case because it is uncomfortable with giving a single contract to a single vendor for all 60,000 seats at the agency. Managers do not believe that any single vendor would be able to fulfill the work required by a single contract of that magnitude.
Independent Consultant	Both trends are underway simultaneously (the outsourcing pie is expanding). In either case, vendors need to work on their fundamentals, i.e., understanding better where they can add value. There is a tendency to win deals and then worry later how to deliver results. Partly for this reasons, outsourcing consultants today ALWAYS insist on building "prenuptial agreements" into contracts that spell out the terms and circumstances that will govern the transition from the incumbent to a new vendor at contract expiration.
Litton/PRC	Regarding an "upmarket," or "downmarket" strategy, Litton/PRC sees low-margin seat management as a way to get the foot in the door for more profitable business, such as network storage. Regarding profit margins, we believe that—in general—the more remote work that can be done on a remotely managed basis and the less labor-intensive, the more profitable.
Perot Systems [#22]	Perot Systems is focused on the "upmarket".
Raytheon [#7]	The outsourcing market as a whole is definitely moving "upmarket." By this, respondent meant a trend toward outsourcing that included hardware as well as people. Also, he called this "privatization" in distinction from "outsourcing." The distinction hinges on whether, or not, the vendor takes responsibility for staffing and staff operations ONLY, or takes responsibility (if not ownership) of hardware and networks as well. Much federal outsourcing involved rather transparent switches whereby employees left their offices on Friday as civil servants and returned on Monday to the same jobs in the same offices as private contractors. As originally conceived, Groundbreaker was supposed to be a privatization, whereby the vendor would take responsibility for hardware as well as people. For political reasons internal to the NSA, the final contract was scaled back to mere outsourcing, as defined above. The respondent saw this a great retreat and reacted with disappointment. On the subject of the NSA, the respondent was quite gloomy. He said that the Cray supercomputers that the agency had purchased a few years ago would be obsolete within 4-5 years. Even now, Raytheon believes it could build an array of parallel processors that could equal or outperform the Cray supercomputers. As an illustration of mindset of some members of top management there, he described the desk of a high-level agency executive: PC sits in the corner under a dust cover. On the desk sit a legal pad and pencils. A secretary prints out e-mail and takes dictation as if it were 1950.
The Outsourcing Institute [#2]	Respondent sees the outsourcing industry moving clearly "upstream" toward BPO as vendors offer increasingly more comprehensive packages of services.
UNISYS [#16]	Our business is clearly moving upmarket, but we are however a full-service provider.
USInternet-working [#14]	Respondent believes that both the commercial and public sectors are moving "upmarket." From the point of view of USI, this trend has been evidenced by the extent to which customers demand multiple applications as they attempt to integrate legacy systems. To meet this demand from the State of Maryland, USI partners with CSC and SAIC.

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?	
ACS	While ACS doesn't have anything like the deep pockets of Litton, nonetheless, finding "proposal money" has never been a barrier to seeking new business. (Litton could afford to spend $10 million to cover proposal and bid preparation costs; at ACS such an amount would be considered astronomical.) Capital isn't typically required for asset acquisition connected with outsourcing deals. ACS prefers to team with leasing companies that provide whatever financing is required. Overall, IT outsourcing (bodies + assets) requires more capital than DoD contracts.
CSC (1) [#3]	How many of skills are transferable to the commercial market? The most readily transferable areas of expertise are: • Rigor in program management • Ability to deal with complex issues • Ability to apply the Carnegie Mellon model for performance achievement Example: CSC's successes in the federal market were critical to DuPont's decision to award CSC a large outsourcing contract in the commercial market. CSC's ability to penetrate the commercial market depended, in many cases, on similar situations where prospects were "seeded" with stories of what the company had achieved in the federal market. This proves as well the extent to which skills and processes are transferable between federal and commercial markets. Most important of these is the rigor of project management in the federal market. The ability required there to deal with complex issues, regulatory environment, etc. fosters a process discipline that is very transferable to the commercial market. The most significant barrier to entering any new market is the lack of established trust between customers and vendors. Trust is very important. Even in the federal market, understanding the real mission of many agencies is not easy, yet in every case the vendor must demonstrate a deep understanding of the client's business in order to offer a better value proposition. In particular, our mastery of Carnegie Mellon software development metrics puts us in a select category of vendors that are attractive to new customers based on objectively demonstrated expertise. This expertise has been used on numerous, demanding outsourcing contracts, such for Aegis, air traffic control and NASA. Also worth noting, we have 47 years of experience in program management, including provision of on-going training. (We do training in-house even though we recruit externally.)
CSC (2) [#5]	The greatest barrier to entering a new market is typically lack of name recognition. Even so, all of the potential barriers noted are important (financial, technical, marketing, organization, staffing, management). Historically, CSC has spent little on promotion to achieve better name recognition. It should probably have spent more. In the past, CSC business has spread by word of mouth between satisfied customers. Now, the company targets the "thought leadership" of various industries as a strategy to get a foot in the door for the CSC brand. (Clearly, the situation is totally different in the federal market where CSC has a much better established position.)

EDS [#21]	Respondent doesn't really believe that there are any (merely) "horizontal" applications. Even in the case of CRM, HR and accounting, he believes that customers have a strong preference for a vendor that is able to demonstrate in-depth understanding of their industry. Therefore, to be successful in entering new markets, vendors must be able to hire experts in the target industry that are able to demonstrate the benefit of their years of experience by solving customer problems creatively—even if nominally "horizontal" with cross-industry application. Respondent also believes that there is something called "critical mass" at work. If gaining a foothold in a new industry is difficult, there is also a snowball effect whereby success breeds more success—once vendor has achieved a minimum criticel mass of business. **How does an unknown vendor establish an identity in a new market?** He must acquire and demonstrate an understanding of the dynamics of that new market, the issues that concern its players, the structure of the market, its IT spending characteristics, its priorities, etc. The next step (for EDS) would be to map the vendor's capabilities to this aggregate industry model. Next, the vendor must develop a strategy for meeting the needs of customers in this new market. In the case of making a transition from the federal to the commercial markets, respondent doesn't believe that customers will pay attention to the type of market so much as to the nature of the solution and the vendor's success in solving a business problem. Comment: "You're only as good as your last client." (In this context, he described how EDS monitors customer satisfaction on a daily basis according to an on-going methodology. The goal is to solve problems ASAP that could impair the client relationship.) At the same time, image and perception are important. In order to gain a toehold in a new market, smaller vendors should partner as subs with larger prime vendors on contracts. EDS does this often with other vendors. Alliances and partnerships are critically important. EDS differed with other survey respondents by denying that the vendor had, or would enter a new market through an acquisition.
Entex IT Services [#13]	There are fewer barriers of entry to vendors of horizontal products than to vendors whose products are specialized according to vertical industry. However, this approach does expose vendors to more intense competition and the threat of commoditization. The most important weapon in overcoming barriers to entering new markets is technical expertise, especially in the areas of application development and application management because they are higher value-added. Customers of horizontel IT products are less concerned that vendors demonstrate expertise in their vertical industry than in their core technical competencies. In the federal market, vendors need to prove their understanding of the government market and its characteristics. Without the benefit of the name recognition advantage of Siemens, Entex would (did) have difficulty in entering new markets. Lack of name recognition is definitely a problem. **Marketing** Does Entex use outsourcing consultants? Not much contact so far. Consultants are more active in Europe. The type of services offered by Entex take the company off the radar screens of most outsourcing consultants.

Fed Data [#17]	While commercial company business is attractive for many reasons, respondent thought that the transition from commercial to federal would be more difficult than the reverse due to the long sales cycle in the federal market, the complexities of the procurement process and the importance of having personal relationships in place. A vendor wanting to move from the federal to the commercial market, in his view, must expect to need to set up a virtual "mirror" organization to serve commercial clients. Salesmen, etc. would need to be recruited who had commercial experience. As an exception, the technical staff and project managers could probably be re-trained successfully for work in the commercial market. Beyond that, such a transition would only work with the help of good partner relationships. (Even the commercial partnering model is very different from that used in the federal market.) Lack of commercial backlog and reference clients would definitely be a handicap. Respondent thought that commercial clients might be interested in a vendor's technicel solutions for federal clients, but he was skeptical that this alone would win business, i.e, without being introduced by a commercial partner with excellent credentials. Respondent noted the irony that federal clients are very anxious to benefit from vendor experience in solving problems for commercial clients, but commercial clients are not nearly so keen on letting federal vendors do work for them. In theory, this gives an advantage to primerily commercial vendors that want to enter the federal market, yet, they (for reasons outlined above) are often put off by the difficulties that they encounter. (As an example, a spokesperson for Cap Gemini E&Y said emphatically that the vendor had decided NOT to pursue any work for federal clients because of the barriers and difficulty in doing business in that market made it categorically unattractive.) Respondent commented that CSC had encountered "difficulty" in applying its commercial business model in the federal market.
Getronics [#10]	**Barriers to Entry** Lack of dependable partner relationships. • Respondent used the example of seet management, but the point is applicable in general. He pointed out the danger of undue reliance on a partner to provide a critical element of a comprehensive seat management solution. Vendors must have in-house core competencies required to bid for target business. Also, remember that menaging partner relationships is to manage a "moving target." For example, expect that a "Statement of Work" will be obsolete almost as soon as it is formulated. • Remember: "learning is incremental," meaning that there is no short cut to developing the technical and business knowledge required for success. How important are partner relationships? Prime contractors are vulnerable. On the commercial IT outsourcing side, three out of four primes have had major problems with their subcontractors. These problems reflect, in part, bad management. In addition, they reflect fundamental incompatibilities, inequitable cost-sharing arrangements, conflicting processes and tools, as well as people who can't cooperate. **Commercial versus Federal Market** The commercial market offers tremendous potential for growth of IT outsourcing. Vendors wanting to move from the federal to the commercial market must take in to account the significant differences between the government's procurement policies and standard sales practices in the commercial market. Ultimately, there is a great deal of similarity between the business processes of government agencies and commercial businesses. Yet, vendors can trip on unforeseen differences in approach. For example, Getronics prepared TCO studies for its seat management solution (a common practice on the commercial side) only to be told that they violated FAR 9.5, which prohibits vendor conflicts of interest. (Solution: these need to be prepared by a third-party, not the vendor directly—especially if based on privileged information that is available only to qualified federal contractors). Remember, "IT can be a competitive weapon for customers, which depends on quality IT vendors and their core competencies.

Independent Consultant	Regarding the transition from federal to commercial markets, the truth is that commercial customers are seldom impressed to learn what vendors did in the federal market even if the opposite is true (federal agency customers are usually very interested to learn what vendors did/are doing for commercial customers). Federal customers want, in particular, to hear how the private sector is standardizing, adopting to industry-standard solutions, etc. The key to success in the fed-to-commercial transition is to stress the nature of technical solutions independent of the customer's identity. In short, talk up your achievements themselves. The same sales staff with federal experience MAY be able to function in the commercial market, but it must be able to show strong understanding of technology, to show HOW business problems were solved, in order to undercut customer tendency to undervalue federal sector IT work. Also, vendors should take pains to prevent salesmen from closing deals on which they can't deliver, or at least not cost effectively. Salesmen must understand what the vendor can really deliver, and usually this involves an appreciation of specialized solutions. In terms of strategy, while there is a great potential for new outsourcing business in general, vendors must avoid the temptation to "hybridize," i.e., offer themselves as experts in both infrastructure and business transaction processing. Pick one or the other and excel at it. If you decide to expand your expertise, then go out and build it, but don't expect to find a short cut to spending time and money on the effort. Commercial vendors that want to move into the federal market are usually put off by the complexity of the federal contract proposal preparation and bidding process, including the protocols and security issues involved.
Keane [#15]	Federal vs Commercial Market From Keane's point of view, the federal market is less attractive than the commercial market. In contrast, Keane sees better potential at the state & local levels of the public sector. For example, outsourcing initiatives underway in Maine and North Carolina in the area of e-government are more advanced than those of the federal government. The federal customer is behind the state & local government customer. Rates and profits are lower in the federal market, but size of contracts can be quite large and the long-term nature of the business is attractive. In short, respondent believes that, for many vendors, doing business in the federal market is like holding bonds in place of stocks. Importantly, federal customers are increasingly interested in learning what vendors are doing/have done in the commercial market (while the reverse is much less common). Keane often takes commercially tested practices and applies them to work in for the federal government.
Keane [#6]	The greatest barrier to entry in new markets is lack of name recognition. Even with a $100 federal unit, Keane must partner with other vendors as a key element of its application management market strategy. Success in a new market depends largely on developing differentiators, i.e, ways to separate you from the crowd of other vendors whose names are already known. While partnering is usually necessary, some vendors partner reluctantly and only at customer insistence. There is an advantage to being in both the federal and commercial markets. While the federal customer wants to "commercialize" IT solutions, commercial customers tend not to be impressed (at least initially) with work done in the federal market. Eventually, however, commercial customers come to appreciate the quality, methodology and process of work done for federal customers.

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<tr><td>Litton/PRC [#1]</td><td>

Why diversify by moving into the commercial market?

- Management wants to promote value of "dual use" technology.
- We have found that our federal market skill sets apply well to the needs of commercial market clients.
- Ultimately, we see better growth potential in the commercial market than in the federal market.
- Our success in the commercial storage network business has encouraged us to continue in this direction.

How is this migration from federal to commercial market being managed?

- We began the process 7-8 years ago. We now have a different Web site for commercial business (www.outsourceprc.com. Here, we make a point of NOT promoting our federal market experience because we have no name recognition in the commercial market.
- Our strategy is to pursue OEM partnerships in both the federal and commercial markets as a way to advance the promotion of our capabilities with commercial customers. We make a point of avoiding direct competition with the top-tier vendors such as IBM Global, CSC and EDS.

Barriers to entry to the commercial market?

- Lack of name recognition or brand franchise among commercial customers. Trust is the critical element of the vendor/client relationship and it isn't easy to create it in the short term.
- We depend—to tell the truth—on the value of the "Litton" name, which has cachet, even though it hasn't been used on consumer products for many years.
- On the other hand, had we been "blessed" with a name such as "Fed Data," we wouldn't have had a prayer of success in this migration to the commercial market.
- Commercial business operates along totally different lines than federal business, i.e., fixed-price contracts. Federal contracts are usually more flexible.

Greatest problems related to transition from federal to commercial outsourcing:

- The commercial world is vast, it is difficult to pitch to prospective customers in vertical industries without demonstrated expertise in that vertical.
- Transition requires an entirely different sales staff that is commercial oriented.

Also, the competitive bidding process in these markets differs markedly. Overall, costs in the commercial market run higher. SLAs differ as well. Note: SLA expectations in the federal sector are rising (they had been significantly lower than in the commercial sector).

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<tr><td>Lockheed Martin [#4]</td><td>

The most important barriers to entering a new market are mainly organizational, and secondarily financial. A vendor needs ample funds to be taken seriously in the market. Vendors with limited financial resources should confine their offer to remote application management as a solution to customers' constraints due to the skills shortage.

IBS' policy is to avoid capital risk. Contract cycles are shorter in the commercial sector, typically 3-5 years rather than eight, as is common in the federal sector. A typical IBS deal, such as Gateway computer, can be implemented in 120 days.

In respondent's opinion, the government is a better buyer than commercial market buyers of IT outsourcing services. Reason: the government knows how to deal with outsourcing services and has senior executive IT managers. In the commercial market, outsourcing project liaison is often handed over to junior IT staff.

IBS rejects deals if a customer is deemed "unsuitable," for example, if the company has never done outsourcing, and doesn't use a consultant or lawyer. In such cases, the likelihood of loss or litigation is higher and the quality of the RFP is lower.

One red flag: when outsourcing is called in as a solution to a troubled M&A relationship.

Lack of name recognition in a market is certainly a major handicap. The solution is to deliver skills. Lockheed Martin provides an advantageous pool of resources. IBS can, when necessary, get hold of expert staff from anywhere in the Lockheed Martin universe. Intercompany transfers are used. Also, divisions can award intercompany subcontracts, or "hire" internally. And the company hires off the street.

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	LM has a strong Chief Technology Officer. In addition, "business acquisition skills" are transferable between federal and commercial markets. The principal barriers are the differing financial and accounting systems used in these two markets. Also, the nomenclature used is different. At IBS, staff (technical and sales) working on commercial projects is generally kept separate from those working on federal projects. Yet, there have been transfers between the two groups (but not all are successful). A transfer from the commercial to the federal market is less likely to be successful.
Perot Systems [#22]	Respondent believes that financial and organizational are equally difficult barriers. Successful existing business units are competing for the same capital resources and have a proven track record and history. One of the key areas affecting your ability to obtain capital is the proposed organizational structure. Financial and organizational alignment should be considered part of your strategy while marketing, technical, and staffing is more tactical in nature and is something you can leverage from existing business units.
Raytheon [#7]	Respondent believes that virtually every vendor that is active in the federal market wants to diversify by doing business for commercial customers. However, the barriers of entry for moving from the federal to commercial market are formidable. All of the ones noted (financial, technical, marketing, organization, staffing and management) are relevant. Vendors want to leverage their federal experience into more lucrative work in the private sector, yet they are—in general—totally unprepared for the "cut-throat" nature of commercial competition. Federal salesmen are more collegial and adopt easily a cooperative stance among each other. In contrast, commercial vendors have no need to deal with GSA schedules, or similar bureaucratic obstacles. Also, salary levels commanded by commercial sales staff are much higher than those applicable to the federal sales staff. For example, salesmen work in the federal market for $75,000 while their counterparts in the commercial market are earning $200-300,000 annually in commission income. It will be very difficult to convince commercial customers to do business with a vendor that has experience primarily, or entirely in the federal market. A very different set of skills is required. The bridge should be technology and technical skills that are transferable. Respondent doesn't believe that commercial customers are likely to be impressed by reference clients in the federal market. Reason: commercial customers perceive their technical requirements to be higher. When asked about the level of technical skill demanded by typical federal customers, respondent insisted that "the federal government doesn't know how to write an effective SLA." For example, the government writes a SLA that requires all calls to be answered within ten seconds of the first ring. Accordingly, the vendor is rated on his speed of response. Note: there is no metric for the effectiveness of the answer. As a result, vendor could get monkeys to answer the telephone and still get paid!
SAIC [#20]	The primary barrier to entry is the need for a new sales force. You can't use the same salesmen for the commercial market as you did for the federal market. Salesmen need to have a keen understanding of their customers' markets. Exacerbating this situation will be the inability of salesmen to impress commercial clients with accounts of work done by the vendor in the federal market. In contrast, federal clients tend to be impressed by what vendors have done/are doing in the commercial market. Nevertheless, respondent thought that making a transition from the federal to the commercial market would be more difficult than the reverse due to the complexity of the regulations that govern the federal procurement process. Teaming with vendors already established in a new market only works if you are small. A large vendor must buy its way into a new market by acquiring a service provider that is already established and respected based on successful, on-going business in the new industry.
The Outsourcing Institute [#2]	Regarding barriers to entering new markets, respondent believes strongly that "deals are done between people." Therefore, sales and sales management are critically important. Also critical are project managers, who are becoming increasingly "free agents" in the industry ("wheeler-dealers"). The most experienced project managers come from the federal market, which has developed an established methodology for project management.

UNISYS [#16]	Federal A-76 plans play an important role in outsourcing. Staffing and Marketing are also significant barriers.
USInternet-working [#14]	USI does not see the same set of competitors in the commercial sector as it does in the federal sector. Reason: there are significant barriers to entry in the federal market. USI has a geographical advantage being located close to Washington, D.C. Federal buyers have been reassured that the company understands its security needs, in part, by making personal, on-site visits to USI's Annapolis facilities. Moving from the federal to the commercial market is much more difficult. Reason: difference in mindset of vendor staff, difference in the accounting systems used. Also, entering the commercial market requires a large capital investment. Moving from one market to the other requires establishing a new sales team. Commercial salesmen need a substantial re-orientation in order to be successful in the federal market. Also, personal relationships are very important—in terms of clients and SI vendor/partners. While relationships are always important and valuable to sales, they are MORE important in the federal market. This is also true in the state and local government markets. At the state level, ALL sales are based on personal relationships. Lack of name recognition could be an important problem. Clearly, vendors with an established reputation in the commercial market will find it easier to leverage that success in the federal market than the reverse. Achieving distinction in some kind of specialization can offer a shortcut solution to this problem. Vendors with commercial experience that enter the federal market typically agonize over the "crawling pace" of the sales cycle when compared to the commercial market.
7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?	
ACS Government Solutions Group [#8]	• Recent changes in the federal procurement/contracting system have made it much harder for vendors to win business away from incumbents. These changes function as an incentive to obviate the burdensome paperwork required to evaluate new bids by simply renewing contracts with incumbents. • Aggregation of discrete types of work into ever-larger megacontracts makes it increasingly more difficult for small and medium-sized vendors to win awards. • As a result, they are obligated to win subcontracts from primes that are reluctant to give up shares of their business, unless absolutely necessary. Smaller vendors are unable to bid directly for these large contracts, which is fueling the drive toward partnering (sometimes reluctantly). • Despite all the publicity to the contrary, the government does not seem to be enforcing set-asides to small business—which is facing tough times in the federal market for the reasons noted above. • Because Wall Street determines what a company's stock is worth, ACS—like other vendors—has been obligated to re-invent itself as an "e-company." This has had a big effect on the federal market, but now appears to be losing steam.
Compaq	These factors are minimal constraints if the outsourcer has both the delivery infrastructure and resources to leverage.
Convergys [#19]	To date, this has not been a problem. In general, Convergys does NOT want to take over customer HW assets, but could use leasing as an alternative. Clearly, having excess capacity in your data canters is an asset. For that reason, company feels itself at a disadvantage in Europe where it does not, as yet, have its own data center facility. As a temporary remedy, it has entered into partnering arrangements. For this, the larger you are, the more clout you have. Company could use the BOT model outside of the U.S. to mitigate risk to invested capital. At least 80% of company outsourcing work is done remotely at present (at facilities owned by Convergys); 20% is done on the customer's premises.
CSC (1) [#3]	As a public company, CSC must provide its shareholders with a meaningful risk-weighted return. Therefore, it must balance business risks. Broad experience lets us gauge risk with accuracy. We have an in-house system model for program management that includes computation of costs and profits.

CSC (2)	Difficulties in obtaining capital required for closing outsourcing deals has never been a problem for CSC. Yet, availability of capital has seldom been a clear-cut differentiator or predictor of market success. For example, Lockheed Martin's commercial IT business unit can claim no barrier to funding from its deep-pocketed parent, nevertheless, its successes in the market remain modest. The same can be said for UNISYS (which is leaving the federal market). Companies such as CSC and ACS are at no disadvantage due to difficulties in accessing capital, but the situation depends greatly on the type of outsourcing business that a vendor does and its stage in the business lifecycle. For example, newly founded Exodus Communications had to use equity to fund its capital requirements.
EDS	After admitting that he had no experience working for a small vendor, respondent said that availability of capital had never been a barrier to new business in his experience. Although he could recall no deal that had been turnad down due to the unavailability of capital, he did admit that capital was an important factor in the competitive outsourcing market. He said that EDS did not often resort to off-balance sheet solutions, such as leasing, because it believed that it could manage equipment assets better than any leaseholder.
Entex	Based on access to the financial resources of the Siemens global enterprise, Entex faces no capital constraints in pursuing new business.
Fed Data	Cost or lack of capital has never been an obstacle to new outsourcing contracts for Fed Data. As an example, respondent said that he had spent $50,000 to obtain a $5 million annual contract revenue stream, which he considered quite acceptable. Overall, he thought that federal outsourcing required little in the way of capital outlay. Whether for federal or commercial clients, he stressed that vendors need to use leasing companies for HW purchases. Even Fed Data, which has deep pockets, avoids outlays for capital equipment purchases as part of outsourcing deals. He gave the Peace Corps contract as another example; it required very little by way of upfront cepital outlays. In the context of leasing, respondent contradicted other survey respondents who claimed that leasing incurred tax liabilities. Fed Data respondent insisted that equipment located on federal facilities incurred no property tax burden.
Getronics	Should the vendor supply HW on a lease rather than purchase basis? Often the decision hinges on taxes. If the vendor owns equipment assets, it pays an 8% property tax in the District of Columbia and 4.5% in Virginia. In many cases, direct vendor ownership of HW results in a 15-20% cost markup. If the government owns the HW itself, it pays nothing (but then, after a few years, faces the threat of obsolescence along with the burden of disposal). Because recourse to leasing agencies (for equipment acquisition) is always an available alternative, vendor availability of capital is not a barrier to closing outsourcing deals. Yet, vendors should expect (and be able) to invest in the software tools that will be required to fulfill contracts. Because agencies are often in transition between technologies, vendors may spend $250,000-1 million upfront to develop the tools required to standardize, streamline and fulfill contracts.
Independent Consultant	While not a problem for CSC, it has been a problem for ACS. At times, the company had to offer a qualified proposal due to the inability to deploy sufficient capital investment. In respondent's opinion the way to avoid this is to plan growth and, in any plan, capital is only one factor among many.
	There isn't a great need for large amounts of capital for upfront investments in connection with most outsourcing deals. Most costs result from acquiring customer staff. Even so, these costs are built into the financial structure of the entire deal. While the data center/ infrastructure outsourcing business may be an exception, this is not the most attractive segment of the commercial outsourcing merket for other reasons. It has been commoditized and reduced to single-digit profit margins.
Litton/PRC	On the issue of capital investments, we don't find capital availability a constraint because there are numerous sources of financing, such as GM Capital, when needed. Capital commitments do raise the risk level, but the risk is seldom with the hardware. Deals fall apart based on service shortfalls. As a result, if we need to dispose of contracted equipment whose purchase was financed, customers almost never ask us to pick it up. They usually buy us out at the end of a contract agreement. We see outsourcing project risk in two

	levels: 1-staffing; 2-assets.
Perot Systems	As we all know pursuit cost can be very expensive. With that being said, capital to pursue an opportunity that we believe has a high probability of Perot Systems being successful is not a factor in our opportunity pursuits. Capital allocation requests for pursuits are denied only when we perceive there is a less than average chance of being successful.
Raytheon [#7]	Vendors incur virtually no capital constraints with traditional IT outsourcing. However, in the cast of a privatization of government hardware assets, capitel is required. Even so, monies can typically be expended incrementally on the road to a complete buyout. The best solution: credit the vendor from the customer's cost-savings so that the vendor acquires eventual ownership of assets at the end of the contract term, without the need to make out-of-pocket cash payments.
SAIC	While large infrastructure outsourcing deals require large amounts of capital, other forms of outsourcing do not. Leasing arrangements will always represent a costly, premium solution from the client's point of view. He thought that only an unsophisticated customer would accept a leasing arrangement. The BOT option is an acceptable alternative, but one that is not often used because clients seldom want to take IT work back in-house once it has been outsourced.
The Outsourcing Institute	While deep-pocket financial resources always confer certain advantages, neither availability nor cost of capital should be considered an obstacle to bidding new outsourcing business. Judicious management of leasing relationships and contracts can obviate the need for vendor borrowing. Another possible solution is to form a customer/vendor joint-venture, or partnership that permits off-balance sheet financing. *The way to enter any new market is to find an anchor client that is willing to serve as a reference in that segment.* Differences between federal and commercial market? The bid/proposal process in the federal market can be very long, detailed and burdensome. The sales cycle in the commercial market is usually shorter and simpler. In either case, it is important to write detailed SLAs that are flexible enough to take into account changes in business conditions. EDS was/is particularly good at this aspect of bidding. In some cases, vendor experience in the federal market can be used to advantage in the commercial market. Examples of vendors that have done this with great success include: CSC, Lockheed Martin and Litton. Initially, virtually all of their business was in the federal sector, but slowly and quietly, commercial deals began to happen. **How to overcome customer resistance in the commercial market?** Explain what you did in the federal market. Emphasize the scale and scope of those projects. For example, CSC began with labor-intensive, multivendor federal projects and edvanced to sophisticated technical work as a prime contractor. Don't neglect to mention your experience with federal staff transfers in connection with outsourcing deals. In the federal markat, transfers of 200-300 people are common. The lack of vertical industry knowledge in the commercial sector should not pose an insurmountable handicap. Federal market vendors should be able to leverage their federal experience based on what their people actually accomplished. Avoid splashy advertising. This will only wasta money. However, consider that you may need a new sales taam. Federal sales are built on established *relationships*. Also, relations between vendors and the government are often contentious (which can only be handled by experienced sales people). Also, expect deals to be done in the commercial sector at greater spaed, involving unexpected developments. Expect as wall top executives to wield a great deal of clout, whoever may present himself initially as a decision-maker. One point worth noting: many marketing practices that are common in the commercial sector, such as client entertainment, are illegal in the federal market.
UNISYS [#16]	Bid activity/capital is based on priority of the outsourcing bid.

USInternet-working [#14]	Cost (and availability) of capital is a serious issue and a barrier to entry. Undercaptalization has caused the demise of numerous would-be ASPs. The ASP business is very capital intensive for vendors and USI has been successful in the market to a large measure because it has been very successful in raising equity funding. Bottom line: USI has, itself, lost no new business due to insufficient capital
8. What important changes do you see at work in the outsourcing market today?	
ACS Government Solutions Group [#8]	The role of the CIO and technology as it relates to business success or failure has increased in importance. As a result the need to buy sourcing solutions based on results is becoming the norm. From the point of view of ACS, "pure outsourcing" means providing people (bodies). This is generally less profitable than "impure outsourcing," consisting of people plus high value-added networking, application or other consulting services. "Profitability" is difficult to measure because easy assumptions don't always apply. For example, while teaming with a prime on a contract is generally perceived to be lower-margin for the subs, ACS factors in the much lower cost of preparing proposals and bidding directly. Also, subbing generally leads to a pipeline of additional business, so it is usually worthwhile to participate as a means of getting a vendor's foot in the door to places that would be otherwise inaccessible. Therefore, while seat management and desktop service contracts may not appear attractive in themselves, they can serve as conduits to other, more attractive business. Beyond that, respondent believes strongly that the critical key to profitability is not the size of the margin associated with a given contract, but the way in which the contract is managed and strategized, i.e., how this contract/business fits into a comprehensive sales/marketing plan.
Convergys	The ASP model is "outsourcing light." Expect sharp consolidation in this segment of outsourcing. Also, expect increasing demand for, and use of offshore outsourcing facilities. Convergys is moving in this direction and will likely announce such a facility soon. It already has a data center in Canada. The role of consultants to expedite outsourcing deals will increase. Convergys has had relationships with them in the past. They can provide critical help when a vendor moves into a new market.
CSC (1) [#3]	Clearly, customers want increasingly comprehensive outsourcing contracts (for example, the LOGMA army contract). The first federal outsourcing contracts involved the transfer of civil servants and covered rudimentary transaction processing tasks. These contracts were followed with more complex ones involving enterprise architectures and supply chain management. Overall, customers are driven by the value potential of IT outsourcing. Also, they are trying to cope with technological change. They don't know how to do it and they are admitting with increasing frequency that they need help in identifying the best solutions to their business problems. The federal retirement situation is a "bombshell." We see federal employee unions as important allies (ex. IRS). Sole-sourcing? If you become a real "solutions provider," then you become a natural contender for sole-sourced contracts. Much work is done in the federal market under task orders, and these are not necessarily competitive (ex. the contract that USPS awarded recently to Federal Express on a sole-sourced basis). The new Republican administration may allocate higher budgets to the DoD, but eventually "reality will set in" and the government will be obligated to move increasingly toward privatization of functions that are currently performed by civil servants and/or military personnel.
CSC	Customers want to grow their businesses, but they cannot do so with their existing IT infrastructure. They can't support their actual or expected growth with existing staff and facilities. CSC sees much opportunity around the globe, especially for work with U.S. companies that are expanding abroad. Typically, CSC begins a relationship by doing work for the U.S. units, and then expands the relationship to doing client work for units located outside of the U.S. The average size of outsourcing contracts is increasing, at least for CSC even

	while the number of deals is shrinking somewhat. CSC revenues are now about $5 billion, derived from work for Fortune 500 companies. CSC targets "mid-tier" customers, which it describes as having revenues or $1-5 billion. Top-tier companies typically have revenues above $5 billion. As an example, J. Crew awarded a contract based on an IT budget of $2-30 million annually. Companies in this mid-tier segment can't field sufficient IT resources and they outsource out of necessity. Opportunities are now increasingly global rather than national and the most attractive segment has become the midmarket—which is also on the move globally. Vendors expecting to make the transition from the federal to the commercial market need to build a base on their federal experience—following CSC's example. The company took its 10-15 years of experience in working for federal clients that made high demands for technical discipline and process management to the commercial market, albeit with adaptations. We discovered that we could be very successful with commercial clients by applying the same processes globally that we had used for federal customers. At the same time, realize that partnerships take time-whether with customers or other vendors. You must work your wey up to a position of trust. There is no shortcut to the position of "trusted advisor." Insofar as possible, use industry analysts to spread the word about your capabilities cost-effectively. In the 1990s, customers were motivated to outsource primarily by a desire to achieve cost-savings. This motive was superseded by a realization that lack of internal resources made outsourcing an imperative beyond potential cost-savings. Eventually, cost-savings will move back into the top position as an action criterion, but at the moment customers are giving priority to the need to standardize their IT environments as a precondition for achieving cost-savings. CSC showcases its heritage of work experience in the area of security for classified federal customers. Worth noting, this experience proved decisive in winning the Nortel contract. Top management decided that CSC's skills in this area were eminently transferable—and desirable.
EDS	Respondent cited a move toward strategic outsourcing and away from commodity outsourcing. Discussions between EDS and prospective customers usually center on the nature of the long-term, strategic contribution that the vendor can make to the customer's business model. **Risk-sharing?** Respondent commented that, while the customer wanted to consider the IT vendor a partner, there was no strong trend toward including vendors in risk-sharing and profit-sharing arrangements as part of an outsourcing contract. While customers may be intrigued initially by the idea as a way to provide incentives and punishments to the vendor, they usually conclude that there is no effective wey to measure the vendor's contribution to revenues and profits separate from the rest of the customer's organization. Also, changes in business conditions are common and, when they occur, they usually disrupt whatever sharing arrangements had been in place previously.
Entex	• Customers are looking for more complete outsourcing solutions. They want to work with fewer suppliers. They prefer the prime (general contractor) model whereby a lead vendor manages the relationships and monitors the work of subcontractors. Overall, they want to reduce headcount. • The transition to e-business is making competition between vendors more intense. Smaller vendors are being relegated to subcontract roles, where margins are lower.
Fed Data	Important changes in the federal market include: • People are recognizing the need for change, both in terms of budgets and staffs. • There is a genuine effort underway to understand how to make the transition from internal to outsourced IT functions. • The TCO concept is spreading in the government (even though it is seldom able to specify its costs accurately). Agencies are making progress in analyzing their "hard" costs for equipment, but having great difficulty in assessing their "soft" costs for people, HR, etc., which is necessary in order to compute accurate, projected cost savings.

Getronics	Federal outsourcing business is moving in the same direction as the commercial market—"upwards" toward increasingly comprehensive, BPO-oriented contracts. If so, is seat management on the way out and, as a result, unattractive to vendors? Absolutely not: "Seat management is like getting the camel's nose under the tent." Typically, during the term of a seat management contract, 10-25% of incremental revenue materializes (based on total value of the seat management contract). This explains part of the advantage of being an incumbent; agencies are unlikely to go elsewhere to have work done that can be given conveniently and simply to the vendor that is already on the premises and performing satisfactorily. Does this mean that vendors either can, or should bid for new seat management contracts on a no-profit basis in the hope that these incremental revenues will ultimately make the total customer relationship profitable. Respondent believes that this is a high-risk way to do business because an unprofitable vendor is unlikely to be either able, or motivated, to do the highest quality work on the initial contract. If work on the basic contract is lackluster or deficient, then the expected, incremental revenue will not materialize. In the near future, the federal workforce will experience a massive wave of retirements, and there are no young replacements for them on the horizon. Young recruits want better hardware and working environments. During the next two years, the government will continue to play catch up; after that, expect large new outsourcing contracts because there will be no viable alternative. Union-inspired anti-outsourcing efforts (TRAC) will continue, but reality can't be changed.
Independent Consultant	Clearly, the outsourcing market is moving toward BPO in the sense that customers are using vendors to take over even more complex and comprehensive packages of business functions. At the same time, vendors should be aware that the opportunity is greater than the reality. Clients continue to be reluctant to hand over to vendors too much of what they perceive to be "control" over their core business processes, so fulfilling the market's potential remains a hard sell. Also, never forget that there is always internal resistance to BPO. Incumbent employees always fear that headcount reductions will inevitably follow any BPO contract, if not all outsourcing. **The SLA Game** Clients look to SLAs as a justification for their decision to give up direct control; SLAs are wielded as indirect control. Yet, in most cases, customers demand very exacting SLAs without realizing or admitting that, in fact, the high levels demanded by the SLA may never have been achieved by the organization, may not be possible, or—if possible—may be neither necessary, nor cost-effective. Smart vendors can expect to find excellent opportunities for growth in the ASP field (fixed services delivered for fixed prices on a monthly pay-by-the-drink basis). The danger is excessively fast growth and letting costs get out of control. Remember: ultimately, when all is said and done, ALL outsourcing deals are motivated by a customer desire to save money, however expressed.

<table>
<tr><td>Keane</td><td> Market Trends
In his opinion, the ASP model has failed—at least insofar as having an appeal for Keane's target market of Global 2000 organizations. They require significant amounts of customization, cannot use "plain Vanilla" applications. Therefore, ASPs cannot serve their needs cost-effectively.
Changes in the Outsourcing Market

Customer interest in IT outsourcing is rising, especially for application management and development. Now, customers outsource these functions as part of a competitive strategy. They want to streamline their operations, offload nonstrategic IT functions so that internal staff can be used for higher value-added, core, proprietary IT development projects.
The role of the CIO is changing. He/she is no longer an all-around guru or "builder." Today, the CIO functions more as a general contractor (supervisor) of IT outsourcing vendor relationships.
Customers are moving toward one-stop shopping for outsourcing, but they also want best-of-breed solutions. Therefore, larger companies are less interested in "extreme" outsourcing whereby they hand over to an outsourcing vendor complete responsibility for their entire IT infrastructure. Large companies want to select the best solutions available, even if procured from a variety of vendors. In contrast, smaller companies may still find "total" or "extreme" outsourcing appealing whereby they, in effect, depend entirely on outsourcers for their back office and IT infrastructure.
Also, large organizations are increasingly skeptical that any IT vendor can "do it all," including IBM. Customers are maturing and moving up a learning curve. When data center management is outsourced today, applications are usually kept in-house, or given to a different vendor.
Contract consultants are being used with increasing frequency. They are advising customers to avoid long contracts, aim at 3-5 year durations, insist on best-of-breed solutions and a favorable value metric.
</td></tr>
<tr><td>Keane 2</td><td> Customers are developing a much higher comfort level than ever before with the outsourcing of more comprehensive departmental functions. They like the idea of IT-oriented facilities management with us as a partner.
Some consultants are now charging a "success fee" for introducing vendors to prospective customers. Example: Everest, which has a vendor/client exchange service. Clients are typically aware of consultant fees, but consider them part of the total cost of a deal. While consultants never take responsibility for a client's decision, it is clear that there are times when they are able to dictate to the customer which vendor to select.
However, the use of consultants doesn't eliminate the need for a good sales and marketing effort. Consultants can be a positive element of the total sales process, particularly if they have strong personal relationships and reputations.
Important outsourcing consultants include, in addition to Everest, Gartner, Technology Business International (TBI), Technology Partners International (TPI) and Transition Partners, along with The Outsourcing Institute.
Vendors entering the market need to convince these consultants of their value proposition.
Customers are getting into more sophisticated types of contracting and they are using outside consultants. There is increasing pressure to improve SLA promises. The challenge is to deliver business value based on demonstrable metrics and performance measurements. Historically, the federal market has been more demanding in this regard than the commercial market, but that is changing rapidly. There is much business available for maintenance of legacy IT systems, but this work is being rapidly commoditized and is no longer considered attractive by vendors.
If you look at the IT outsourcing market from the top down from the vendor's point of view, the most profitable types of business are:

A combination of new application development and maintenance of existing applications
Consulting-oriented work to plan, build and strategize new IT structures
Least profitable is data center management and transaction processing.

Also attractive, application management contracts that include e-solution development work. </td></tr>
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	Keane's formula is: • Plan – consulting, strategy • Build – e-solutions, Web-enablement • Manage – full application management outsourcing and/or development, data center management (or federal seat management)
Lockheed Martin	The most important change over recent years has been the government's decision (mainly DoD) to give up insisting on "bespoke," or customized IT solutions, either equipment or software. Now, the government prefers to buy commonly available solutions off the shelf. This represents a big change. Another important change has been the increasing use of outsourcing consultants by customers. Today it is common to spend 5% of the total contract value on paying consultants—and they work for both customers and vendors. Preferences IBS would prefer to do high-end, high value-added e-business projects, but to date the company has done somewhat small deals, which are typically broken in to pieces and awarded to multiple vendors. IT infrastructure management is still profitable, but it is very difficult to differentiate yourself in this segment from your competitors. The skills have been commoditized. Also, these projects are complex and require highly developed project management skills on the part of the vendor. This is a perennial challenge: how to differentiate your company and your offer from competitors. IBS doesn't play in the same league as IBM, EDS and CSC. IT targets deals in the hundreds of millions of dollars, not billions. Respondent describes IBS as "big enough to do the job, but small enough to give attention to customer needs." In contrast, for a company such as IBM, NO deal is big. IBM has a pipaline of $1 billion deals. For IBS, the "sweet spot" is a deal in the $100-500 range. There it can compete effectively. IBS bills itself as a "full-term participant" that is more accessible to client managements.
Perot Systems [#22]	The ability to do something better, faster and cheaper is the price of entry today. Clients today are looking for strategic partners that offer breadth and depth. Clients are seeking ways that they can drive business to fewer partners and hold them accountable for the results. Basically treating their service providers as an extension of their IT department and business units. One other area that we, the incumbents, seem to be ignoring is the possibility of new competitors in our space. We have done a very good job of warning our clients that, in the new economy paradigm, competitors are in every vartical. We point to Enron and others as examples. The creation of sharad services groups that are independent of their parents possess industry knowledge, relationships, and an understanding of industry applications and technologies that can be tapped as solutions. They have been authorized to capture revenue from other firms, but because of their organizational structure, they have not been successful. I see these as potential back office competitors. One the front end what if Amazon, Yahoo or Ebey decided to get into the CRM space? The virtual companies we are building today possess the skillsets and knowledge to be our potential competitors tomorrow.
Lockheed Martin [#4]	Important Changes Underway in the Outsourcing Industry Primary among these, at least in the federal market, is the anti-outsourcing lobby. Respondent believes strongly that union-led efforts to kill federal outsourcing will lead to disaster. The A-76 machinery in place that attempts to verify the cost-effectiveness of outsourcing is not working well because of the many difficulties in the way of computing federal costs. "Savings" can be deceptive, primarily because they ignore the need for technology "refresh." The desire of federal employees to assure their job security is understandable, but doomed. The skills shortage will grow ever more acute. Also, the federal "customer" is incapable of foreseeing technological advances. The slow procurement cycle ensures that almost whatever is purchased will be obsolete, or almost obsolete by the time it is implemented. The skills shortage will worsen. Why would young techies want to work for the government, the respondent asks, when they typically have more computing power on their wrist watches,

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<tr><td></td><td>or in their PDAs than they can find on many agency desktops. Techies will be attracted to work environments were they can use cutting-edge technology. Obsolete federal hardware only exacerbates the flight of young techies to the commercial sector.</td></tr>
<tr><td>SAIC [#20]</td><td>Customers are becoming more sophisticated and outsourcing is becoming more acceptable. CIOs used to oppose outsourcing; now, they embrace it. The size of deals is getting smaller, which reflects—in part—reluctance to give up too much control (customers are giving a larger number of smaller-sized outsourcing contracts to multiple vendors).

Question: Is the role of customer-engaged consultants becoming more common and more important?

Yes, but consultants can create a conflict of interest with clients because they are paid on a time-spent basis. Therefore, it is to their interest to lengthen the sales/proposal/bid process rather than shorten it.

When asked if vendors could, or should depend on consultants to bring them into outsourcing deals in new markets, respondent commented that this was a "loser's point of view, depending on the consultants used." He said that Cap Gemini had won some excellent business through TPI and other consultants because, while the vendor's work was good, it had little name recognition in the U.S. market. Consultants liked being able to recommend a lesser-known, but high-quality vendor to clients because it made them appear more competent.

Respondent emphasized that the use of consultants to bring in outsourcing business should be regarded as merely an alternate sales channel, not one that any vendor could rely on exclusively.</td></tr>
<tr><td>UNISYS</td><td>In the federal marketplace, UNISYS believes that outsourcing will play a significant role as government is being downsized and asked to do more with less. A-76 issues and unions need to be addressed.</td></tr>
<tr><td>USInternet-working</td><td>Today, there is much better recognition of the value of IT outsourcing than there was previously. And there is better understanding of the ASP model—albeit acceptence has been quicker in the commercial market than in the federal market.

Currently, USI has a total of 208 clients, signed over the past two years (during the first year of the company's existence, it was not operational). Total value of signed contracts exceeds $400 million. USI gained its first public sector client in 2Q 1999, its second in 3Q 1999, and the remaining ones in 3Q and 4Q 2000.

Use of Consultants

Respondent: "I don't like consultants because they are difficult to manage. I prefer the direct sales model.

We rely on outsourcing consultants to bring us into deals, but we must maintain our own in-house sales force as well. At the least, we need sales closers."</td></tr>
<tr><td colspan="2">9. Top down, which types of outsourcing can you do most profitably? (Reasons?)</td></tr>
<tr><td>COMPAQ [#18]</td><td>• Full IT and Process Outsourcing – ability and expertise to manage the clients desired business results.
• "Next Generation Mgmt" Infrastructure – ability to manage the risk of transition to the clients' desired state.
• EWorkplace (asset mgmt) – the managament of all change, moves, adds around network access devices such as: desktop, PDA, messaging and enterprise help desk support.

<u>REASON:</u> expertise, process and methodologies that can provide the desired consistent office environment required by the client to perform their business offerings is situated in a highly competitive market. (4) Customer Care (Enterprise Help Desk)

<u>REASON</u>: specific helpdesk support (level 1) is focused usuelly on cost reduction for the client. The market is a highly competitive market when the offering is transitioned to an enterprise approach integrating requirements for multi-language, application and international support the value to both the client and the sourcer increase. (5) Private Storage Utility and Business Continuity

<u>REASON</u>: This offering provides the integrated support of both product and services to secure the valuable information of our clients.</td></tr>
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Convergys	Most profitable – Billing solutions due to high transaction volume; next call centers. Company prefers longer-term contracts (5 years +) in order to maximize profit.
Entex	Without a doubt, network management and consulting are much more profitable for Entex than "break/fix" desktop services. Yet, Entex will not enter into a desktop services contract on a low or no-profit basis in the hope that future, lucrative additional business will materialize to make the overall relationship profitable. While it is true that having an incumbent contractor relationship almost always results in incremental business, to depend on that business from the outset is a recipe for disaster.
Fed Data	Types of Outsourcing that Can Be Done Most Profitably • Enterprise seat management, meaning bundled contracts for help desk, network menagement, LAN, break/fix work, HW/SW acquisition, some application management and development work • Network/LAN administration • Help desk (which has been mainly commoditized) • Web hosting/Web site development Contracts here are small, but likely to grow in volume and importance for the government. Logicon is doing some work on the state and local government level, including data center management. The potential for this is good, but contracts at present are small. E-gov is still in the future.
Getronics	Getronics sees excellent potential in seat management in the federal market. Getronics has experience in dealing with unions in non-seat management contracts. Confrontation is unnecessary. However, vendors must recognize that unions have an inherent, vested interest in increasing headcount, not reducing it, which creates fundamental conflicts of interest between unions and outsourcers. Vendors need to face the truth: "You can't be everything to everyone." Respondent believes strongly that you need to be able to use the same software tool set for a significant period of time (in order to amortize your costs). Yet, this did not mean that Getronics was inclined to acquire the software companies that are its current partners and on which it depends for elements of its, in effect, proprietary seat management solution. Reason: "We don't want to be in the software business." Getronics does, however, build/assemble a basic tools that it uses repeatedly. It does NOT buy off-the-shelf solutions from Tuvalu or Computer Associates.
Litton/PRC	For us, the most profitable type of outsourcing business is network services and remote storage. Desktop services trails. In our experience, commercial contracts are usually at least twice as profitable as federal ones, i.e., with 20% margins rather than 10%. We would enter a market with low profit margins (5-6%) only if we thought there was good potential to move the business up quickly to the 10-12% level. This group accounts for 20% of total revenues. There are no staff training problems that are critical to our group.
Perot Systems	Business Process Outsourcing: Most organizations today view the automation of a business process as a major milestone, and in many cases it is. However, the true value is to determine if the process is worth automating to begin with. Business Process Automation provides the initial quick hit to secure funding from CapX. The real value though is how a particular process, or subprocess, can be redesigned and measured to become better aligned to the corporate vision and strategy. The inefficiencies once identified and resolved deliver significant operational and cost improvement and in some situations positively affect top line growth. Application Outsourcing: We have the ability to transfer this work to a JV in India, HPS, that is a Managed Level 5 of the Capability Maturity Model for the Software Engineering Institute. This disciplined process approach provides us with efficiencies that reduces the time and risk in making enhancements and performing maintenence of the chosen application. Additionally the Indian labor rates are significantly lower than US based rates allowing us to perform this service better, faster and cheaper than our clients. Web Management Services: The ability to combine our infrastructure competency with HPS

	enables Perot Systems to compete very effectively in this space, especially when the requirement is high availability supporting a mission critical application. Program Management: Perot Systems will outsource the management of a single or multiple projects and leverage ours, or the clients, project management methodology. These engagements typically involved some type of risk/reward component which significantly increases the operational margins for Perot.
SAIC	SAIC can do the management and development of SW applications most profitably—along with related consulting. For a somewhat lower margin, it could also do network management profitably. Clearly, data center menagement and desktop management were the least profitable types of outsourcing for SAIC.
UNISYS [#16]	Data Center, Infrastructure and transaction processing.
10. In which type of outsourcing do you have the most expertise and success? (Future?)	
ACS Government Solutions Group [#8]	Information technology outsourcing
CSC	In the federal market, CSC considers application management an important strength. In the commercial market, application management is typically bundled with a variety of other services in the commercial market. During the last three years, CSC was well positioned to leverage commercially tested solutions to federal clients—as evidenced by wins at IRS and the Army logistics contracts. Also, experience with delivering on SLAs is critical: vendors in the federal market must be comfortable with performance-based contracting. This is also a great advantage in the commercial market. Beyond that, CSC has 20 years of experience and demonstrated success delivering on contracts for the operation of military bases—despite the political power of unions.
Fed Data	Fed Data's primary expertise is in the seat management/enterprise management area, and secondarily in network management.
Litton/PRC [#1]	Our areas of outsourcing expertise include: • Help desk • Storage on demand (for customers that don't want to buy new storage capacity directly, but prefer that the vendor put his own equipment on the customer's site and operate it). The key to success, for us, in the data storage market is to be able to set up hardware at the customer's facility. It can also be done remotely at our facility, but there is more competition in that approach. We like going to the customer's site because it (literally) gives us a foot in the door with potential for increased account penetration.
Perot Systems [#22]	Enterprise outsourcing today. BPO in the future
UNISYS [#16]	Data Center and Infrastructure management.
11. What process do you use for computing the cost of contract bidding?	
Compaq	Compaq has disciplined approaches to pricing.
Convergys [#19]	Company uses a standard price book that includes Total Cost of Ownership models (TCO). These will vary depending on the billing platform used. Convergys tries to create a strategic partnership with customer: "We try to help the customer understand his TCO—then we show how costs can be cut."
CSC	CSC does a comprehensive solution development/solution design estimate, including the cost of implementation before pricing a deal. Company uses a "cost build up" model (others use a cost-savings or percentage of promised savings method). In the cast of most contracts, there is a base cost to the customer with adjustments according to business volumes. It is important to build variability of parameters into the contract from the start. As an example, due to a late acquisition, the Nortel contract required an adjustment of expected transaction volumes even before the contract was signed.

Entex	Generally, the average size of Entex's bids is small. Large bids require top management's approval. Entex doesn't go cold-calling. It will usually take a piece of a larger contract and try to expand the relationship. The proposal costing model is based on clear definitions of the work to be performed. This is reviewed periodically and profitability is recalculated. Independent audits confirm these numbers. Entex does offer work priced on a volume basis. Key factor: build into SLAs from the outset a clearly defined pricing mechanism that adjusts for changes in the customer's business model. SLAs are more of a problem in Europe. Also, success in pricing requires excellent Project Management skills. Europe is more advanced in the training of project managers (esp. Siemens, which has a high reputation in this area).
Fed Data	Fed Data uses models for projecting cost and pricing models as part of the proposal/bid process. To be worthwhile, seat management contracts need to be sufficiently large to give vendor economies of scale. Cost projection models can be re-used—they are not developed de novo for each new bid. Fed Data uses a knowledge management system and believes that, in general, this approach could be used for bidding in the commercial market as well.
Getronics	Getronics has no "black box" that it uses to compute contract profitability: "We just tinker and adapt." To respondent's knowledge, there is no good contract cost/profit model. In reality, "outsourcing contracts are like DNA, each one is different. Pricing is an art.." because there are no precise data. Expect that the costs, terms and SLAs of an outsourcing contract will be subject to continual change. It is common for vendors to "take hits" in the form of unexpected costs. In the federal market, there is always a security dimension to the work (with associated costs). When agency needs change, and their budgets do not, we are often in the position of negotiating adjustments in SLAs, faster or slower refesh rates, return to service guarantees, etc., in order to keep contract costs within budget AND meet the agency's current requirements. The trick is always to figure out how to do this, make a profit, and NOT change the customer's cost.
Litton/PRC [#1]	We have no master computer model for computing the profitability of a contract.
Lockheed Martin [#4]	Breakeven on contracts is computed according to a sophisticated model that we use. With it, we can track profitability over time and taking into account changes that occur during the life of the contract. In general, we expect breakeven to occur about 1-2 years into a contract, assuming an average term of seven years. Longer contracts clearly provide better opportunities for economies of scale. Upfront outlays can be problematic. Respondent disqualifies IDIQ contracts from ever being considered "outsourcing," which is done on a fixed-task, fixed-cost or cost-plus basis. In respondent's opinion, an IDIQ contract is "a license to spend marketing dollars." IBS uses an in-house model to compute the cost (and profit) from contract bidding. Typically, outsourcing is a low-margin business in the early years. In the past, IBS tried to take the "business case" of the customer into account (stage in company life cycle). Now, IBS prefers multiyear deals whose revenues are booked on a percentage completion basis. IBS prepares bids on a forecast of total contract costs.
Perot Systems [#22]	Each opportunity is assigned a cost center where all expenses for people and material are assigned.
12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?	
ACS Government Solutions Group [#8]	Compared to the 3,000-4,000 people in the IT Technical Solutions part of the Government Solutions Group, the business development staff totals only about 15, plus another 12 that work on proposal preparation. Sales and marketing costs are higher in the commercial market for many reasons, including higher levels of compensation. For example, while a salesman in the federal market may earn a salary of $80-120,000, on the commercial side salaries range from $0-80,000. Why zero? Commercial salesman can forego salary in favor of a percentage of the size of the total deal (typically 2%). As a result, they can earn several hundred thousand dollars.

Convergys	Beyond revenues from outsourcing, Convergys typically derives 20-30% of total revenues from provision of Professional Services in the IMG division. This is usually for some kind of system integration work. Company is often hired to build this component into its original project management plans and contract provisions. This comment was made in the context of asking if the company had ever low-balled a contract proposal for little or no profit in order to get a foot in the customer's door. Respondent denied this (they all do), but admitted that, at times, it could shave the outsourcing contract profit margin if the SI professional services component were large enough. Convergys tries to extend contract durations well before their expiration in order to reinforce client relationships.
Litton/PRC [#1]	All opportunities are modeled with assumptions of the desired target level that we believe we can achieve and are reviewed periodically.
UNISYS [#16]	Yes Our bids are based on contract type and requirements.
	13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)
ACS Government Solutions Group [#8]	Minimal
Convergys [#19]	Respondent believes that company's sales costs are relatively low, at 5% of total contract value—or less. He believes that they could be even lower in the federal market. He commented that he thought there were higher contract capture costs in the federal market, along with a higher level of "hassles." He expects the company's sales and marketing costs to RISE, albeit not so high as the average for software vendors (10-15% of sales revenues).
CSC (1) [#3]	Many task orders include a host of smaller deals that can be bid at little cost.
CSC 2	Business development costs are clearly higher on the commercial side—basically because there is more travel required. All federal clients are located conveniently in one central location. Nevertheless, federal proposal preparation costs are higher than the corresponding costs to prepare a commercial bid. CSC manages costs carefully; all expenses are evaluated with care so that they cannot become burdensome. Company uses a "pursuit model" scaling that computes (and sets a cap on) marketing costs as a percentage of total contract value. Commercial marketing challenge: each company has its own organizational hierarchy, yet vendors must learn how to streamline their sales approach and go directly to the top decision-makers.
Entex	Marketing costs for desktop management are less than those for "complete" or "extreme" outsourcing, i.e., total data center management. National government bids are more expensive (especially in Europe). However, this is a non-issue for Entex, whose business is U.S.-based. Marketing Strategy How does Entex prioritize its prospects? According to (1) size of customer by revenues [Fortune 100-500 ranked]. Currently, Entex has 50 active customers from among the Fortune 100. In particular, Entex pays attention to the "IT intensity" of prospects, or the percentage of revenues allocated annually to the IT budget. By this ranking, manufacturing is lower than financial services because companies in the sector tend to have smaller IT budgets in proportion to revenues. The sweet spot: companies that spend $100-500 million annually based on revenues of at least $1 billion. Entex works prospect lists with some attention to geography, even though outsourcing work can be done remotely. Salesmen usually focus on companies based on HQ and then follow them geographically. The approach of Entex is very different from the approach of Siemens in Europe. In Europe, there is more emphasis on geography, with staff allocated on a geographic basis at regional

	centers, with less on-site staff. In contrast, in the U.S. Entex maintains large numbers of staff working at customer worksites. Other differences between the U.S. and Europe Because the mobile telecom environment is more standardized and more advanced in Europe, wireless LANs are more widespread in Europe. The U.S. market is 3-5 years behind in this respect.
Fed Data	Overall, respondent believes that marketing costs at Fed Data run about 20% of the total cost of doing business, which includes administrative overhead, HR and related, direct costs. Yes, 20% is high now due to various unusual circumstances. He would expect a normal level for such costs to be 10-15% in the federal market and 6-9% in the commercial market. The primary reason by sales costs are lower in the commercial market is that the sales cycle is much shorter.
Getronics	Respondent did not believe that there was much difference, ultimately, in the level of sales and marketing cost levels in the federal and commercial markets. But there is a big difference in the cost of marketing a seat management contract and prospecting for new business on a labor/materials basis. In that case, vendors participate, in essence, in a beauty contest with each other. The process for awarding GSA seat management contracts has been streamlined considerably. They can now be completed in less than six months, while other types of contracts take 6-9 months—and incur higher sales costs. Getronics spends an average of $200,000 in sales costs for each seat management contract that it wins. Decisions may come more quickly in the commercial market, but contract implementation can be slower. Obviously, it is easy to identify federal agency sales targets. This is a more difficult and costly process in the commercial market. On the commercial side, it is usually cost-effective to use consultants. Importance of inside contacts? "We had NO presence at all at Treasury, but we succeeded in winning new business in open competition, without pre-existing relationships." Respondent believes that this is exactly the experience that GSA is promoting.
Independent Consultant	On this point, burdensome Bid and Proposal costs (B&P) can contribute to undoing a vendor's success. This process is generally more complex in the federal market. It is easy to waste money in either the federal or the commercial market if you don't target your efforts carefully. You should always be asking the same question: where can I add value? Take care regarding your relations with outsourcing consultants. Some of them are NOT the vendors' friend. They are making it harder for vendors to close deals insofar as they run up costs. For example, a consultant may believe that it both enhances his client credibility (and fattens his fee) if he summons ten vendors instead of three to present bids. Yet, it is usually more realistic to ask only 2-3 to incur the expense of preparing and presenting bids and the others typically waste their time and money. Truth be told, there is a lot of self-deception at work on all sides of the equation, customer, consultant and vendor.
Litton/PRC	The commercial market has higher sales and marketing costs. As noted earlier, it will cost substantial amounts of money to achieve name recognition initially in the commercial market. Note that many sales and marketing practices that are standard in the commercial market are prohibited in the federal market.

Lockheed Martin	Most outsourcing transactions make provision for imbedded sales and marketing costs along with technical costs. In respondent's opinion, marketing costs are lower with commercial outsourcing deals because the federal procurement process can be quite lengthy. For example, a $750 million federal market deal took three years to negotiate and cost LM millions in expense. In contrast, a commercial deal valued at $350 million required only 12 PowerPoint slides to close the sale. <u>Key point: you must know who the decision-makers are.</u> • IBS wants to do deals that are big enough to eliminate smaller competitors. Above $1 billion, there are only a few players. • IBS doesn't make low-margin contract bids in the hope that we will be able to scrounge some profit out of the deal in future years. This is simply self-deceptive thinking. Sales and Marketing Vendors should establish good contacts with the principal outsourcing consultants, including Transaction Business International (TBI), Transaction Partners International (TPI), Transition Partners, KPMG, the Outsourcing Institute, and the Outsourcing Exchange. Also, vendors should participate in industry conferences and events. Respondent doesn't believe that vendors in the commercial IT outsourcing market need hundreds of salesmen. They only need to establish contact with these few consultants mentioned above. Using them effectively can leverage a vendor's business from zero to $1 billion in 4-5 years. *Take Exult as an example. It went from zero to $3 billion in one year—with no sales force. The company focuses on large BPO, single contracts annually.* Any vendor can enter the commercial market quickly and make a big impact by using consultants. No need to establish a geographically-oriented sales force. There is much pricing pressure and commoditization of services in the IT outsourcing market. As a result, it is very important to avoid excessive SG&A spending—especially because these costs don't rise in proportion to the size of the deal. They remain the same. Ergo, it is more cost-effective to target larger deals.
Perot Systems	Currently, Perot Systems does not compete for Federal contracts. This should provide the strongest answer of the burden in pursuing that business. As for commercial, we are selective on what we pursue so the overall cost, while expensive, is not over burdensome.
Raytheon [#7]	In general, marketing and sales costs will be higher in the commercial market. Although individuals are re-trainable, it is likely that a brand new sales staff would be required by an effort to break into the commercial market from a springboard in the federal sector. Worth noting, personal contacts are critical to success in both markets and salesmen are likely to have cultivated these contacts over a period of years while working successfully in either one or the other of these markets. Marketing and selling costs generated prior to presentation of a proposal are difficult to contain. Keeping such costs to a reasonable level is especially important in the commercial market. Their costs need to be better focused, i.e., targeted to specific industries or industry segments. Vendors need to give careful consideration to their core capabilities and show that they understand the needs of commercial customers.
SAIC [#20]	In the commercial market, a vendor may spend more as a percentage of the total size of the contract. In the federal market, vendor marketing costs may be lower as a percentage of (larger) sized contracts, but the absolute dollar amounts will be similar to costs in the commercial market. While the cost of sales is higher in commercial markets, the gross profit margin is also substantially higher, so deals in that market can bear the higher sales costs without depressing net profits.
USInternet-working [#14]	Finally, while there are potential prospects in every vertical industry, you must spend your sales and marketing budget according to targets and priorities. Spending in too many directions at once will prove unsuccessful. Insofar as there is a tendency to "verticalize" the sales and marketing staff, it is best to let this happen naturally in the course of doing business, rather than by top-down planning.

UNISYS [#16]	Some Federal bid/sales expenses are much lower than in the commercial market.
14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)	
ACS Government Solutions Group [#8]	No, it has not
Convergys	This issue doesn't apply to Convergys to any significant extent. While the company can do "co-sourcing" whereby it takes over the customer's existing call center—and in those case could transfer customer staff to the vendor's payroll, this would be exceptional. Most company work is done remotely by its own full-time staff. However, Convergys has made about 20 successful acquisitions and its ability to absorb acquired staffs comprised an important element of its success in integrating acquired companies.
CSC	CSC has never had difficulty in absorbing qualified staff acquired through outsourcing deals. In fact, it has had exceptional success in this area. For example, in the case of the Army Wholesale Logistics contract, 100% of target staff elected to transfer to CSC. Over the years, CSC has absorbed 30,000 people in this way, many of whom have advanced to high-level positions in the corporation. Protests—CSC has participated in very few federal contract protests. As a matter of policy, the company tries to avoid protests. As an exception, CSC did protest a Boeing award because management believed that the criteria for the award had been unclear. A legal decision was needed to clarify the issue. Ability to absorb new staff resulting from an outsourcing deal has never been an issue for CSC, which has a very high rate of acceptance of employment offers. What is the secret to the company's success in this area? CSC has always made an effort to attract and retain good people and there has always been a flow of staff upward through the organization. New hires know in advance that they have excellent opportunities for advancement at CSC.
Entex	This is not at all a problem for Entex. The company tries to redeploy, relocate staff at the end of a contract insofar as possible. Those that cannot be relocated, or used elsewhere, are let go. Overall, the firm's retention rate is very good.
Fed Data	So far, Fed Data has had no problems in transferring civil servants to vendor's payroll. Such transferred staff usually needs training, particularly in company techniques and processes.
Litton/PRC [#1]	NO
Raytheon [#7]	Generally, there are few problems involved with absorbing staff through an outsourcing contract—particularly beceuse staff is usually guaranteed no more than two yeas of employment. At that point, the best can be retained and promoted; the nonperformers can be let go. In truth, few federal IT workers feel confident in their ability to compete successfully in the commercial market. Even so, parity and benefits clauses are built into outsourcing contracts in order to assure a high transfer rate.
SAIC	Difficulties in transferring staff as part of an outsourcing deal has not been a problem for SAIC—partly because it avoids commodity data center contracts. If client wants to effect a staff transfer in order to reduce headcount, HR processes and procedures become very important. However, for high-margin, high value-added work, staff transfers are rarely an issue. Overall, SAIC as an employee-owned firm has little turnover. This status gives it a "positive discriminator" in the market, i.e., it is perceived to be a highly desirable new employer.
15. What is your policy toward dealing with unions? (How important?)	
Compaq	We are open depending on the opportunity, the legal constraints of the client/labor relationship and the geography.
CSC	CSC has some experience with unions, especially in Europe and in the public sector. CSC tries to "manage" union relationships so that unionized employees remain with the customer.
Lockheed Martin	IBS does have some experience with unions, but mainly on the federal side.

Perot Systems [#22]	There is no specific policy. Each contract is addressed on a case by case basis.
SAIC [#20]	They will remain marginal players in the IT industry for the foreseeable future.
The Outsourcing Institute [#2]	On the issue of private sector unions, respondent advises vendors to try to avoid dealing with unions. They could create serious and problematic issues.
UNISYS [#16]	Not applicable.
USInternet-working	Because USI does not "threaten" to take over the data center, it keeps a lower profile than the SI vendors and has not been target of the anti-outsourcing groups. DoD? No business there for USI yet. The current sales staff has entirely a civilian orientation.
16. How ready is your organization to bid on contracts in the federal (or commercial) market? What would you need to do to become ready?	
ACS Government Solutions Group [#8]	We already do this and have many reference-able clients.
Perot Systems [#22]	We are prepared to bid any contract we choose to pursue in the commercial space.
SAIC [#20]	We are actively involved in both commercial and federal outsourcing.
17. What changes are you seeing in customer motives for outsourcing IT?	
COMPAQ [#18]	They are considering the strategic nature of outsourcing ability to impact business results quickly.
Lockheed Martin [#4]	In the federal market, established procurement processes level our prices. In that market, if you exceed your competitor's bid by 5%, you are out of the game. Price is important and high-priced vendors are eliminated early. In contrast, while pricing is important in the commercial market, the environment is more elastic, assignments and processes more varied. In the 1980s, customers used outsourcing mainly to achieve cost-savings. In the 1990s, customers are outsourcing because they lack the internal IT staff required to meet their needs. Also, they give much more priority to time-to-market issues. Timing is critical and outsourcing is seen as a shortcut to market.
Perot Systems [#22]	Customers are not looking for cost reduction as the primary reason to outsource. Service levels and value to the business units are what they are focused on today. This should be expected since most are evaluated based on customer satisfaction surveys.
UNISYS [#16]	They are increasingly motivated by the IT skills shortage; also, corporate downsizing is a critical issue.
18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?	
COMPAQ [#18]	Company size cannot be limited universally to revenue, this criterion is sensitive to other key factors such as industry, business model and services or goods provided.
Convergys	Convergys doesn't categorize prospective customers according to revenue size. Rather it looks for "emerging" companies that appear poised for rapid growth—which would mean rapid expansion of its relationship with Convergys as well. The important issues are customer's financial viability, strategy and growth potential. At times, Convergys has elected on its own NOT to continue a client relationship because it had determined there was no real profit potential.

Lockheed Martin [#4]	Customer size by revenue is an important marketing criterion because it bears a direct relation to the size of the outsourcing deal that can be put together, i.e., customer spending is linked to revenue by a certain percentage. However, as indicated above, ALL of IBS' outsourcing deals were won through relationships with consultants (who are paid $2,000 daily). Note in particular the success of The Outsourcing Institute (OSI) in bringing vendors new business. Also worth noting, consultants like OSI are attempting to set up a new electronic marketplace that will match outsourcing customers and vendors.
Perot Systems [#22]	Companies of any size can benefit from an outsourcing relationship. The ability to select a partner you can trust and focus on core competencies offers significant value.
UNISYS [#16]	Past performance should be more important than company size
19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?	
COMPAQ [#18]	Control of proprietary data is a trust some of our clients place with us. It must be treated as such.
Fed Data [#17]	Federal agencies are very aware of the importance of secure data management, but seat management outsourcing tends to be accepted without provoking fears of loss of control. This is primarily a problem of perception (or misperception). For example, a remote networking management solution doesn't necessarily give the client less control—only differerent, i.e, not on site.
Perot Systems	Customers are sensitive to the areas of control & IP (Internet Protocol). Control has not been a sticking point. If there are elements in the outsource that include proprietary data, ownership of the data remains the clients but the processes we put in place to manage that information remains Perot's IP. Clients typically do not have an issue with you maintaining the IP you bring to them, it's the IP you develop with them that can become a sensitive area.
UNISYS [#16]	In the federal marketplace, control is very important issue
20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)	
COMPAQ [#18]	It depends on the nature of the business arrangement. Unbundled services are typically provided in the Govt. Market or for services that are highly competitive and basic i.e., help desk out-tasking, etc.
Perot Systems [#22]	Today the bulk of our business is bundled but we are moving towards unbundled. Our preference is to manage in a bundle, but it doesn't matter what we want, it's what the client wants and feels comfortable with in the scope of a relationship.

Exhibit D-2

Tabulation of Vendor Interview Survey Responses by Respondent

ACS Government Solutions Group [#8]	Background ACS considers itself a "pure play" outsourcing vendor among vendors that derive virtually all of their revenues from IT outsourcing. Overall, the company's $2 billion revenue mix is two-thirds commercial, one-third public sector, which includes federal (both civilian and DOD) as well as state & local. In the Government Solutions Group alone, revenues are split between IT solutions ($300-400 million annually), ACS Defense ($100 million annually) and Business Application Systems ($100-200 million annually). The state & local government division does about $600 million annually; another $100 million of state & local business is done outside of the Government Solutions Group. The respondent has been at ACS for two years. Prior to that, he worked at Wang and was part of the capture team that won the ODIN seat management contract. Most of his professional experience is on the DoD side of the market, especially in electronic warfare. **Market Orientation** Within the federal market, ACS targets specific agencies as their best sources of business growth, ranked according to the best match between ACS areas of expertise and agency requirements. Other considerations include: • Where do we have the best technical solutions? • Where can we find a "level playing field"? (In some agencies, the incumbent is so well entrenched that it is virtually impossible to win new contracts.) ACS considers itself to be the top vendor in the network security market segment, as evidenced by work for NASA. Also, ACS considers itself to be the biggest factor in the imaging market where it does $400 million annually. In seat management, ACS has 300,000 seats under management. **Market Direction** Is your business moving "upmarket"? ACS considers itself to be a "services company," which means that it wants to provide bodies and sell solutions. It wants to build on its experience with the ODIN contract. GSA seat management has not been very successful, but NASA's ODIN contract was structured differently. OAO and ACS each has responsibility for multiple NASA sites. Typically, seat management contracts are difficult because vendors must interact with a multiplicity of other vendors, as well as with civil servants. Respondent: "Give me an empty room, and would love to do seat management." Better are contracts where seat managament is included along with networking and application services. The ACS Government Solutions Group works closely with its counterparts in commercial sales. Staff meets regularly, compares notes. Some prospects are marketed jointly and there has been much benefit from this close cooperation. The commercial culture provides depth of knowledge in the area of "best practices." The federal market culture provides excellent depth of project management skills, technical discipline and rigor of methodology. In a few cases, commercial clients have been brought to see what is being done in the federal market. They have been so impressed that commercial deals were closed in the offices of the Government Solutions Group. **Barriers to Entry** Some barriers to entry on the federal side include the following: • A vendor must be an incumbent at an agency in order to get a foot in the door. • You need to have established personal relationships—and you can't walk the hallways to introduce yourself in secure environments. Access is a major issue. • The government doesn't really want full competition, which makes it difficult for a new vendor to break in. Because the federal procurement process is so onerous, despite recent efforts to streamline, there is an increasing tendency to make new awards to incumbents as an expediency. Consequently, it can be very difficult to unseat an incumbent. Some barriers to entry on the commercial side include:

- Marketing must be undertaken in a totally different way, cost are higher.
- You need new people for commercial work, or you must undertake a long, difficult re-training effort.
- For ACS, the best way to enter a new market is to acquire an existing company with a good reputation and on-going business. This can provide a platform for further expansion.

How important is cost, or availability of capital?

While ACS doesn't have anything like the deep pockets of Litton, nonetheless, finding "proposal money" has never been a barrier to seeking new business. (Litton could afford to spend $10 million to cover proposal and bid preparation costs; at ACS such an amount would be considered astronomical.)

Capital isn't typically required for asset acquisition connected with outsourcing deals. ACS prefers to team with leasing companies that provide whatever financing is required. Overall, IT outsourcing (bodies + assets) requires more capital than DoD contracts.

Changes underway in the outsourcing market?

- Recent changes in the federal procurement/contracting system have made it much harder for vendors to win business away from incumbents. These changes function as an incentive to obviate the burdensome paperwork required to evaluate new bids by simply renewing contracts with incumbents.
- Aggregation of discrete types of work into ever-larger megacontracts makes it increasingly more difficult for small and medium-sized vendors to win awards.
- As a result, they are obligated to win subcontracts from primes that are reluctant to give up shares of their business, unless absolutely necessary. Smaller vendors are unable to bid directly for these large contracts, which is fueling the drive toward partnering (sometimes reluctantly).
- Despite all the publicity to the contrary, the government does not seem to be enforcing set-asides to small business—which is facing tough times in the federal market for the reasons noted above.
- Because Wall Street determines what a company's stock is worth, ACS—like other vendors—has been obligated to re-invent itself as an "e-company." This has had a big effect on the federal market, but now appears to be losing steam.

Levels of profitability

From the point of view of ACS, "pure outsourcing" means providing people (bodies). This is generally less profitable than "impure outsourcing," consisting of people plus high value-added networking, application or other consulting services. "Profitability" is difficult to measure because easy assumptions don't always apply.

For example, while teaming with a prime on a contract is generally perceived to be lower-margin for the subs, ACS factors in the much lower cost of preparing proposals and bidding directly. Also, subbing generally leads to a pipeline of additional business, so it is usually worthwhile to participate as a means of getting a vendor's foot in the door to places that would be otherwise inaccessible. Therefore, while seat management and desktop service contracts may not appear attractive in themselves, they can serve as conduits to other, more attractive business.

Beyond that, respondent believes strongly that the critical key to profitability is not the size of the margin associated with a given contract, but the way in which the contract is managed and strategized, i.e., how this contract/business fits into a comprehensive sales/marketing plan.

How burdensome are sales and marketing costs?

Compared to the 3,000-4,000 people in the IT Technical Solutions part of the Government Solutions Group, the business development staff totals only about 15, plus another 12 that works on proposal preparation.

Sales and marketing costs are higher in the commercial market for many reasons, including higher levels of compensation. For example, while a salesman in the federal market may earn a salary of $80-120,000, on the commercial side salaries range from $0-80,000.

Why zero? Commercial salesman can forego salary in favor of a percentage of the size of the total deal (typically 2%). As a result, they can earn several hundred thousand dollars.

Applicast [#9]	**Background** Menlo Park-California-based Applicast is an Application Service Provider that specializes in serving the midmarket, high-tech industry ("the premier, total-solution [ASP] for aggressive-growth companies"). Recently, it merged with Englewood, Colorado-based Agilera ("the first ASP to offer a combination of hosted solutions and value-added services"). Applicast defines "midmarket" loosely as comprising companies with $0-1 billion in revenues. In a crowded field, Applicast differentiates itself from its competitors by eschewing "legacy baggage," i.e., the high overhead resulting from established infrastructure, staff consultants, etc. It was formed as a new organization specifically to serve the new ASP market. One key element of success has been to partner effectively with complementary companies. Respondent has a background in IT management and systems integration for the midmarket. Applicast wants to replace the customer's "back office" by offering required functionality on a service basis. **Market Orientation** To date, Applicast does no business in the federal market. Management considers the public sector (including federal) market unattractive because of excessive bureaucracy and the slow pace of change. Applicast wants to work with customers that are ready to transform themselves, and quickly. Applicast management perceives the public market as lacking in opportunity to achieve innovative implementations in a short timeframe. Conversely, it is seeking to build a client base among fast-growing, innovative commercial companies. It would rather expand into complementary vertical industries. For this, success hinges on the ability to understand a customer's industry-specific requirements. It is not enough to propose generic, or standardized, horizontal software applications (such as plain-Vanilla PeopleSoft). Applicast sees the most profit and the best growth prospects in "upmarket" solutions that fall within the category of Business Process Management (BPO). Applicast has no proprietary software, but does have proprietary, industry-specific packages or templates that consist of pre-configured, complementary software applications. It is critically important to "speak the customer's language." Applicast is not a BPO vendor, but believes that it has a BPO focus, or orientation. **Barriers to Entry** The most important barriers to entry in to a new vertical market are: • Capital • Time • People • Effective organization The last point is very important. Vendors need to be able to mobilize a coordinated, team effort in order to break into a new market successfully. All of the elements noted above must be organized to optimal effectiveness according to the demands of the new market. These include "subject" expertise in the new industry, technical and application expertise, and skilled support staff. **Availability of Capital** With Agilera, Applicast now has a partner with deep pockets and, as a result, suffers no capital availability constraints. This is important because the capital market virtually shut down last year for the ASP segment. Overall, availability of capital is very important because, more than anything perhaps, ASP customers want scalability (and vendors want economies of scale). Insufficient capital to scale up in order to meet customer demand would/could result in lost business. ASP outsourcers require large amounts of capital for upfront investments required by new contracts. Typically, Applicast expects breakeven after 2-3 quarters on a 3-5 year contract. **How to Enter a New Market** One way to enter a new market successfully is to provide charter, core customers with an incentive (cash rebates and discounts?) in exchange for serving as reference customers. **Changes Underway in the Outsourcing Market**

	"There is a Darwinian process underway" whereby compenies able to get the money required to build and scale, or partner intelligently, will survive. Those that cannot do this will suffer from the upcoming industry consolidation thet will occur. So far, there have been no major, high-profile business disasters resulting from failure of an ASP—but one is sure to occur, over time, with very negative consequences for customer perceptions of all ASP vendors. **Which types of outsourcing can you do most profitably?** The value chain looks like this: • BPO at the top as the highest, value-added level of outsourcing business. • Next come the "tools" providers, like Applicast, that permit customers to offload much, if not all, of their specific, burdensome business functions. • The providers of generic, horizontal (non-industry specific) software applications rank next to last. These low value-added services include e-mail, standardized HR or accounting functions and services. • At the bottom are Managed Service Providers (MSP) thet serve only as performance. ASPs must provide dependable, utility-like service against cerefully crafted SLA. The ASP model differs fundamentally from that of ordinary IT outsourcing because the ASP is held accountable on a monthly basis. It has become an industry-standard practice that a dissatisfied customer cen withhold his monthly payment. This doesn't happen with traditional SI or IT outsourcing.
COMPAQ [#18]	**Background** Respondent has primary responsibility for development of the outsourcing offerings for Compaq Global Services. He has 20 years in the business selling, delivering and building different approaches Compaq Global Services has been providing outsourcing services since the late 1980s. From an outsourcing perspective, very little of Compeq's business is in the U.S. Federal **Best Growth Potential For IT Outsourcing** Telecom, Financial, Mfg, and Retail/Distribution **Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?** We are moving upmarket to become a virtual support function to the CIO. **How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?** Developing and delivering a creditable value proposition that the clients in the new market will buy. **To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?** These factors are minimel constraints if the outsourcer has both the delivery infrastructure and resources to leverage. **What important changes do you see at work in the outsourcing market today?** The role of the CIO and technology as it relates to business success or failure has increased in importance. As a result the need to buy sourcing solutions based on results is becoming the norm. **Top down, which types of outsourcing can you do most profitably? (Reasons?)** • Full IT and Process Outsourcing – ability and expertise to manage to the clients desired business results. • "Next Generation Mgmt" Infrastructure – ability to manage the risk of transition to the clients desired state. • eWorkplace (asset mgmt) – the management of all change, moves, adds around network access devices such as: desktop, PDA, messaging and enterprise help desk support. REASON: expertise, process and methodologies that can provide the desired consistent office environment required by the client to perform their business offerings is situated in a highly competitive market. (4) Customer Care (Enterprise Help Desk)

	REASON: specific helpdesk support (level 1) is focused usually on cost reduction for the client. The market is a highly competitive market when the offering is transitioned fo an enterprise approach integrating requirements for multi-language, application and international support the value to both the client and the sourcer increase. (5) Private Storage Utility and Business Continuity. REASON: This offering provides the integrated support of both product and services to secure the valuable information of our clients. **In which type of outsourcing do you have the most expertise and success? (Future?)** Information technology sourcing. **What process do you use for computing the cost of contract bidding?** Compaq has disciplined approaches to pricing. **Do you have a dynamic model for estimating total contract profitability as changes are made over time?** Yes **How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)** Minimal **Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)** No it has not **What is your policy toward dealing with unions? (How important?)** We are open depending on the opportunity, the legal constraints of the client/labor relationship and the geography. **How ready is your organization to bid on contracts in the federal (or commercial) market? What would you need to do to become ready?** We already do this and have many reference-able clients. **What changes are you seeing in customer motives for outsourcing IT?** They are considering the strategic nature of its ability to impact business results quickly. **To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?** Company size cannot be limited universally to revenue, this criterion is sensitive to other key factors such as industry, business model and services or goods provided. **In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?** Control of proprietary data is a trust some of our clients place with us. It must be treated as such. **Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)** It depends on the nature of the business arrangement. Unbundled services are typically provided in the Govt. Market or for services that are highly competitive and basic i.e., help desk out-tasking, etc.
Convergys [#19]	Respondent is VP for marketing strategy and has responsibilities for both planning and implementation of sales globally. Also, he has done corporate planning with a focus on strategy. He joined Convergys in 1991 prior to its spin-off from Cincinnati Bell. (Convergys was formed from the CIBIS and Matrix units of Cincinnati Bell, which were the IT operations and marketing units.) Initially, Respondent was co-located in Fairfax, Virginia, with CIBIS' federal market unit. This assignment lasted three years, after which Cincinnati Bell decided to leave the federal market and concentrate on its present areas of expertise: billing, call center and customer care solutions for the telecom (mainly wireless), technology and financial services markets.

Company Background

Presently, Convergys is divided into two divisions, Information Management Group (IMG) and Customer Management Group (CMG). The IMG division represents about 60% of revenues, derived primarily from customers in the wireless telecom industry. Overall, Convergys believes that it is the dominant U.S., if not global, vendor of comprehensive customer care and billing solutions for the telecom industry. It also serves the "technology" industry, which it defines to include ISP and related computer HW vendors. In financial services, it serves banks and other institutions primarily in connection with the telecom industry and call center operations. Convergys also has a large share of cable and broadband provider billing operations.

Company does business in Europe and Latin America and is now in the process of setting up several offshore IT centers (including in Israel) from which it will serve global clients. A Latin American center is being set up with a Brazilian partner on a Build Operate Transfer (BOT) model whereby Convergys will operate the center initially, but ownership will revert over time to the local partner.

Currently, Convergys does not do business at all in the U.S. federal market.

In the 1980s, CIBIS [predecessor to Convergys] made acquisitions in order to enter the federal market, especially in the facilities management segment. By the 1993-94 period, management decided to divest all federal market operations in order to focus entirely on providing billing and call center services to commercial customers. Currently, the company is divided into two divisions, IMB = Information Management Group [formerly CIBIS]; and CMG = Customer Management Group [formerly MATRIX]. These had been part of Cincinnati Bell prior to the Convergys spin-off.

Convergys offers both products and services. These can be bundled into large, comprehensive outsourcing contracts. Alternatively, customers can purchase specific business solutions that they implement themselves. Convergys has little proprietary. Rather, it markets value-added, proprietary packages of third-party software that has been "pre-integrated" to work together. This proprietary architecture is important because of the growing complexity in the telecom market of the "rating of events" problem. This refers to the difficulty of assembling disparate kinds of transaction data from around the world, applying the correct billing and rate information in order to assure high level of customer service to client's customers.

Growth Markets

As indicated earlier, Respondent views the telecom, technology and financial services industries as the company's best growth prospects. Fully 80% of revenues are derived from the telecom sector. In the technology sector, customers include ISP, broadband providers, Dell and other IT hardware vendors. In financial services, the company works with banks primarily by providing call center services. It does no network or data center management.

Outlook for Outsourcing

Respondent believes that the market for the kind of "end-to-end" solutions that Convergys offers is growing rapidly. Demand for customer service and billing solutions will only increase. Worth noting, Convergys also offers the third component of the billing/CRM-call center triad: CRM analytics, or knowledge management that converts the billing and transaction information into useful marketing data for customers.

Cost and Availability of Capital

To date, this has not been a problem. In general, Convergys does NOT want to take over customer HW assets, but could use leasing as an alternative. Clearly, having excess capacity in your data centers is an asset. For that reason, company feels itself at a disadvantage in Europe where it does not, as yet, have its own data center facility. As a temporary remedy, it has entered into partnering arrangements. For this, the larger you are, the more clout you have. Company could use the BOT model outside of the U.S. to mitigate risk to invested capital.

At least 80% of company outsourcing work is done remotely at present (at facilities owned by Convergys); 20% is done on the customer's premises.

Important Changes in the Outsourcing Market

The ASP model is "outsourcing light." Expect sharp consolidation in this segment of outsourcing. Also, expect increasing demand for, and use of offshore outsourcing facilities. Convergys is moving in this direction and will likely announce such a facility soon. It already

	has a data center in Canada. The role of consultants to expedite outsourcing deals will increase. Convergys has had relationships with them in the past. They can provide critical help when a vendor moves into a new market. **Most Profitable Kinds of Outsourcing** Most profitable – Billing solutions due to high transaction volume; next call centers. Company prefers longer-term contracts (5 years +) in order to maximize profit. **Barriers to Entry** Convergys doesn't believe there is a place for it in the federal market because it specializes in mission-critical applications. Its customers prefer its solutions because they are field-tested. Respondent doesn't believe that the kind of work that the company does has a wide application in the federal market, except perhaps at the IRS. In his view, "the federal market is a world unto itself." He believes that sales staffs need to be different (it is more difficult to send federal salesmen into the commercial market). All parts of the organization, including technical, sales and office staffs need to adapt to the characteristics of each market—which differ significantly. **Process Used to Compute Costs** Company uses a standard price book that includes Total Cost of Ownership models (TCO). These will vary depending on the billing platform used. Convergys tries to create a strategic partnership with customer: "We try to help the customer understand his TCO—then we show how costs can be cut." **Model Used to Estimate Profitability** Beyond revenues from outsourcing, Convergys typically derives 20-30% of total revenues from provision of Professional Services in the IMG division. This is usually for some kind of system integration work. Company is often hired to build this component into its original project management plans and contract provisions. This comment was made in the context of asking if the company had ever low-balled a contract proposal for little or no profit in order to get a foot in the customer's door. Respondent denied this (they all do), but admitted that, at times, it could shave the outsourcing contract profit margin if the SI professional services component were large enough. Convergys tries to extend contract durations well before their expiration in order to reinforce client relationships. **How Burdensome are Sales and Marketing Costs?** Respondent believes that company's sales costs are relatively low, at 5% of total contract value—or less. He believes that they could be even lower in the federal market. He commented that he thought there were higher contract capture costs in the federal market, along with a higher level of "hassles." He expects the company's sales and marketing costs to RISE, albeit not so high as the average for software vendors (10-15% of sales revenues). **Problematic Staff Transfers** This issue doesn't apply to Convergys to any significant extent. While the company can do "co-sourcing" whereby it takes over the customer's existing call center—and in those case could transfer customer staff to the vendor's payroll, this would be exceptional. Most company work is done remotely by its own full-time staff. However, Convergys has made about 20 successful acquisitions and its ability to absorb acquired staffs comprised an important element of its success in integrating acquired companies. **Relevance of Customer Revenue Size** Convergys doesn't categorize prospective customers according to revenue size. Rather it looks for "emerging" companies that appear poised for rapid growth—which would mean rapid expansion of its relationship with Convergys as well. The important issues are customer's financial viability, strategy and growth potential. At times, Convergys has elected on its own NOT to continue a client relationship because it had determined there was no real profit potential.
CSC (1) [#3]	Respondent has a high-level position in CSC's federal group, with responsibility for both

civilian and DoD business.

Background

Federal market work comprises about 25% of CSC's total revenues. This has declined at times to 23%, but the target remains 25%. Another 3-5% of total revenues derives from work in the state and local levels of the public sector. Fifteen years ago, federal business comprised 70% of CSC's total revenues, including outsourcing and facilities management. Overall, outsourcing comprises 38%.

Historically, CSC leveraged its work for General Dynamics to enter the federal market. The key to success in this market has been strong program management skills, good software development capability, and skill in dealing with complex systems and security environments. Another key to success: thorough knowledge of agencies and customer needs.

Transferable Skills

How many of these skills are transferable to the commercial market? Best transferable areas of expertise are:

Rigor in program management

Ability to deal with complex issues

Ability to apply the Carnegie Mellon model for performance achievement

Example: CSC's successes in the federal market were critical to DuPont's decision to award CSC a large outsourcing contract in the commercial market.

CSC's ability to penetrate the commercial market depended, in many cases, on similar situations where prospects were "seeded" with stories of what the company had achieved in the federal market. This proves as well the extent to which skills and processes are transferable between federal and commercial markets.

Most important of these is the rigor of project management in the federal market. The ability required there to deal with complex issues, regulatory environment, etc. fosters a process discipline that is very transferable to the commercial market.

Direction of Outsourcing Market

Clearly, customers want increasingly comprehensive outsourcing contracts (for example, the LOGMA army contract). The first federal outsourcing contracts involved the transfer of civil servants and covered rudimentary transaction processing tasks. These contracts were followed with more complex ones involving enterprise architectures and supply chain management.

Market Barriers

The most significant barrier to entering any new market is the lack of established trust between customers and vendors. Trust is very important. Even in the federal market, understanding the real mission of many agencies is not easy, yet in every case the vendor must demonstrate a deep understanding of the client's business in order to offer a better value proposition.

In particular, our mastery of Carnegie Mellon software development metrics puts us in a select category of vendors that are attractive to new customers based on objectively demonstrated expertise. This expertise has been used on numerous, demanding outsourcing contracts, such for Aegis, air traffic control and NASA.

Also worth noting, we have 47 years of experience in program management, including provision of on-going training. (We do training in-house even though we recruit externally.)

Availability of Capital

As a public company, CSC must provide its shareholders with a meaningful risk-weighted return. Therefore, it must balance business risks. Broad experience lets us gauge risk with accuracy. We have an in-house system model for program management that includes computation of costs and profits.

Changes in the Market

Overall, customers are driven by the value potential of IT outsourcing. Also, they are trying to cope with technological change. They don't know how to do it and they are admitting with increasing frequency that they need help in identifying the best solutions to their business problems.

The federal retirement situation is a "bombshell." We see federal employee unions as

	important allies (ex. IRS). Sole-sourcing? If you become a real "solutions provider," then you become a natural contender for sole-sourced contracts. Much work is done in the federal market under task orders, and these are not necessarily competitive (ex. the contract that USPS awarded recently to Federal Express on a sole-sourced basis). The new Republican administration may allocate higher budgets to the DoD, but eventually "reality will set in" and the government will be obligated to move increasingly toward privatization of functions that are currently performed by civil servants and/or military personnel. **Areas of Expertise** In the federal market, CSC considers application management an important strength. In the commercial market, application management is typically bundled with a variety of other services in the commercial market. During the last three years, CSC was well positioned to leverage commercially tested solutions to federal clients—as evidenced by wins at IRS and the Army logistics contracts. Also, experience with delivering on SLAs is critical: vendors in the federal market must be comfortable with performance-based contracting. This is also a great advantage in the commercial market. Beyond that, CSC has 20 years of experience and demonstrated success delivering on contracts for the operation of military bases—despite the political power of unions. **Sales & Marketing Costs** Many task orders include a host of smaller deals that can be bid at little cost. **Staff Transfers** CSC has never had difficulty in absorbing qualified staff acquired through outsourcing deals. In fact, it has had exceptional success in this area. For example, in the case of the Army Wholesale Logistics contract, 100% of target staff elected to transfer to CSC. Over the years, CSC has absorbed 30,000 people in this way, many of whom have advanced to high-level positions in the corporation. Protests—CSC has participated in very few federal contract protests. As a matter of policy, the company tries to avoid protests. As an exception, CSC did protest a Boeing award because management believed that the criteria for the award had been unclear. A legal decision was needed to clarify the issue.
CSC (2) [#5]	**Background** Respondent represents the "capture" side of CSC's commercial outsourcing business. The vendor has centralized all contract capture activities in one place—including some federal outsourcing. CSC tries to bring its vertical industry expertise to bear on the capture process, including in particular the federal, health care and financial services markets. **Best Outsourcing Opportunities** CSC sees the best opportunities for growth in its commercial IT outsourcing business in financial services (banking and insurance), manufacturing (esp. electrical) and other industries. Since mid-1998, the company has done relatively little work in accounting (other than Y2K-related). Overall, consolidation in the banking industry has been good for IT outsourcing, yet the end of Y2K spending depressed the volume of business. Now there is a powerful trend in play toward standardization, esp. in the areas of application management, or applications infrastructure. Customers want vendors to buy their data centers, run and operate them. In some cases, customer's want work done on their premises (whether they, or the vendor own the hardware); in other cases, customers either agree to having their work done remotely at the vendor's data center. Ultimately, customers become comfortable with the idea of vendors acquiring and running their hardware, located on the customer's premises, while the vendor does work for third parties. This kind of flexibility greatly enhances the cost-effectiveness of deals to customers and the profitability of them to vendors. While our financial service customers tend to be headquartered in the U.S., their operations

are global. So far, we do all work for them in the U.S., however, we are exploring the possibility of using offshore IT vendors as partners in countries such as India. No initiatives in this area have yet been implemented.

Market Trends

Customers want to grow their businesses, but they cannot do so with their existing IT infrastructure. They can't support their actual or expected growth with existing staff and facilities. CSC sees much opportunity around the globe, especially for work with U.S. companies that are expanding abroad. Typically, CSC begins a relationship by doing work for the U.S. units, and then expands the relationship by doing client work for units located outside of the U.S. The average size of outsourcing contracts is increasing, at least for CSC even while the number of deals is shrinking somewhat.

CSC revenues are now about $5 billion, derived from work for Fortune 500 companies. CSC targets "mid-tier" customers, which it describes as having revenues or $1-5 billion. Top-tier companies typically have revenues above $5 billion. As an example, J. Crew awarded a contract based on an IT budget of $2-30 million annually. Companies in this mid-tier segment can't field sufficient IT resources and they outsource out of necessity.

Types of Outsourcing Done

CSC does a wide range of types of outsourcing, including Web-hosting, applications management (ex. health care and financial services) and is a leading provider for the insurance industry (ex. recent acquisition of Mynd, which only reinforced a prior position of strength). Last year, there was a noticeable trend toward "downmarket" outsourcing (transaction processing), but this was likely an anomaly.

Barriers to Entry

The greatest barrier to entering a new market is typically lack of name recognition. Even so, all of the potential barriers noted are important (financial, technical, marketing, organization, staffing, management).

Historically, CSC has spent little on promotion to achieve better name recognition. It should probably have spent more. In the past, CSC business has spread by word of mouth between satisfied customers. Now, the company targets the "thought leadership" of various industries as a strategy to get a foot in the door for the CSC brand. (Clearly, the situation is totally different in the federal market where CSC has a much better established position.)

Capital Availability

Difficulties in obtaining capital required for closing outsourcing deals has never been a problem for CSC. Yet, availability of capital has seldom been a clear-cut differentiator or predictor of market success.

For example, Lockheed Martin's commercial IT business unit can claim no barrier to funding from its deep-pocketed parent, nevertheless, its successes in the market remain modest. The same can be said for UNISYS (which is leaving the federal market). Companies such as CSC and ACS are at no disadvantage due to difficulties in accessing capital, but the situation depends greatly on the type of outsourcing business that a vendor does and its stage in the business lifecycle. For example, newly founded Exodus Communications had to use equity to fund its capital requirements.

Market Developments

Opportunities are now increasingly global rather than national and the most attractive segment has become the midmarket—which is also on the move globally.

Vendors expecting to make the transition from the federal to the commercial market need to build a base on their federal experience—following CSC's example. The company took its 10-15 years of experience in working for federal clients that made high demands for technical discipline and process management to the commercial market, albeit with adaptations. We discovered that we could be very successful with commercial clients by applying the same processes globally that we had used for federal customers.

At the same time, realize that partnerships take time-whether with customers or other vendors. You must work your way up to a position of trust. There is no shortcut to the position of "trusted advisor."

Insofar as possible, use industry analysts to spread the word about your capabilities cost-effectively.

	In the 1990s, customers were motivated to outsource primarily by a desire to achieve cost-savings. This motive was superseded by a realization that lack of internal resources made outsourcing an imperative beyond potential cost-savings. Eventually, cost-savings will move back into the top position as an action criterion, but at the moment customers are giving priority to the need to standardize their IT environments as a precondition for achieving cost-savings. CSC showcases its heritage of work experience in the area of security for classified federal customers. Worth noting, this experience proved decisive in winning the Nortel contract. Top management decided that CSC's skills in this area were eminently transferable—and desirable. **Costs** CSC does a comprehensive solution development/solution design estimate, including the cost of implementation before pricing a deal. Company uses a "cost build up" model (others use a cost-savings or percentage of promised savings method). In the case of most contracts, there is a base cost to the customer with adjustments according to business volumes. It is important to build variability of parameters into the contract from the start. As an example, due to a late acquisition, the Nortel contract required an adjustment of expected transaction volumes even before the contract was signed. **Marketing Costs** Business development costs are clearly higher on the commercial side—basically because there is more travel required. All federal clients are located conveniently in one central location. Nevertheless, federal proposal preparation costs are higher than the corresponding costs to prepare a commercial bid. CSC manages costs carefully; all expenses are evaluated with care so that they cannot become burdensome. Company uses a "pursuit model" scaling that computes (and sets a cap on) marketing costs as a percentage of total contract value. Commercial marketing challenge: each company has its own organizational hierarchy, yet vendors must learn how to streamline their sales approach and go directly to the top decision-makers. **Staff Transfers** Ability to absorb new staff resulting from an outsourcing deal has never been an issue for CSC, which has a very high rate of acceptance of employment offers. What is the secret to the company's success in this area? CSC has always made an effort to attract and retain good people and there has always been a flow of staff upward through the organization. New hires know in advance that they have excellent opportunities for advancement at CSC. **Unions** CSC has some experience with unions, especially in Europe and in the public sector. CSC tries to "manage" union relationships so that unionized employees remain with the customer.
EDS [#21]	**Background** Respondent was a senior VP of Sales with 24 years of experience at EDS. Previously, he was president of the banking and financial services division (eight years); he ran the transportation industry group and, for four years, was in charge of the GM relationship on location in Michigan. He has been heavily involved in sales and business development in both the governmental and commercial markets. He has both a CPA and MBA-Finance educational background. **Company Structure** Respondent explained that EDS has currently four operational divisions: • Information Solutions (which includes traditional outsourcing and comprises 80% of EDS' total revenues); • A.T. Kearney, high-end management consultants; • E-solutions, which does Web development and related Internet work; • Business Process Management, which includes a large health care, claims-processing operation along with other commodity date processing.

He confirmed that 14% of total EDS revenues derive from the U.S. federal market and 58% overall from the U.S. market. Of total global sales, 60% derives from IT outsourcing. An estimated 2% comes from the non-federal, U.S. state and local government market.

Growth Prospects

EDS sees the best prospects in the financial services, telecom, manufacturing, energy, and health care industries. In addition, the company finds the federal and state public sectors attractive along with transportation—especially the "emerging" transportation segments of air, car rental, and freight.

Direction of Market

EDS believes that the market is definitely moving toward more comprehensive outsourcing deals because company managements are looking for long-term, strategic business partners that are able to add value to their businesses. The vendor's role is clearly becoming more strategic than tactical—as it was in the past, i.e., a provider of short-term, clearly defined solutions.

Fewer customers are opting to select a team of various service vendors that they need to manage themselves. However, customers do often prefer to outsource while retaining certain specifically defined IT functions to do internally. Even EDS seldom wins ALL of a customer's IT budget.

Barriers to Entry

Respondent doesn't really believe that there are any (merely) "horizontal" applications. Even in the case of CRM, HR and accounting, he believes that customers have a strong preference for a vendor that is able to demonstrate in-depth understanding of their industry. Therefore, to be successful in entering new markets, vendors must be able to hire experts in the target industry that are able to demonstrate the benefit of their years of experience by solving customer problems creatively—even if nominally "horizontal" with cross-industry application.

Respondent also believes that there is something called "critical mass" at work. If gaining a foothold in a new industry is difficult, there is also a snowball effect whereby success breeds more success—once vendor has achieved a minimum critical mass of business.

How does an unknown vendor establish an identity in a new market?

He must acquire and demonstrate an understanding of the dynamics of that new market, the issues that concern its players, the structure of the market, its IT spending characteristics, its priorities, etc.

The next step (for EDS) would be to map the vendor's capabilities to this aggregate industry model.

Next, the vendor must develop a strategy for meeting the needs of customers in this new market.

In the case of making a transition from the federal to the commercial markets, respondent doesn't believe that customers will pay attention to the type of market so much as to the nature of the solution and the vendor's success in solving a business problem. Comment: "You're only as good as your last client."

(In this context, he described how EDS monitors customer satisfaction on a daily basis according to an on-going methodology. The goal is to solve problems ASAP that could impair the client relationship.)

At the same time, image and perception are important. In order to gain a toehold in a new market, smaller vendors should partner as subs with larger prime vendors on contracts. EDS does this often with other vendors. Alliances and partnerships are critically important.

EDS differed with other survey respondents by denying that the vendor had, or would enter a new market through an acquisition.

Importance of Capital

After admitting that he had no experience working for a small vendor, respondent said that availability of capital had never been a barrier to new business in his experience. Although he could recall no deal that had been turned down due to the unavailability of capital, he did admit that capital was an important factor in the competitive outsourcing market.

He said that EDS did not often resort to off-balance sheet solutions, such as leasing, because

	it believed that it could manage equipment assets better than any leaseholder. **Changes in the Market** Respondent cited a move toward strategic outsourcing and away from commodity outsourcing. Discussions between EDS and prospective customers usually center on the nature of the long-term, strategic contribution that the vendor can make to the customer's business model. **Risk-sharing?** Respondent commented that, while the customer wanted to consider the IT vendor a partner, there was no strong trend toward including vendors in risk-sharing and profit-sharing arrangements as part of an outsourcing contract. While customers may be intrigued initially by the idea as a way to provide incentives and punishments to the vendor, they usually conclude that there is no effective way to measure the vendor's contribution to revenues and profits separate from the rest of the customer's organization. Also, changes in business conditions are common and, when they occur, they usually disrupt whatever sharing arrangements had been in place previously.
Entex IT Services [#13]	**Background** Respondent is a SVP for strategy at Entex IT Services. He has responsibility for planning, marketing strategy and is directly involved with the development of outsourcing proposals. At Entex, federal and commercial businesses are treated as a single entity. Respondent came to work at Entex in the U.S. after the Siemens acquisition. He has substantial prior experience with Siemens in Europe. Currently, public sector comprises only 10% of Entex's total revenues, commercial work represents 90%. Of public sector work, only 10% derives from the federal government—the rest, from work for state and local government clients. The company's primary products are desktop services and network management. **Background of the Siemens Acquistion Last Year of Entex** At present, Entex is a wholly owned subsidiary of Siemens Business Services (SBS), based in Germany. Entex operations are integrated fully into Siemens on a global basis. SBS is divided into SBS consulting and IT Services. Entex is part of the IT Services group. **Marketing Strategy** How does Entex prioritize its prospects? According to (1) size of customer by revenues [Fortune 100-500 ranked]. Currently, Entex has 50 active customers from among the Fortune 100. In particular, Entex pays attention to the "IT intensity" of prospects, or the percentage of revenues allocated annually to the IT budget. By this ranking, manufacturing is lower than financial services because companies in the sector tend to have smaller IT budgets in proportion to revenues. The sweet spot: companies that spend $100-500 million annually besed on revenues of at least $1 billion. Entex works prospect lists with some attention to geography, even though outsourcing work can be done remotely. Salasmen usually focus on companies based on HQ and then follow them geographically. The approach of Entex is very different from the approach of Siemens in Europe. In Europe, there is more emphasis on geography, with steff allocated on a geographic basis at regional centers, with less on-site staff. In contrast, in the U.S. Entex mainteins large numbers of staff working at customer worksites. **Other differences between the U.S. and Europe** Because the mobile telecom environment is more standardized and more advanced in Europe, wireless LANs are more widespread in Europe. The U.S. market is 3-5 years behind in this respect. **Most Attractive Markets** Financial services (including insurance) and health care [a stronghold of Siemens] appear to have the most potential for Entex. Nevertheless, the company is active in almost all vertical industries. Sales and marketing are not organized by vertical industry. Entex believes that its primary offer, desktop services, is a horizontal product that can be sold in every industry to organizations above a certain size (3-5,000 seats). Overall, the IT outsourcing market is clearly moving "upmarket" toward more comprehensive contracts. Customers want relief from the burden basic IT operations and they want to

advance an agenda that includes a transition toward e-business—and lower headcount. Cost-savings are less important than streamlining management structure.

Barriers to Entry

There are fewer barriers of entry to vendors of horizontal products than to vendors whose products are specialized according to vertical industry. However, this approach does expose vendors to more intense competition and the threat of commoditization. The most important weapon in overcoming barriers to entering new markets is technical expertise, especially in the areas of application development and application management because they are higher value-added.

Customers of horizontal IT products are less concerned that vendors demonstrate expertise in their vertical industry than in their core technical competencies. In the federal market, vendors need to prove their understanding of the government market and its characteristics.

Without the benefit of the name recognition advantage of Siemens, Entex would (did) have difficulty in entering new markets. Lack of name recognition is definitely a problem.

Marketing

Does Entex use outsourcing consultants? Not much contact so far. Consultants are more active in Europe. The type of services offered by Entex take the company off of the radar screens of most outsourcing consultants.

Bid/Proposal Process

Generally, the average size of Entex's bids is small. Large bids require top management's approval. Entex doesn't go cold-calling. It will usually take a piece of a larger contract and try to expand the relationship.

The proposal costing model is based on clear definitions of the work to be performed. This is reviewed periodically and profitability is recalculated. Independent audits confirm these numbers. Entex does offer work priced on a volume basis. Key factor: build into SLAs from the outset a clearly defined pricing mechanism that adjusts for changes in the customer's business model. SLAs are more of a problem in Europe. Also, success in pricing requires excellent Project Management skills. Europe is more advanced in the training of project managers (esp. Siemens, which has a high reputation in this area).

Burdensome Sales & Marketing Expenses

Marketing costs for desktop management are less than those for "complete" or "extreme" outsourcing, i.e., total data center management. National government bids are more expensive (especially in Europe). However, this is a non-issue for Entex, whose business is U.S.-based.

Staff Transfers

This is not at all a problem for Entex. The company tries to redeploy, relocate staff at the end of a contract insofar as possible. Those that cannot be relocated, or used elsewhere, are let go. Overall, the firm's retention rate is very good.

Cost of Capital

Based on access to the financial resources of the Siemens global enterprise, Entex faces no capital constraints in pursuing new business.

Changes Underway in Outsourcing Market

Customers are looking for more complete outsourcing solutions. They want to work with fewer suppliers. They prefer the prime (general contractor) model whereby a lead vendor manages the relationships and monitors the work of subcontractors. Overall, they want to reduce headcount.

The transition to e-business is making competition between vendors more intense. Smaller vendors are being relegated to subcontract roles, where margins are lower.

Entex participates in the federal market in both prime and subcontractor roles.

Most Profitable Types of Business

Without a doubt, network management and consulting are much more profitable for Entex than "break/fix" desktop services.

Yet, Entex will not enter into a desktop services contract on a low or no-profit basis in the hope that future, lucrative additional business will materialize to make the overall relationship profitable. While it is true that having an incumbent contractor relationship almost always

	results in incremental business, to depend on that business from the outset is a recipe for disaster.
Fed Data [#17]	Respondent is a VP for IT management services with responsibility for Fed Data's work on ODIN and GSA seat management contracts. He worked on the original proposal development. Prior to that, he had IT managerial positions at the Kennedy Space Center and the Johnson Space Center. Overall, he has 20 years of experience in IT, virtually all in the federal market. At Fed Data, he has project management responsibility for the Peace Corps and Wright Patterson AFB outsourcing contracts. Overall, Fed Data is working with agencies that are playing "catch up" with the NMCI/EDS contract. They want to roll up smaller projects into a similar, large contract vehicle, but this will take some time. To date, Fed Data has won only smaller, discrete task orders. **Fed Data Background** Fed Data is now a part of Logicon, which is Northrop Grumman's IT services division. (When the Litton/PRC acquisition is completed, part of it will join Logicon, and part will go directly to Northrop Grumann. While Fed Data and Logicon have a few commercial clients, 90% of their work is for federal clients. Of that, only 10% comprises IT outsourcing. According to respondent, commercial IT work at Fed Data is done by completely separate work groups. There is virtually no synergy between the federal and commercial market teams. The company's commercial work was described as "oddball" projects that included help desk and network management work—but no data center outsourcing. Currently, Fed Data has a backlog of about $20 million in annual revenue from signed contracts. By comparison, Logicon had $400 million in 1998 and has grown to $2.1 billion today. On the top level, Northrop Grumann has annual revenues of $10 billion; Logicon represents $2.5 billion of this (including Fed Data). Litton/PRC has annual revenues of $5.5 billion. **Growth Potential** Respondent sees excellent long-term growth potential for increased desktop management business (task orders) from the DoD, Army and Air Force. These agencies are now trying to follow the example of the Navy's NMCI contract. While they don't anticipate any dramatic new budget allocations, the DoD appears increasingly willing to change existing budget allocations in order to roll up GSA task orders and other BPA contracts in to evermore comprehensive "bundled" large contracts for a wider range of work. In this context, respondent corroborated opinions expressed by other vendors to the effect that the federal government's entire IT infrastructure would be virtually obsolete in less than five years. This reality, along with the skills shortage, budget restrictions and pending retirements, would make IT outsourcing unavoidable. **Direction of Federal Market** Fed Data wants to pull out of the facilities management segment of IT outsourcing. Because the potential for increased business in the federal seat management market is excellent, Fed Data is not actively pursuing commercial clients. However, when pressed, he said that he thought the following mix of business would be ideal: • 50% federal • 25% state & local • 25% commercial The federal market is clearly moving "upmarket," albeit slowly. For example, the SSA wants to outsource only 2,000 seats as a test case because it is uncomfortable with giving a single contract to a single vendor for all 60,000 seats at the agency. Managers do not believe that any single vendor would be able to fulfill the work required by a single contract of that magnitude. **Barriers to Entry** While commercial company business is attractive for many reasons, respondent thought that the transition from commercial to federal would be more difficult than the reverse due to the long sales cycle in the federal market, the complexities of the procurement process and the importance of having personal relationships in place. A vendor wanting to move from the federal to the commercial market, in his view, must expect

to need to set up a virtual "mirror" organization to serve commercial clients. Salesmen, etc. would need to be recruited who had commercial experience. As an exception, the technical staff and project managers could probably be re-trained successfully for work in the commercial market.

Beyond that, such a transition would only work with the help of good partner relationships. (Even the commercial partnering model is very different from that used in the federal market.) Lack of commercial backlog and reference clients would definitely be a handicap. Respondent thought that commercial clients might be interested in a vendor's technical solutions for federal clients, but he was skeptical that this alone would win business, i.e, without being introduced by a commercial partner with excellent credentials.

Respondent noted the irony that federal clients are very anxious to benefit from vendor experience in solving problems for commercial clients, but commercial clients are not nearly so keen on letting federal vendors do work for them. In theory, this gives an advantage to primarily commercial vendors that want to enter the federal market, yet, they (for reasons outlined above) are often put off by the difficulties that they encounter.

(As an example, a spokesperson for Cap Gemini E&Y said emphatically that the vendor had decided NOT to pursue any work for federal clients because of the barriers and difficulty in doing business in that market made it categorically unattractive.)

Respondent commented that CSC had encountered "difficulty" in applying its commercial business model in the federal market.

Availability and Cost of Capital

Cost or lack of capital has never been an obstacle to new outsourcing contracts for Fed Data. As an example, respondent said that he had spent $50,000 to obtain a $5 million annual contract revenue stream, which he considered quite acceptable. Overall, he thought that federal outsourcing required little in the way of capital outlay. Whether for federal or commercial clients, he stressed that vendors need to use leasing companies for HW purchases. Even Fed Data, which has deep pockets, avoids outlays for capital equipment purchases as part of outsourcing deals. He gave the Peace Corps contract as another example; it required very little by way of upfront capital outlays.

In the context of leasing, respondent contradicted other survey respondents who claimed that leasing incurred tax liabilities. Fed Data respondent insisted that equipment located on federal facilities incurred no property tax burden.

Changes in Outsourcing Underway

Important changes in the federal market include:

- People are recognizing the need for change, both in terms of budgets and staffs.
- There is a genuine effort underway to understand how to make the transition from internal to outsourced IT functions.

The TCO concept is spreading in the government (even though it is seldom able to specify its costs accurately). Agencies are making progress in analyzing their "hard" costs for equipment, but having great difficulty in assessing their "soft" costs for people, HR, etc., which is necessary in order to compute accurate, projected cost savings.

Types of Outsourcing that Can Be Done Most Profitably

- Enterprise seat management, meaning bundled contracts for help desk, network management, LAN, break/fix work, HW/SW acquisition, some application management and development work
- Network/LAN administration
- Help desk (which has been mainly commoditized)
- Web hosting/Web site development Contracts here are small, but likely to grow in volume and importance for the government.

Logicon is doing some work on the state and local government level, including data center management. The potential for this is good, but contracts at present are small. E-gov is still in the future.

Expertise

Fed Data's primary expertise is in the seat management/enterprise management area, and

	secondarily in network management. **Cost Projections** Fed Data uses models for projecting cost and pricing models as part of the proposal/bid process. To be worthwhile, seat management contracts need to be sufficiently large to give vendor economies of scale. Cost projection models can be re-used—they are not developed de novo for each new bid. Fed Data uses a knowledge management system and believes that, in general, this approach could be used for bidding in the commercial market as well. **Sales and Marketing Costs** Overall, respondent believes that marketing costs at Fed Data run about 20% of the total cost of doing business, which includes administrative overhead, HR and related, direct costs. Yes, 20% is high now due to various unusual circumstances. He would expect a normal level for such costs to be 10-15% in the federal market and 6-9% in the commercial market. The primary reason why sales costs are lower in the commercial market is that the sales cycle is much shorter. **Staff Transfers** So far, Fed Data has had no problems in transferring civil servants to vendors' payroll. Such transferred staff usually needs training, particularly in company techniques and processes. **Control Issue** Federal agencies are very aware of the importance of secure data management, but seat management outsourcing tends to be accepted without provoking fears of loss of control. This is primarily a problem of perception (or misperception). For example, a remote networking management solution doesn't necessarily give the client less control—only differarant, i.e, not on site.
Getronics [#10]	**Background** The respondent worked previously for Wang. After Wang's acquisition by Getronics, he became head of outsourcing for the federal group. He has 16 years of experience in the federal market (mainly at PRC) and two years of experience in the commercial market. Significantly, he stressed that the federal and commercial market sales teams are in continual contact, at least weekly, even though they have separate missions. Specifically, respondent has hands-on experience with the ODIN seat management contract. Currently, he is head of that group's Center of Excellence in Seat Management, which has a staff of about ten technical specialists. Getronics has several such Centers of Excellence—including one for Network Security, and another for E-Commerce. For Getronics, "government" means federal. The commercial division handles the few state and local government contracts that have been booked. The Center of Excellence serves as a technical (Best Practices) as well as sales resource. Accordingly, respondent does get involved in the proposal preparation process and consults with business development staff on "alignment" of effort by agency. For Getronics, federal marketing consists primarily of determining which agencies offer the best prospects for new seat management business. **Market Position** Getronics does $3-4 billion in annual revenues worldwide. Of this, the Government Solutions Group in the U.S. contributes about $400 million, or 10% of the total. The corporate target is to grow this business to $1 billion over the next 5-6 years through organic growth and acquisitions. Seat management comprises about 10-15% of the Government Solutions Group's revenues; the remaining 85-90% consists of a variety of professional services (non-outsourcing). According to the respondent, the term "seat management" is essentially a federal-market-specific term. In the commercial market, "desktop services"—the nearest equivalent—usually includes network services, call center and other kinds of work. For some federal customers, seat management contracts are used as a back door vehicle to buy hardware when they can't access a capital expenditure budget. HW purchases are built into the seat management contract under the guise of periodic equipment "refresh" and using existing GSA schedules. Federal budget politics often requires agencies to spend money on a time & materials basis even when this is contrary to the best interest of both the government and the taxpayer. Partly for the reasons noted above, the government's concept of seat management is evolving and becoming increasingly comprehensive. Eventually, it will become something like BPO in

the commercial market. This process will take 4-5 years. At present, they are putting out to bid increasingly extensive pieces of work.

Capital Availability

Should the vendor supply HW on a lease rather than purchase basis? Often the decision hinges on taxes. If the vendor owns equipment assets, it pays an 8% property tax in the District of Columbia and 4.5% in Virginia. In many cases, direct vendor ownership of HW results in a 15-20% cost markup. If the government owns the HW itself, it pays nothing (but then, after a few years, faces the threet of obsolescence along with the burden of disposal).

Direction of the Market

Federal outsourcing business is moving in the same direction as the commercial market—"upwards" toward increasingly comprehensive, BPO-oriented contracts. If so, is seat management on the way out and, as a result, unattractive to vendors? Absolutely not: "Seat management is like getting the camel's nose under the tent." Typically, during the term of a seat management contract, 10-25% of incremental revenue materializes (based on total value of the seat management contract). This explains part of the advantage of being an incumbent; agencies are unlikely to go elsewhere to have work done that can be given conveniently and simply to the vendor that is already on the premises and performing satisfactorily.

Does this mean that vendors either can, or should bid for new seat management contracts on a no-profit basis in the hope that these incremental revenues will ultimately make the total customer relationship profitable. Respondent believes that this is a high-risk way to do business because an unprofitable vendor is unlikely to be either able, or motivated, to do the highest quality work on the initial contract. If work on the basic contract is lackluster or deficient, then the expected, incremental revenue will not materialize.

Barriers to Entry

Lack of dependable partner relationships.

Respondent used the example of seat management, but the point is applicable in general. He pointed out the danger of undue reliance on a partner to provide a critical element of a comprehensive seat management solution. Vendors must have in-house core competencies required to bid for target business. Also, remember that managing partner relationships is to manage a "moving target." For example, expect that a "Statement of Work" will be obsolete almost as soon as it is formulated.

Remember: "learning is incremental," meaning that there is no short cut to developing the technical and business knowledge required for success.

How important are partner relationships? Prime contractors are vulnerable. On the commercial IT outsourcing side, three out of four primes have had major problems with their subcontractors. These problems reflect, in part, bad management. In addition, they reflect fundamental incompatibilities, inequitable cost-sharing arrangements, conflicting processes and tools, as well as people who can't cooperata.

Commercial versus Federal Market

The commercial market offers tremendous potential for growth of IT outsourcing. Vendors wanting to move from the federal to the commercial market must take in to account the significant differences between the government's procurement policies and standard sales practices in the commercial market.

Ultimataly, there is a great deal of similarity between the business processes of government agencies and commercial businesses. Yet, vendors can trip on unforeseen differences in approach. For example, Getronics prepared TCO studies for its seat management solution (a common practice on the commercial side) only to be told that they violated FAR 9.5, which prohibits vendor conflicts of interest. (Solution: these need to be prepared by a third-party, not the vendor directly—especially if based on privileged information that is available only to qualified federal contractors).

Remember, "IT can be a competitive weapon for customers, which depends on quality IT vendors and their core competencies.

Process

Getronics has no "black box" that it uses to computa contract profitability: "We just tinker and adapt." To respondent's knowledge, there is no good contract cost/profit model. In reality, "outsourcing contracts are like DNA, each one is different. Pricing is an art.." because there

	are no precise data. Expect that the costs, terms and SLAs of an outsourcing contract will be subject to continual change. It is common for vendors to "take hits" in the form of unexpected costs. In the federal market, there is always a security dimension to the work (with associated costs). When agency needs change, and their budgets do not, we are often in the position of negotiating adjustments in SLAs, faster or slower refresh rates, return to service guarantees, etc., in order to keep contract costs within budget AND meet the agency's current requirements. The trick is always to figure out how to do this, make a profit, and NOT change the customer's cost. **Sales Costs** Respondent did not believe that there was much difference, ultimately, in the level of sales and marketing cost levels in the federal and commercial markets. But there is a big difference in the cost of marketing a seat management contract and prospecting for new business on a labor/materials basis. In that case, vendors participate, in essence, in a beauty contest with each other. The process for awarding GSA seat management contracts has been streamlined considerably. They can now be completed in less than six months, while other types of contracts take 6-9 months—and incur higher sales costs. Getronics spends an average of $200,000 in sales costs for each seat management contract that it wins. Decisions may come more quickly in the commercial market, but contract implementation can be slower. Obviously, it is easy to identify federal agency sales targets. This is a more difficult and costly process in the commercial market. On the commercial side, it is usually cost-effective to use consultants. Importance of inside contacts? "We had NO presence at all at Treasury, but we succeeded in winning new business in open competition, without pre-existing relationships." Respondent believes that this is exactly the experience that GSA is promoting. **Cost of Capital** Because recourse to leasing agencies (for equipment acquisition) is always an available alternative, vendor availability of capital is not a barrier to closing outsourcing deals. Yet, vendors should expect (and be able) to invest in the software tools that will be required to fulfill contracts. Because agencies are often in transition between technologies, vendors may spend $250,000-$1 million upfront to develop the tools required to standardize, streamline and fulfill contracts. **Important Changes** In the near future, the federal workforce will experience a massive wave of retirements, and there are no young replacements for them on the horizon. Young recruits want better hardware and working environments. During the next two years, the government will continue to play catch up; after that, expect large new outsourcing contracts because there will be no viable alternative. Union-inspired anti-outsourcing efforts (TRAC) will continue, but reality can't be changed. **Profit/Growth Potential** Getronics sees excellent potential in seat management in the federal market. Getronics has experience in dealing with unions in non-seat management contracts. Confrontation is unnecessary. However, vendors must recognize that unions have an inherent, vested interest in increasing headcount, not reducing it, which creates fundamental conflicts of interest between unions and outsourcers. Vendors need to face the truth: "You can't be everything to everyone." Respondent believes strongly that you need to be able to use the same software tool set for a significant period of time (in order to amortize your costs). Yet, this did not mean that Getronics was inclined to acquire the software companies that are its current partners and on which it depends for elements of its, in effect, proprietary seat management solution. Reason: "We don't want to be in the software business." Getronics does, however, build/assemble a basic tool that it uses repeatedly. It does NOT by off-the-shelf solutions from Tuvalu or Computer Associates.
Independent Consultant	**Background** Respondent worked for 20 years at Digital Equipment Corporation in application development

before joining CSC initially as a director IT for a business unit and working later as an account executive. In that role, she gained experience in the federal market by working closely with a major CSC client that was a major federal contractor. She has experience with "full-service" IT outsourcing as well as application development. This exposure to federal business provided experience with large, comprehensive IT outsourcing programs (albeit without any classified software development). Subsequently, she joined ACS where she had responsibility for application management outsourcing for new clients as well as the installed base.

Market Potential

Respondent believes that ASPs have good growth potential. Top-tier, experienced IT vendors can thrive in all verticals because many facets of the services requirements are really generic. As a result, vendors can leverage experience in one vertical to another. Although clients do expect vendors to offer reference clients in their own industry, this need not be a barrier.

Truth be told, customers ALWAYS believe that their needs are unique (and you don't dare contradict them). This customer misperception is based on a lack of technical background. From a technology point of view, there is little significant difference between verticals. Having said that, ASPs are most attractive when they specialize on offering very well chosen selection of applications that are industry-specific.

Market Direction: Upmarket, Downmarket?

Both trends are underway simultaneously (the outsourcing pie is expanding). In either case, vendors need to work on their fundamentals, i.e., understanding better where they can add value. There is a tendency to win deals and then worry later how to deliver results. Partly for this reasons, outsourcing consultants today ALWAYS insist on building "prenuptial agreements" into contracts that spell out the terms and circumstances that will govern the transition from the incumbent to a new vendor at contract expiration.

Barriers to Entry

Regarding the transition from federal to commercial markets, the truth is that commercial customers are seldom impressed to learn what vendors did in the federal market even if the opposite is true (federal agency customers are usually very interested to learn what vendors did/are doing for commercial customers). Federal customers want, in particular, to hear how the private sector is standardizing, adopting to industry-standard solutions, etc.

The key to success in the fed-to-commercial transition is to stress the nature of technical solutions independent of the customer's identity. In short, talk up your achievements themselves. The same sales staff with federal experience MAY be able to function in the commercial market, but it must be able to show strong understanding of technology, to show HOW business problems were solved, in order to undercut customer tendency to undervalue federal sector IT work.

Also, vendors should take pains to prevent salesmen from closing deals on which they can't deliver, or at least not cost effectively. Salesmen must understand what the vendor can really deliver, and usually this involves an appreciation of specialized solutions. In terms of strategy, while there is a great potential for new outsourcing business in general, vendors must avoid the temptation to "hybridize," i.e., offer themselves as experts in both infrastructure and business transaction processing. Pick one or the other and excel at it. If you decide to expand your expertise, then go out and build it, but don't expect to find a short cut to spending time and money on the effort.

Commercial vendors that want to move into the federal market are usually put off by the complexity of the federal contract proposal preparation and bidding process, including the protocols and security issues involved.

Cost and Availability of Capital

While not a problem for CSC, it has been a problem for ACS. At times, the company had to offer a qualified proposal due to the inability to deploy sufficient capital investment. In respondent's opinion the way to avoid this is to plan growth and, in any plan, capital is only one factor among many.

Changes in the Market

Clearly, the outsourcing market is moving toward BPO in the sense that customers are using vendors to take over ever more complex and comprehensive packages of business functions. At the same time, vendors should be aware that the opportunity is greater than the reality. Clients continue to be reluctant to hand over to vendors too much of what they perceive to be

	"control" over their core business processes, so fulfilling the market's potential remains a hard sell. Also, never forget that there is always internal resistance to BPO. Incumbent employees always fear that headcount reductions will inevitably follow any BPO contract, if not all outsourcing. **The SLA Game** Clients look to SLAs as a justification for their decision to give up diract control; SLAs are wielded as indirect control. Yet, in most cases, customers demand very exacting SLAs without realizing or admitting that, in fact, the high levels demanded by the SLA may never have been achieved by the organization, may not be possible, or—if possible—may be neither necessary, nor cost-effective. Smart vendors can expect to find excellent opportunities for growth in the ASP field (fixed servicas delivered for fixed prices on a monthly pay-by-the-drink basis). The danger is excessively fast growth and letting costs get out of control. Remember: ultimately, when all is said and done, ALL outsourcing deals are motivated by a customer desire to save money, however expressed. **Marketing Costs** On this point, burdensome Bid and Proposal costs (B&P) can contribute to undoing a vendor's success. This process is generally more complex in the federal market. It is easy to waste money in either the federal or the commercial market if you don't target your efforts carefully. You should always be asking the same question: where can I add value? Take care regarding your relations with outsourcing consultants. Some of them are NOT the vendors' friend. They are making it harder for vendors to close deals insofar as they run up costs. For example, a consultant may believe that it both enhances his client credibility (and fattens his fee) if he summons ten vendors instead of three to present bids. Yet, it is usually more realistic to ask only 2-3 to incur the expense of preparing and presenting bids and the others typically waste their time and money. Truth be told, there is a lot of self-deception at work on all sides of the equation, customer, consultant and vendor.
Keane [#15]	Respondent is a VP with responsibility for external communications, including industry analysts, investor relations and other. **Background on Keane** As a percentage of total company revenue, Keane's public sector business represents about 15%. Overall, about 60% of the company's turnover derives from IT outsourcing of various kinds. • Keane has four main business divisions: • Application development and management (9% is outsourcing) • E-solutions projects (9-10% is outsourcing) • Business innovation and consulting (1% is outsourcing) • Managed IT Keane earns about 38% of its revenues from "e-solutions projects." According to respondent, Keane has never lost an outsourcing customer based on poor performanca: "[Outsourcing] is not a market for people who can't perform." Of Keane's total revenue, 60-70% derives from multiyear outsourcing contracts. **Market Trends** In his opinion, the ASP model has failed—at least insofar as having an appeal for Keane's target market of Global 2000 organizations. They require significant amounts of customization, cannot use "plain Vanilla" applications. Therefore, ASPs cannot server their needs cost-effectively. **Changes in the Outsourcing Market** Customer interest in IT outsourcing is rising, especially for application management and development. Now, customers outsource these functions as part of a competitive strategy. They want to streamline their operations, offload nonstrategic IT functions so that internal staff can be used for higher value-added, core, proprietary IT development projects.

	The role of the CIO is changing. He/she is no longer an all-around guru or "builder." Today, the CIO functions more as a general contractor (supervisor) of IT outsourcing vendor relationships. Customers are moving toward one-stop shopping for outsourcing, but they also want best-of-breed solutions. Therefore, larger companies are less interested in "extreme" outsourcing wheraby they hand over to an outsourcing vendor complete responsibility for their entire IT infrastructure. Large companies want to select the best solutions available, even if procured from a variety of vendors. In contrast, smaller companies may still find "total" or "extreme" outsourcing appealing whereby they, in effect, depend entirely on outsourcers for their back office and IT infrastructure. Also, large organizations are increasingly skeptical that any IT vendor can "do it all," including IBM. Customers are maturing and moving up a learning curve. When data center management is outsourced today, applications are usually kept in-house, or given to a different vendor. Contract consultants are being used with increasing frequency. They are advising customers to avoid long contracts, aim at 3-5 year durations, insist on best-of-breed solutions and a favorable value metric. **Federal vs Commercial Market** From Keane's point of view, the federal market is less attractive than the commercial market. In contrast, Keane sees better potential at the state & local levels of the public sector. For example, outsourcing initiatives underway in Maine and North Carolina in the area of e-government are more advanced than those of the federal government. The federal customer is behind the state & local government customer. Rates and profits are lower in the federal market, but size of contracts can be quite large and the long-term nature of the business is attractive. In short, respondent believes that, for many vendors, doing business in the federal market is like holding bonds in place of stocks. Importantly, federal customers are increasingly interested in learning what vendors are doing/have done in the commercial market (while the reverse is much less common). Keane often takes commercially tested practices and applies them to work in the federal government.
Keane [#6]	Respondent has 20 years of experience in the IT industry, including consulting. His background includes work at Wang where he managed outsourcing projects prior to coming to Keane. At Keane, he works for both internal and external clients. His outsourcing responsibilities include sales and delivery. **Background** Outsourcing comprises about 50% of Keane's total revenues. Of that, work for commercial clients represents about 80% of outsourcing revenues; work in the federal market represents about 20% of total outsourcing revenues. Management believes that this is an optimal diversification for the company. Overall, the federal unit represents about 10-15% of total company revenues. **Growth Prospects** Keane sees excellent potential for growth of its public sector business, federal as well as state and local government. Beyond that, it sees good opportunity in financial services, insurance, manufacturing and utilities—which is currently experiencing unfavorable market conditions. Telco is another market for good growth. Keane does a lot of what it calls "backfilling" gaps in customer resources by deploying contract staff either on site, or at a remote location. (Sometimes "remote" is only a few blocks away from the customer's premises.) In addition, Keane sends customer work to its own "remote" data center in Halifax, Nova Scotia. Keane has done some deals to provide HR solutions and is strong in system integration. These markets remain attractive. **Market Trends** Customers are developing a much higher comfort level than ever before with the outsourcing of more comprehensive departmental functions. They like the idea of IT-oriented facilities management with us as a partner. Some consultants are now charging a "success fee" for introducing vendors to prospective customers. Example: Everest, which has a vendor/client exchange service. Clients are

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typically aware of consultant fees, but consider them part of the total cost of a deal. While consultants never take responsibility for a client's decision, it is clear that there are times when they are able to dictate to the customer which vendor to select.
However, the use of consultants doesn't eliminate the need for a good sales and marketing effort. Consultants can be a positive element of the total sales process, particularly if they have strong personal relationships and reputations.
Important outsourcing consultants include, in addition to Everest, Gartner, Technology Business International (TBI), Technology Partners International (TPI) and Transition Partners, along with The Outsourcing Institute.
Vendors entering the market need to convince these consultants of their value proposition.
Barriers to Entry
The greatest barrier to entry in new markets is lack of name recognition. Even with a $100 million federal unit, Keane must partner with other vendors as a key element of its application management market strategy.
Success in a new market depends largely on developing differentiators, i.e, ways to seperate you from the crowd of other vendors whose nemes are already known. While partnering is usually necessary, some vendors partner reluctantly and only at customer insistence.
There is an advantage to being in both the federal and commercial markets. While the federal customer wants to "commercialize" IT solutions, commercial customers tend not to be impressed (at least initially) with work dona in the federal market. Eventually, however, commercial customers come to appreciate the quality, methodology and process of work done for federal customers.
Availability of Capital
There isn't a great need for large amounts of capital for upfront investments in connection with most outsourcing deals. Most costs result from acquiring customer staff. Even so, these costs are built into the financial structure of the entire deal. While the data center/ infrastructure outsourcing business may be an exception, this is not the most attractive segment of the commercial outsourcing market for other reasons. It has been commoditized and reduced to single-digit profit margins.
Market Trends
Customers are getting into more sophisticated types of contracting and they are using outside consultants. There is increasing pressure to improve SLA promises. The challenge is to deliver business value based on demonstrable metrics and performance measurements. Historically, the federal market has been more demanding in this regard than the commercial market, but that is changing rapidly. There is much business available for maintanance of legacy IT systems, but this work is being rapidly commoditized and is no longer considered attractive by vendors.
If you look at the IT outsourcing market from the top down from the vendor's point of view, the most profitable types of business are:

A combination of new application development and maintenance of existing applications
Consulting-oriented work to plan, build and strategize new IT structures
Least profitable is data center management and transaction processing.

Also attractive, application managament contracts that include e-solution development work.
Keane's formula is:

Plan – consulting, strategy
Build – e-solutions, Web-enablement
Manage – full application management outsourcing and/or development, data center management (or federal seat management)

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<tr><td>Litton/PRC [#1]</td><td>
This respondent has a high level position in the company's outsourcing organization. Project managers report to him. He has overall responsibility for contract "capture" and management.
Background
Depending on one's definition of outsourcing, Litton/PRC does about $175 million annually in outsourcing, representing about 95% in the federal sector and the remaining 5% in the non-
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federal public sector. On a dollar basis, outsourcing accounts for about 25-30% of total revenues.

Parent Litton Industries does commercial outsourcing, but those activities are totally separate from the Litton/PRC unit.

[A contract at Federal Data/Logicon speculated that—after the Northrop Grumman acquisition of Litton Industries, Litton/PRC would be folded into the Fed Data/Logicon unit. However, this respondent believed that the it would likely be joined directly to Northop. The matter is as yet unresolved.]

Markets

Litton/PRC has been active in the staff augmentation and [physical] asset management. Currently, the company is most active in the following outsourcing markets:

- Seat management
- Network management
- Help desk
- Application management
- Storage on demand (SAN - storage area networks) where Litton/PRC owns and operates the storage servers for clients

The company is attempting to diversify away from federal market seat management and into the sate and local government markets, especially for data storage, which is experiencing huge growth. In the area of asset "takeover" or management, company has only one contract for $15 million (a GSA seat management contract). The storage-on-demand business is still small, but Litton/PRC expects "tremendous" growth in this market.

Why diversify by moving into the commercial market?

Management wants to promote value of "dual use" technology.

We have found that our federal market skill sets apply well to the needs of commercial market clients.

Ultimately, we see better growth potential in the commercial market than in the federal market.

Our success in the commercial storage network business has encouraged us to continue in this direction.

How is this migration from federal to commercial market being managed?

We began the process 7-8 years ago. We now have a different Web site for commercial business (www.outsourceprc.com). Here, we make a point of NOT promoting our federal market experience because we have no name recognition in the commercial market.

Our strategy is to pursue OEM partnerships in both the federal and commercial markets as a way to advance the promotion of our capabilities with commercial customers. We make a point of avoiding direct competition with the top-tier vendors such as IBM Global, CSC and EDS.

Barriers to entry to the commercial market?

Lack of name recognition or brand franchise among commercial customers. Trust is the critical elemant of the vendor/client relationship and it isn't easy to create it in the short term.

We depend—to tell the truth—on the value of the "Litton" name, which has cachet, even though it hasn't been used on consumer products for many years.

On the other hand, had we been "blessed" with a name such as "Fed Data," we wouldn't have had a prayer of success in this migration to the commercial market.

Commercial business operates along totally different lines than federal business, i.e., fixed-price contracts. Federal contracts are usually more flexible.

Upmarket, or Downmarket Trend?

Regarding an "upmarket," or "downmarket" strategy, Litton/PRC sees low-margin seat management as a way to get the foot in the door for more profitable business, such as network storage. Regarding profit margins, we believe thet—in general—the more remote work that can be done on a remotely managed basis and the less labor-intensive, the more profitable.

Capital Investments for Outsourcing

On the issue of capital investments, we don't find capital availability a constraint because there

	are numerous sources of financing, such as GM Capital, when needed. Capital commitments do raise the risk level, but the risk is seldom with the hardware. Deals fall apart based on service shortfalls. As a result, if we need to dispose of contracted equipment whose purchase was financed, customers almost never ask us to pick it up. They usually buy us out at the end of a contract agreement. We see outsourcing project risk in two levels: 1-staffing; 2-assets. **Types of Outsourcing Done Most Profitably** For us, the most profitable type of outsourcing business is network services and remote storage. Desktop services trails. In our experience, commercial contracts are usually at least twice as profitable as federal ones, i.e., with 20% margins rather than 10%. We would enter a market with low profit margins (5-6%) only if we thought there was good potential to move the business up quickly to the 10-12% level. This group accounts for 20% of total revenues. There are no staff training problems that are critical to our group. **Barriers to Entry** Greatest problems related to transition from federal to commercial outsourcing: The commercial world is vast, it is difficult to pitch to prospective customers in vertical industries without demonstrated expertise in that vertical. Transition requires an entirely different sales staff that is commercial oriented. Also, the competitive bidding process in these markets differs markedly. Overall, costs in the commercial market run higher. SLAs differ as well. Note: SLA expectations in the federal sector are rising (they had been significantly lower than in the commercial sector). Our **areas of outsourcing expertise** include: Help desk Storage on demand (for customers that don't want to buy new storage capacity directly, but prefer that the vendor put his own equipment on the customer's site and operate it). The key to success, for us, in the data storage market is to be able to set up hardware at the customer's facility. It can also be done remotely at our facility, but there is more competition in that approach. We like going to the customer's site because it (literally) gives us a foot in the door with potential for increased account penetration. **Greatest Potential New Market** We see the best potential for commercial outsourcing business in the financial vertical (banking and insurance), utilities (esp. natural gas companies), health care, entertainment. Most important, in the commercial market the customer must have confidence in the vendor as a partner. At the same time, the customer expects the vendor to be profitable. Therefore, as changes are made to the original contract agreement, customers understand that costs can rise and they are willing to pay. All of this is much more difficult in the federal market. Often, FAR is used as an excuse to deny changes in the contract, or to pay additional costs. In the end, it is more difficult to make money in the federal market. **Computer Modeling** We have no master computer model for computing the profitability of a contract. **Sales & Marketing** The commercial market has higher sales and marketing costs. As noted earlier, it will cost substantial amounts of money to achieve name recognition initially in the commercial market. Note that many sales and marketing practices that are standard in the commercial market are prohibited in the federal market.
Lockheed Martin [#4]	**Background** Respondent has responsibility for IT outsourcing strategy and business development in the commercial Integrated Business Solutions (IBS) division. He also manages alliances and partnering relationships. He began his career at PMS in the insurance industry. All of this division comprises commercial client work. It does no federal business. Federal outsourcing is done through the Information Support Systems division, which provides technical services to government agencies.

Best Market Potential

Respondent sees the best potential for new IT outsourcing business in the financial services and utilities industries. Utilities are particularly attractive due to deregulation and the turmoil surrounding changing market relationships.

Of Lockheed Martin's total revenues, IT outsourcing plays a small role, comprising less than $1 billion annually. This is split about half federal, half commercial. The division does NO transaction processing. The company also does some business in the state and local government market segment, which amounts to about $400 million annually.

Market Outlook

In terms of types of outsourcing, respondent sees the best growth potential in BPO work. Nevertheless, he believes that the IT outsourcing market is moving in two directions simultaneously, toward increasingly comprehensive as well as toward "low-end," specific-application services and transaction processing.

The answer depends on who is making business decisions. CEOs think in terms of BPO ("big picture") or ASP ("BP0 by the drink").

The IBS division has chosen NOT to organize around vertical industries. Instead, it targets large multinational customers that want to buy services only. IBS has no interest in acquiring customer assets or managing facilities.

IBS can build e-business centers, but would prefer to do remote application management for clients who don't want to own their own data centers. Also, IBS would like to sell spacial solutions such as supply chain management.

IBS does not believe in "building ahead of the curve," i.e., running the risk of excess capacity in either equipment or staff. It strives to stay just slightly ahead of demand. In this, and other ways, IBS benefits from its experience in both the U.S. and South America.

Barriers to Entry

The most important barriers to entering a new market are mainly organizational, and secondarily financial. A vendor needs ample funds to be taken seriously in the market. Vendors with limited financial resources should confine their offer to remote application management as a solution to customers' constraints due to the skills shortage.

IBS' policy is to avoid capital risk. Contract cycles are shorter in the commercial sector, typically 3-5 years rather eight, as is common in the federal sector. A typicel IBS deal, such as Gateway computer, can be implemented in 120 days.

In respondent's opinion, the government is a better buyer than commercial market buyers of IT outsourcing services. Reason: the government knows how to deal with outsourcing services and has senior executive IT managers. In the commercial market, outsourcing project liaison is often handed over to junior IT staff.

IBS rejects deals if a customer is deemed "unsuitable," for example, if the company has never done outsourcing, and doesn't use a consultant or lawyer. In such ceses, the likelihood of loss or litigation is higher and the quality of the RFP is lower.

One red flag: when outsourcing is called in as a solution to a troubled M&A relationship.

Changes in the Market

The most important change over recent years has been the government's decision (mainly DoD) to give up insisting on "bespoke," or customized IT solutions, either equipment or software. Now, the government prefers to by commonly available solutions off the shelf. This represents a big change.

Another important change has been the increasing use of outsourcing consultants by customers. Today it is common to spend 5% of the total contract value on paying consultants—and they work for both customers and vendors.

Preferences

IBS would prefer to do high-end, high value-added e-business projects, but to date the company has done somewhat small deals, which are typically broken in to pieces and awarded to multiple vendors.

IT infrastructure management is still profitable, but it is very difficult to differentiate yourself in this segment from your competitors. The skills have been commoditized. Also, these projects are complex and require highly developed project management skills on the part of the vendor.

This is a perennial challenge: how to differentiate your company and your offer from competitors. IBS doesn't play in the same league as IBM, EDS and CSC. IT targets deals in the hundreds of millions of dollars, not billions.

Respondent describes IBS as "big enough to do the job, but small enough to give attention to customer needs. In contrast, for a company such as IBM, NO deal is big. IBM has a pipeline of $1 billion deals. For IBS, the "sweet spot" is a deal in the $100-500 range. There it can compete effectively. IBS bills itself as a "full-term participant" that is more accessible to client managements.

Barriers to Entry

Lack of name recognition in a market is certainly a major handicap. The solution is to deliver skills. Lockheed Martin provides an advantageous pool of resources. IBS can, when necessary, get hold of expert staff from anywhere in the Lockheed Martin universe. Intercompany transfers are used. Also, divisions can award intercompany subcontracts, or "hire" internally. And the company hires off the street.

LM has a strong Chief Technology Officer. In addition, "business acquisition skills" are transferable between federal and commercial markets. The principal barriers are the differing financial and accounting systems used in these two markets. Also, the nomenclature used is different.

At IBS, staff (technical and sales) working on commercial projects is generally kept separate from those working on federal projects. Yet, there have been transfers between the two groups (but not all are successful). A transfer from the commercial to the federal market is less likely to be successful.

Bid Process

IBS uses an in-house model to compute the cost (and profit) from contract bidding. Typically, outsourcing is a low-margin business in the early years. In the past, IBS tried to take the "business case" of the customer into account (stage in company life cycle). Now, IBS prefers multiyear deals whose revenues are booked on a parcentage completion basis. IBS prepares bids on a forecast of total contract costs.

Sales and Marketing Costs

Most outsourcing transactions make provision for imbedded sales and marketing costs along with technical costs. In respondent's opinion, marketing costs are lower with commercial outsourcing deals because the federal procurement process can be quite lengthy. For example, a $750 million federal market deal took three years to negotiate and cost LM millions in expense. In contrast, a commercial deal valued at $350 million required only 12 PowerPoint slides to close the sale.

<u>Key point: you must know who the decision-makers are.</u>

IBS wants to do deals that are big enough to eliminate smaller competitors. Above $1 billion, there are only a few players.

IBS doesn't make low-margin contract bids in the hope that we will be able to scrounge some profit out of the deal in future years. This is simply self-deceptive thinking.

Sales and Marketing

Vendors should establish good contacts with the principal outsourcing consultants, including Transaction Business International (TBI), Transaction Partners International (TPI), Transition Partners, KPMG, the Outsourcing Institute, and the Outsourcing Exchange. Also, vendors should participate in industry conferences and events.

Respondent doesn't believe that vendors in the commercial IT outsourcing market don't need hundreds of salesmen. They only need to establish contect with these few consultants mentioned above. Using them effectively can leverage a vendor's business from zero to $1 billion in 4-5 years.

Take Exult as an example. It went from zero to $3 billion in one year—with no sales force. The company focuses on large BPO, single contracts annually.

Any vendor can enter the commercial market quickly and make a big impact by using consultants. No need to establish a geographically-oriented sales force.

There is much pricing pressure and commoditization of services in the IT outsourcing market.

	As a result, it is very important to avoid excessive SG&A spending—especially because these costs don't rise in proportion to the size of the deal. They remain the same. Ergo, it is more cost-effective to target larger deals. **To what extent are customers price sensitive?** In the federal market, established procurement processes level our prices. In that market, if you exceed your competitor's bid by 5%, you are out of the game. Price is important and high-priced vendors are eliminated early. In contrast, while pricing is important in the commercial market, the environment is more elastic, assignments and processes more varied. **Changes in Customer Motivation** In the 1980s, customers used outsourcing mainly to achieve cost-savings. In the 1990s, customers are outsourcing because they lack the internal IT staff required to meet their needs. Also, they give much more priority to time-to-market issues. Timing is critical and outsourcing is seen as a shortcut to market. **Relevance of Customer Size by Revenue** Customer size by revenue is an important marketing criterion because it bears a direct relation to the size of the outsourcing deal that can be put together, i.e., customer spending is linked to revenue by a certain percentage. However, as indicated above, ALL of IBS' outsourcing deals were won through relationships with consultants (who are paid $2,000 daily). Nota in particular the success of The Outsourcing Institute (OSI) in bringing vendors new business. Also worth noting, consultants like OSI are attempting to set up a new electronic marketplace that will match outsourcing customers and vendors. **Union Policy** IBS does have some experience with unions, but mainly on the federal side.
Perot Systems [#22]	**Background** Personally, the respondent manages client relationships. As a company, Perot assists customers with aligning, managing and applying technology toward client business objectives. Respondent has been in the IT outsourcing field for five years. He began his career at EDS where he achieved Inner Circle Status as one of the top sales people globally. He now represents Perot System's Integrated Solutions Group and is one of the top sales people representing this group. **Market Position** Perot Systems does no business at all in the U.S. federal market. **In which vertical industries do you see the best growth potential for IT outsourcing?** Financial Services, Manufacturing and Healthcare **Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?** Perot Systems is focused on the "upmarket". **How would you categorize the most important barrier to entering a new market, Financial? Technical? Marketing? Organization? Staffing? Management? Other?** Respondent believes that financial and organizational are equally difficult barriers. Successful existing business units are competing for the same capital resources and have a proven track record and history. One of the key areas affecting your ability to obtain capital is the proposed organizational structure. Financial and organizational alignment should be considered part of your strategy while marketing, technical, and staffing is more tactical in nature and is something you can leverage from existing business units. **To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?** As we all know pursuit cost can be very expensive. With that being said, capital to pursue an opportunity that we believe has a high probability of Perot Systems being successful is not a factor in our opportunity pursuits. Capital allocation requests for pursuits are denied only when we perceive there is a less than average chance of being successful. **What important changes do you see at work in the outsourcing market today?** The ability to do something better, faster and cheaper is the price of entry today. Clients today

	are looking for strategic partners that offer breadth and depth. Clients are seeking ways that they can drive business to fewer partners and hold them accountable for the results. Basically treating their service providers as an extension of their IT department and business units. One other area that we, the incumbents, seem to be ignoring is the possibility of new competitors in our space. We have done a very good job of warning our clients that in the new economy paradigm competitors are in every vertical. We point to Enron and others as examples. The creation of shared services groups that are independent of their parents possess industry knowledge, relationships, and an understanding of industry applications and technologies that can be tapped as solutions. They have been authorized to capture revenue from other firms but because of their organizational structure have not been successful. I see these as potential back office competitors. One the front end what if Amazon, Yahoo or Ebay decided to get into the CRM space? The virtual companies we are building today possess the skillsets and knowledge to be our potential competitors tomorrow. **Top down, which types of outsourcing can you do most profitably? (Reasons?)** <u>Business Process Outsourcing</u>: Most organizations today view the automation of a business process as a major milestone, and in many cases it is. However, the true value is to determine if the process is worth automating to begin with. Business Process Automation provides the initial quick hit to secure funding from CapX. The real value though is how a particular process, or subprocess, can be redesigned and measured to become better aligned to the corporate vision and strategy. The inefficiencies once identified and resolved deliver significant operational and cost improvement and in some situations positively affect top line growth. <u>Application Outsourcing</u>: We have the ability to transfer this work to a JV in India, HPS, that is a Managed Level 5 of the Capability Maturity Model for the Software Engineering Institute. This disciplined process approach provides us with efficiencies that reduce the time and risk in making enhancements and performing maintenance of the chosen application. Additionally the Indian labor rates are significantly lower than U.S. based rates allowing us to perform this service better, faster and cheaper than our clients. <u>Web Management Services</u>: The ability to combine our infrastructure competency with HPS enables Perot Systems to compete very effectively in this space, especially when the requirement is high availability supporting a mission critical application. <u>Program Management</u>: Perot Systems will outsource the management of a single or multiple projects and leverage ours, or the clients, project management methodology. These engagements typically involved some type of risk/reward component which significantly increases the operational margins for Perot. **In which type of outsourcing do you have the most expertise and success? (Future?)** Enterprise outsourcing today. BPO in the future. **What process do you use for computing the cost of contract bidding?** Each opportunity is assigned a cost center where all expenses for people and material are assigned. **Do you have a dynamic model for estimating total contract profitability as changes are made over time?** All opportunities are modeled with assumptions of the desired target level that we believe we can achieve and are reviewed periodically. **How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)** Currently, Perot Systems does not compete for Federal contracts. This should provide the strongest answer of the burden in pursuing that business. As for commercial, we are selective on what we pursue so the overall cost, while expensive, is not over burdensome. **Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)** NO **What is your policy toward dealing with unions? (How important?)** There is no specific policy. Each contract is addressed on a case by case basis. **How ready is your organization to bid on contracts in the federal (or commercial)**

	market? What would you need to do to become ready? We are prepared to bid any contract we choose to pursue in the commercial space. **What changes are you seeing in customer motives for outsourcing IT?** Customers are not looking for cost reduction as the primary reason to outsource. Service levels and value to the business units are what they are focused on today. This should be expected since most are evaluated based on customer satisfaction surveys. **To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?** Companies of any size can benefit from an outsourcing relationship. The ability to select a partner you can trust and focus on core compatencies offers significant value. **In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?** Customers are sensitive to the areas of control & IP. Control has not been a sticking point. If there are elements in the outsource that include proprietary data, ownership of the data remains the clients but the processes we put in placa to manage that information remains Perot's IP. Clients typically do not have an issue with you maintaining the IP you bring to them, it's the IP you develop with them that can become a sensitive area. **Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)** Today the bulk of our business is bundled but we are moving towards unbundled. Our preference is to manage in a bundle, but it doesn't matter what we want, it's what the client wants and feels comfortable with in the scope of a relationship.
Raytheon [#7]	**Background** The respondent has been an observer as well as a participant in the outsourcing initiatives of various government agencies. At Raytheon, he played a key role in preparing the company's bid for the NSA's Groundbreaker contract. All of his professional experience has been in the federal market. Currently, Raytheon does less than 5% of its business in commercial markets. **Market Potential** While there is great potential for growth in all segments of both the federal and commercial outsourcing market, Raytheon targets in particular the intelligence agencies—all of which are watching the development of the Groundbreaker contract in order to decide whether to follow. **Market Direction** The outsourcing market as a whole is definitely moving "upmarket." By this, respondent meant a trend toward outsourcing that included hardware as wall as people. Also, he called this "privatization" in distinction from "outsourcing." The distinction hinges on whether, or not, the vendor takes responsibility for staffing and staff operations ONLY, or takes responsibility (if not ownership) of hardware and networks as well. Much federal outsourcing involved rather transperent switches whereby employees left their offices on Friday as civil servants and returned on Monday to the same jobs in the same offices as private contractors. As originally conceived, Groundbreaker was supposed to be a privatization, whereby the vendor would take responsibility for hardware as well as people. For political reasons internal to the NSA, the final contract was scaled back to mere outsourcing, as defined above. The respondent saw this as a great retreat and reacted with disappointment. On the subject of the NSA, the respondent was quite gloomy. He said that the Cray supercomputers the agency had purchased a few years ago would be obsolete within 4-5 years. Even now, Raytheon believes it could build en array of parallel processors that could equal or outperform the Cray supercomputers. As an illustration of mindset of some members of top management there, he described the desk of a high-level agency executive: PC sits in the corner under a dust cover. On the desk sit a legal pad and pencils. A secretary prints out e-mail and takes dictation as if it were 1950. **Barriers to Entry** Respondent believes that virtually every vendor that is active in the federal market wants to diversify by doing business for commercial customers. However, the barriers of entry for moving from the federal to commercial market are formidable. All of the ones noted (financial,

technical, marketing, organization, staffing and management) are relevant. Vendors want to leverage their federal experience into more lucrative work in the private sector, yet they are—in general—totally unprepared for the "cut-throat" nature of commercial competition. Federal salesmen are more collegial and adopt easily a cooperative stance among each other. In contrast, commercial vendors have no need to deal with GSA schedules, or similar bureaucratic obstacles.

Also, salary levels commanded by commercial sales staff are much higher than those applicable to the federal sales staff. For example, salesmen work in the federal market for $75,000 while their counterparts in the commercial market are earning $200-300,000 annually in commission income.

Sales & Marketing

In general, marketing and sales costs will be higher in the commercial market. Although individuals are re-trainable, it is likely that a brand new sales staff would be required by an effort to break into the commercial market from a springboard in the federal sector. Worth noting, personal contacts are critical to success in both markets and salesmen are likely to have cultivated these contacts over a period of years while working successfully in either one, or the other of these markets.

It will be very difficult to convince commercial customers to do business with a vendor that has experience primarily, or entirely in the federal market. A very different set of skills is required. The bridge should be technology and technical skills that are transferable.

Respondent doesn't believe that commercial customers are likely to be impressed by reference clients in the federal market. Reason: commercial customers perceive their technical requirements to be higher.

When asked about the level of technical skill demanded by typical federal customers, respondent insisted that "the federal government doesn't know how to write an effective SLA."

For example, the government writes a SLA that requires all calls to be answered within ten seconds of the first ring. Accordingly, the vendor is rated on his speed of response. Note: there is no metric for the effectiveness of the answer. As a result, vendor could get monkeys to answer the telephone and still get paid!

Capital Constraints

Vendors incur virtually no capital constraints with traditional IT outsourcing. However, in the case of a privatization of government hardware assets, capital is required. Even so, monies can typically be expended incrementally on the road to a complete buyout. The best solution: credit the vendor from the customer's cost-savings so that the vendor acquires eventual ownership of assets at the end of the contract term, without the need to make out-of-pocket cash payments.

Important Changes Underway in the Outsourcing Industry

Primary among these, at least in the federal market, is the anti-outsourcing lobby. Respondent believes strongly that union-led efforts to kill federal outsourcing will lead to disaster. The A-76 machinery in place that attempts to verify the cost-effectiveness of outsourcing is not working well because of the many difficulties in the way of computing federal costs. "Savings" can be deceptive, primarily because they ignore the need for technology "refresh." The desire of federal employees to assure their job security is understandable, but doomed. The skills shortage will grow ever more acute. Also, the federal "customer" is incapable of foreseeing technological advances. The slow procurement cycle ensures that almost whatever is purchased will be obsolete, or almost obsolete by the time it is implemented.

The skills shortage will worsen. Why would young techies want to work for the government, the respondent asks, when they typically have more computing power on their wrist watches, or in their PDAs than they can find on many agency desktops. Techies will be attracted to work environments were they can use cutting-edge technology. Obsolete federal hardware only exacerbates the flight of young techies to the commercial sector.

Financial Metrics

Breakeven on contracts is computed according to a sophisticated model that we use. With it, we can track profitability over time and taking into account changes that occur during the life of the contract.

In general, we expect breakeven to occur about 1-2 years into a contract, assuming an

	average term of seven years. Longer contracts clearly provide better opportunities for economies of scale. Upfront outlays can be problematic. Respondent disqualifies IDIQ contracts from ever being considered "outsourcing," which is done on a fixed-task, fixed-cost or cost-plus basis. In respondent's opinion, an IDIQ contract is "a license to spend marketing dollars." **How Burdensome are Sales and Marketing Costs?** Marketing and selling costs generated prior to presentation of a proposal are difficult to contain. Keeping such costs to a reasonable level is especially important in the commercial market. Their costs need to be better focused, i.e., targeted to specific industries or industry segments. Vendors need to give careful consideration to their core capabilities and show that they understand the needs of commercial customers. **Staffing** Generally, there are few problems involved with absorbing staff through an outsourcing contract—particularly because staff is usually guaranteed no more than two yeas of employment. At that point, the best can be retained and promoted; the nonperformers can be let go. In truth, few federal IT workers feel confident in their ability to compete successfully in the commercial market. Even so, parity and benefits clauses are built into outsourcing contracts in order to assure a high transfer rate.
SAIC [#20]	Respondent has recently moved into a very high level executive position with responsibility for all commercial, and some federal outsourcing business. This new position is more senior than that held by its predecessor and signals a significant reorganization of the vendor's approach to outsourcing—primarily by piercing the stovepipes between the federal and commercial markets. Respondent believes that commercial and federal outsourcing operations should be operated separately—but the units should be able to leverage each other's assets. Respondent has 30 years of experience in outsourcing, beginning at the federal division at UNISYS. As indicated above, he does not believe that a vendor operating in both markets can use the same sales force, but he does believe that the same technical staff can work in both markets. Beyond that, vendors need to pay attention to the differing cost accounting systems used in federal and commercial markets. **Background** Currently, 50% of SAIC's total revenues of $5.5 billion [2000; FYJan 31] derive from business in the federal sector, 50% from the commercial market. Of this,13% represents outsourcing. SAIC's primary vertical markets are: • <u>The oil & gas industry</u> (built around core, global contracts with BP in a large joint venture, Entessa, with Petavesa, the Venezuelan oil company; • <u>Utilities</u> – built on core contracts with Entergy and the Scottish Power authority (SAIC's largest contract); • <u>State and local government</u> – built on the core contract shared with CSC for San Diego County, where SAIC is headquartered. (While the contract was announced as a CSC win, respondent commented that "SAIC brought CSC into the deal.") • <u>Federal</u> – built on core contracts with the FBI for data security and • SW engineering In addition, the financial services and manufacturing industries are also important to SAIC, but to a lesser degree. **Verticals with the Best Outsourcing Growth Potential** Primarily the oil & gas industry, telecom / IT, energy (including the utilities). Respondent believes that the utilities and telecom markets globally are very attractive because of continuing deregulation—which is even a factor in the U.S., as evidenced by California. More important, the utilities and telecom industries have an established billing system in place that reaches all businesses and consumers. This puts them in a very unique position. Other growth areas—financial services and manufacturing, to a lesser extent. **Direction of Business, Upmarket or Downmarket?** The outsourcing business has changed considerably since the 1989-1990 period, which was dominated by the commodity, data- processing model for outsourcing. During the last ten years, outsourcing has become much more "socially acceptable" as a form of business to be

used in both the commercial and federal markets. The government has always used contractors; "outsourcing" came later. Outsourcing has only recently gone beyond the realm of commodity data center work. Top-tier vendors don't want to be in this market segment because they can't do the work with adequate profit margins.

Question: Does the trend toward data centers devoted to Web-hosting represent an exception to this view?

No, because the co-location model for Web-hosting as exemplified by Exodus Communications, which has been essentially a "real estate plus electricity" play is doomed. Exodus is losing money and attempting to move toward a higher value-added, higher-margin "managed services" business model. Elsewhere, this market segment suffers from acute oversupply. IBM and a host of other vendors have been opening new data centers around the world, which is leading rapidly to oversupply relative to demand. This situation reduces Web-hosting to the level of commodity processing, drives prices down and competition up. Vendors such as PSINet thought that they could buy their way into this market successfully (through the Metamor acquisition), but they learned that it wasn't enough to purchase assets; you need to know what to do with them (which PSINet didn't).

Barriers to Entry

The primary barrier to entry is the need for a new sales force. You can't use the same salesmen for the commercial market as you did for the federal market. Salesmen need to have a keen understanding of their customers' markets. Exacerbating this situation will be the inability of salesmen to impress commercial clients with accounts of work done by the vendor in the federal market. In contrast, federal clients tend to be impressed by what vendors have done/are doing in the commercial market.

Nevertheless, respondent thought that making a transition from the federal to the commercial market would more difficult than the reverse due to the complexity of the regulations that govern the federal procurement process.

Teaming with vendors already established in a new market only works if you are small. A large vendor must buy its way into a new merket by acquiring a service provider that is already established and respected based on successful, on-going business in the new industry.

Capital Constraints

While large infrastructure outsourcing deals require large amounts of capital, other forms of outsourcing do not.

Leasing arrangements will always represent a costly, premium solution from the client's point of view. He thought that only an unsophisticated customer would accept a leasing arrangement.

The BOT option is an acceptable alternative, but one that is not often used because clients seldom want to take IT work back in-house once it has been outsourced.

Important Changes in the Outsourcing Market

Customers are becoming more sophisticated and outsourcing is becoming more acceptable. CIOs used to oppose outsourcing; now, they embrace it. The size of deals is getting smaller, which reflects—in part—reluctance to give up too much control (customers are giving a larger number of smaller-sized outsourcing contracts to multiple vendors).

Question: Is the role of customer-engaged consultants becoming more common and more important?

Yes, but consultants can create a conflict of interest with clients because they are paid on a time-spent basis. Therefore, it is to their interest to lengthen the sales/proposal/bid process rather than shorten it.

When asked if vendors could, or should depend on consultants to bring them into outsourcing deals in new markets, respondent commented that this was a "loser's point of view, depending on the consultants used." He said that Cap Gemini had won some excellent business through TPI and other consultants because, while the vendor's work was good, it had little name recognition in the U.S. market. Consultants liked being able to recommend a lesser-known, but high-quality vendor to clients because it made them appear more competent.

Respondent emphasized that the use of consultants to bring in outsourcing business should be regarded as merely an alternate sales channel, not one that any vendor could rely on exclusively.

	Most Profitable Kinds of Outsourcing Work SAIC can do the management and development of SW applications most profitably—along with related consulting. For a somewhat lower margin, it could also do network management profitably. Clearly, data center management and desktop management were the least profitable types of outsourcing for SAIC. **Burdensome Sales and Marketing Costs** In the commercial market, a vendor may spend more as a percentage of the total size of the contract. In the federal market, vendor marketing costs may be lower as a percentage of (larger) sized contracts, but the absolute dollar amounts will be similar to costs in the commercial market. While the cost of sales is higher in commercial markets, the gross profit margin is also substantially higher, so deals in that market can bear the higher sales costs without depressing net profits. **Problematic Staff Transfers** Difficulties in transferring staff as part of an outsourcing deal has not been a problem for SAIC—partly because it avoids commodity data center contracts. If client wants to effect a staff transfer in order to reduce headcount, HR processes and procedures become very important. However, for high-margin, high value-added work, staff transfers are rarely an issue. Overall, SAIC as an employee-owned firm has little turnover. This status gives it a "positive discriminator" in the market, i.e., it is perceived to be a highly desirable new employer. **Policy toward unions?** They will remain marginal players in the IT industry for the foreseeable future.
The Outsourcing Institute [#2]	The respondent has a broad background in IT outsourcing, having worked at UNISYS, AT&T Solutions, Cap Gemini and other firms prior to The Outsourcing Institute. Previously, he worked with Victor Millar, co-founder of Andersen Consulting, who is now CEO of VC Fund. He has been selling IT outsourcing deals since 1982. **Background on The Outsourcing Institute** It is a private organization that was formed in 1993. It owns a Web site. The purpose of the organization is to become a primary resource for the outsourcing industry, along the lines of a professional association, but with practical benefits. The Institute hosts Forbes magazine events and co-sponsors publications. It aims to be a neutral clearinghouse for information on best practices, events, etc. It coordinates with DCI on participation in large, industry events. It has no paid membership, but has built a DB ("Accelerator") of 24,000 industry participants—including buyers, sellers and "influencers." The organization derives income from consulting fees and provision of various kinds of marketing assistance. In addition, the Institute receives income from finder's fees generated by helping vendors win new outsourcing business for vendors. (Typically, 8-15% of total contract value is spent on deal marketing.) Currently, the Institute maintains an Outsourcing Index, which is the core of its clearinghouse efforts. The organization has a staff of 18 people, headed by its founder, Frank Casale. Initially, Michael Corbett was a principal in the organization, but he subsequently founded his own company, Michael Corbett & Associates, which is an outsourcing consultant. At present, the Institute is seeking VC funding. In his opinion, generally, the federal and commercial outsourcing businesses of vendors are operated in complete independence. He regards this as unfortunate. *The Accelerator*—offered on the Institute Web site—was conceived as a start up portal for the exchange of data by all participants in the outsourcing process. **Outsourcing Growth Potential** He sees the best growth potential in financial services, manufacturing (particularly for supply-chain-related work, and for facilities management work for companies like Bechtel and Fluor). He believes that IT outsourcing only represents about half of the total outsourcing market. The next largest segment is facilities management, both pure real estate and a sophisticated mix of real estate and IT. The last segment is HR management. [This split ignores manufacturing outsourcing.] In respondent's view, it is unfortunate that the federal and commercial sides of outsourcing management are usually entirely separate.

	Industry Direction He sees the outsourcing industry moving clearly "upstream" toward BPO as vendors offer increasingly more comprehensive packages of services. **Barriers to Entry** Regarding barriers to entering new markets, respondent believes strongly that "deals are done between people." Therefore, sales and sales management are critically important. Also criticel are project managers, who are becoming increasingly "free agents" in the industry ("wheeler-dealers"). The most experienced project managers come from the federal market, which has developed an established methodology for project management. **Availability of Capital** While deep-pocket financial resources always confer certain advantages, neither availability nor cost of capital should be considered an obstacle to bidding new outsourcing business. Judicious management of leasing relationships and contracts can obviate the need for vendor borrowing. Another possible solution is to form a customer/vendor joint-venture, or partnership that permits off-balance sheet financing. *The way to enter any new market is to find an anchor client that is willing to serve as a reference in that segment.* **Differences Between Federal and Commercial Markets** Differences between federal and commercial market? The bid/proposal process in the federal market can be very long, detailed and burdensome. The sales cycle in the commercial market is usually shorter and simpler. In either case, it is important to write detailed SLAs that are flexible enough to take into account changes in business conditions. EDS was/is perticularly good at this aspect of bidding. In some cases, vendor experience in the federal market can be used to advantage in the commercial market. Examples of vendors that have done this with great success include: CSC, Lockheed Martin and Litton. Initially, virtually all of their business was in the federal sector, but slowly and quietly, commercial deals began to happen. **How to overcome customer resistance in the commercial market?** Explain what you did in the federal market. Emphasize the scale and scope of those projects. For example, CSC began with labor-intensive, multivendor federal projects and advenced to sophisticated technical work as a prime contractor. Don't neglect to mention your experience with federal staff transfers in connection with outsourcing deals. In the federal market, transfers of 200-300 people are common. The lack of vertical industry knowledge in the commercial sector should not pose an insurmountable handicap. Federal market vendors should be able to leverage their federal experience based on what their people actually accomplished. Avoid splashy advertising. This will only waste money. However, consider that you may need a new sales team. Federal sales are built on established *relationships*. Also, relations between vendors and the government are often contentious (which can only be handled by experienced sales people). Also, expect deals to be done in the commercial sector at greater speed, involving unexpected developments. Expect as well top executives to wield a great deal of clout, whoever may present himself initially as a decision-maker. One point worth noting: many marketing practices that are common in the commercial sector, such as client entertainment, are illegal in the federal market. **Unions** On the issue of private sector unions, respondent advises vendors to try to avoid dealing with unions. They could create serious and problematic issues.
UNISYS [#16]	**Background** Respondent is a Manager of Market Development & Planning. He has worked with leading providers of outsourcing to both commercial and public-sector marketplaces. **Outsourcing Experience** About 10% of UNISYS revenues derive from outsourcing. **In which vertical industries do you see the best growth potential for IT outsourcing?**

	The public sector.
	Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?
	Our business is clearly moving upmarket, but we are however a full-service provider.
	How would you categorize the most important barrier to entering a new market, Financial? Technical? Marketing? Organization? Staffing? Management? Other?
	Federal A-76 plans play an important role in outsourcing. Staffing and Marketing are also significant barriers.
	To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?
	Bid activity/capital is based on priority of the outsourcing bid.
	What important changes do you see at work in the outsourcing market today?
	In the federal marketplace, UNISYS believes that outsourcing will play a significant role as government is being downsized and asked to do more with less. A-76 issues and unions need to be addressed.
	Top down, which types of outsourcing can you do most profitably? (Reasons?)
	Data Center, Infrastructure and transaction processing.
	In which type of outsourcing do you have the most expertise and success? (Future?)
	Data Center and Infrastructure management.
	What process do you use for computing the cost of contract bidding?
	Our bids are based on contract type and requirements.
	Do you have a dynamic model for estimating totel contract profitability as changes are made over time?
	Yes
	How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)
	Some Federal bid/sales expenses are much lower than in the commercial market.
	Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)
	No
	What is your policy toward dealing with unions? (How important?)
	Not applicable.
	How ready is your organization to bid on contracts in the federal (or commercial) market? What would you need to do to become ready?
	We are actively involved in both commercial and federal outsourcing.
	What changes are you seeing in customer motives for outsourcing IT?
	They are increasingly motivated by the IT skills shortage; also, corporate downsizing is a critical issue.
	To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?
	Past performance should be more important than company size.
	In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?
	In the federal marketplace, control is very important issue.
	Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)
	Bundled
USInternet-working [#14]	**Background**
	Respondent is a VP for public sector sales. However, prior to assuming this position in spring

2000, he had extensive experience in the commercial IT outsourcing market, beginning with CSC in 1974. At USI, his role includes business development, sales, staffing, and new client capture in the public sector, which at USI includes all of higher education.

At USI, the sales force is organized according to geographical territories. Within each territory, there are multiple VPs with differing responsibilities within the region. Within regions, there is some focus on specific vertical industries depending on which companies are prominent in the area, rather than on a corporate strategy for such diversification. In fact, USI wants to market to all vertical industries because it positions its offer as essentially a "horizontal" service that should be attractive to all companies that share certain non-industry characteristics.

Beyond that, USI wants to come to market by highlighting the specific applications that it offers, rather than its vertical industry expertise. Nevertheless, the company does enjoy some industry-specific advantages in regard to BroadVision for retailing and PeopleSoft in insurance.

Market Position

In respondent's view, the advent of the ASP model represents a significant evolution in the IT industry. He believes that vendors such as CSC, EDS and IBM Global, on the whole, target very comprehensive contracts that include data centers, networks, applications, etc. In contrast, USI targets ONLY the demand for specific apps.

Commercial vs Public Sector Market

To date, USI has only seven clients in the public sector, six in the federal market and one in state and local (the NY Port Authority). Currently, the company is focusing on potential business with the State of Maryland, which leverages its advantageous location in Maryland's state capitol, Annapolis.

Public sector business comprises only 5-10% of USI's total revenues. In the federal market, USI has chosen to partner with big SI vendors. Typically, these vendors do not want to make a large, new investment in hardware and find USI's remote app delivery an attractive alternative.

From a marketing point of view, USI benefits from the extensive customer relationships of these top-tier vendors, e.g., PWC, EDS, IBM. USI believes that it is gaining valuable exposure through partnering. Regarding profitability, while it is true that federal contracts usually carry lower profit margins, their size tends to be larger, which serves as an off-setting factor. As a result, USI has taken no "profit haircut."

Best Potential for Outsourcing

In respondent's view, the ASP offer will be even more attractive to the public sector than to the commercial sector due to the coming wave of retirements of federal IT workers. In his view, the problems created by these retirements will be exacerbated because it will severely handicap the government's independent ability to develop and manage critical SW applications. In addition to the public sector, USI views the financial services (including insurance) and healthcare industries as particularly good prospects. Also, retailing looks promising because retailers are now accepting the need for new e-commerce strategies (that require specialized apps).

Far from suffering from fallout of the demise of the dotcoms, USI enjoys an increasingly prominent and positive market position: "USI is being wooed by big systems integration vendors." USI considers itself to be the number one ASP in the industry, with special expertise in ERP (including Lawson, SAP and Oracle). In fact, less than 10% of USI's clients are dotcoms.

Market Direction

Respondent believes that both the commercial and public sectors are moving "upmarket." From the point of view of USI, this trend has been evidenced by the extent to which customers demand multiple applications as they attempt to integrate legacy systems. To meet this kind of demand from the State of Maryland, USI partners with CSC and SAIC.

Barriers to Entry

USI does not see the same set of competitors in the commercial sector as it does in the federal sector. Reason: there are significant barriers to entry in the federal market. USI has a geographical advantage being located close to Washington, D.C. Federal buyers have been reassured that the company understands its security needs, in part, by making personal, on-site visits to USI's Annapolis facilities.

Moving from the federal to the commercial market is much more difficult. Reason: difference in mindset of vendor staff, difference in the accounting systems used. Also, entering the commercial market requires a large capital investment. Moving from one market to the other requires establishing a new sales team. Commercial salesmen need a substantial re-orientation in order to be successful in the federal market. Also, personal relationships are very important—in terms of clients and SI vendor/partners.

While relationships are always important and valuable to sales, they are MORE important in the federal market. This is also true in the state and local government markets. At the state level, ALL sales are based on personal relationships.

Lack of name recognition could be an important problem. Clearly, vendors with an established reputation in the commercial market will find it easier to leverage that success in the federal market than the reverse. Achieving distinction in some kind of specialization can offer a shortcut solution to this problem.

Vendors with commercial experience that enter the federal market typically agonize over the "crawling pace" of the sales cycle when compared to the commercial market.

Cost of Capital

Cost (and availability) of capitel is a serious issue and a barrier to entry. Undercaptalization has caused the demise of numerous would-be ASPs. The ASP business is very capital intensive for vendors and USI has been successful in the market to a large measure because it has been very successful in raising equity funding. Bottom line: USI has, itself, lost no new business due to insufficient capital.

Changes in the Outsourcing Market

Today, there is much better recognition of the value of IT outsourcing than there was previously. And there is better understanding of the ASP model—albeit acceptance has been quicker in the commercial market than in the federal market.

Currently, USI has a total of 208 clients, signed over the past two years (during the first year of the company's existence, it was not operational). Total value of signed contracts exceeds $400 million. USI gained its first public sector client in 2Q 1999, it second in 3Q 1999, and the remaining ones in 3Q and 4Q 2000.

Use of consultants?

Respondent: "I don't like consultants because they are difficult to manage. I prefer the direct sales model. We rely on outsourcing consultants to bring us into deals, but we must maintain our own in-house sales force as well. At the least, we need sales closers.?"

Market Growth

Major federal agencies want to use the outsourcing model (Justice, Transportation, Agriculture). USI sees no effect yet from the TRAC anti-outsourcing initiatives in Washington. There are many counterpressures. In the end, the federal government will realize that it has no viable alternative to outsourcing because it will soon be unable to operate its own IT infrastructure. Enterprise software, such as PeopleSoft is relatively labor-intensive, and the federal civil service cannot attract sufficient numbers of skilled staff required to operate such applications.

Unions

Because USI does not "threaten" to take over the data center, it keeps a lower profile than the SI vendors and has not been target of the anti-outsourcing groups.

DoD? No business there for USI yet. The current sales staff has entirely a civilian orientation.

Sales & Marketing

Finally, while there are potential prospects in every vertical industry, you must spend your sales and marketing budget according to targets and priorities. Spending in too many directions at once will prove unsuccessful. Insofar as there is a tendency to "verticalize" the sales and marketing staff, it is best to let this happen naturally in the course of doing business, rather than by top-down planning.

Exhibit D-3

Tabulation of User Interview Survey Responses by Respondent

	Eaton Corp
	2. What is your role?
	Overall IS responsibility
	3. Please indicate the nature of your experience with outsourcing (IT or otherwise).
	Varied, used extensively for development and ERP work. Some e-business, Website design and some related development.
	4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)
	No, we prefer to award specific contracts for a discrete piece of work.
	5. To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?
	Recoverable costs from departmental budgets.
	6. How do you determine which outsourcing vendors to invite to bid?
	We work from an existing list of preferred (known) vendors to which we add and remove. Generally an outsourcing contract is awarded to a company with which we have an already established relationship.
	7. How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?
	Not really applicable. They would have to meet the criteria (as per Q6)
	8. How important is the outsourcer' ability to attract and acquire your targeted staff (as part of a proposed contract)?
	Not really important. We tend to outsource contracts when we lack sufficient internal resources. Our in-house staff either assists these contracts in secondary role, or is assigned a new piece of work (totally unrelated). Transfer of staff has not occurred to date.
	9. What important changes do you see at work in the outsourcing market today?
	More selective. The market is becoming more discrete, with organizations having greater specialization. I think that there is a decrease in the "larger all-encompassing" projects. User companies lack some of the management tools internally, the vendor must proactively manage the customer (as well as the project). Outsourcing is moving away from maintanance of products and support of users towards working on new architecture and solution development..
	10. Which type of outsourcing fits best your company's needs? (and why)
	Smaller independent companies that provide specific services. Help desk, Internet Web services, production of documentation, training, raw coding and programming. Not purely a support arrangement; they need to provide stability in an older operating environment.
	11. How is outsourcing affecting your industry? (Effect on growth? Profitability?)
	Not measurable in commercial business terms. Outsourcing is an essential link with our in-house technical delivery teams. We have improved time scales for on-going development and achieved better quality at a reasonable cost.
	12. How has your attitude toward IT outsourcing changed over the past year?
	Little. We are committed to a business transformation program and outsourcing is part of that building block for the future.

	13. Are you as attracted by outsourcing entire business processes as by off-loading commodity transaction processing?
	Not at all. Our policy towards outsourcing is (as per Q10)
	14. Have you computed the contribution made by outsourcing to your company's overall profitability? (To cost-reduction of IT depart?)
	We have been able to reduce our internal headcount and not have to increase new-skill recruitment. We have also been able to better control the overall IT overhead and budget. We are maximizing the returns on our original IT investment; bringing operational benefits to the company.
	15. Do you prefer longer or shorter contract durations? (Why?)
	Our contracts have always tended to be short and we don't see this changing.
	16. Have you in mind a ranking regarding which types of outsourcing are the most costly? (Reasons?)
	No
	17. In relation to outsourcing, how sensitive are you to the issue of control, in general, and control of proprietary data in particular?
	Very sensitive.
	18. How strong is your relationship with incumbent outsourcers? (Probability of sole-sourcing new contracts?)
	Relationship is good. We always have prior working knowledge and exposure with the vendor, so our risk is minimized.
	19. To what extent, if any, have union relations affected your desire or ability to outsource?
	Not an issue.
	20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?
	Doesn't really bother us. We tend to avoid the large players as we get better service from smaller companies.
HOLOGIC, INC	
	2. What is your role?
	Overall director of all IT
	3. Please indicate the nature of your experience with outsourcing (IT or otherwise).
	Have been involved in several outsourcing arrangements in many mixed environments
	4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)
	In an ideal world, we would go with as much bundled as possible. We have a large contract with ADP, but we still have the need to place 2-3 other individual contracts with other service vendors
	5. To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?
	The primary reasons were that we had a mixed environment of DEC/Compaq, Solaris and Unisys. Control of this became very difficult and cumbersome, so we started to outsource different elements of this. We did have the objective to reduce the main overhead of the service cost and to be able to complete other (new) IT projects faster.
	6. How do you determine which outsourcing vendors to invite to bid?
	• Proven record, expertise. Must be a solution provider. Knowledgeable in our application types and operating environment. Proven success on similar types of outsourcing projects. • Expertise in Web-enabled financial software.

	7. How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?
	In theory it would not prevent us. Our current situation is that we have contracts to be outsourced. We want to remove that responsibility from us to a partner vendor to allow the vendor and ourselves to focus on our technical strengths.
	8. How important is the outsourcer's ability to attract and acquire your targeted staff (as part of a proposed contract)?
	Important in that they manage the human resources. We had problems in recruitment and retention of staff, so this is an essential part of the project.
	9. What important changes do you see at work in the outsourcing market today?
	Some services are easier to contract out now. Operational duties are spreading into new IT areas especially CRM. Outsourcing is now an acceptable process and customers are more intuitive.
	10. Which type of outsourcing fits best your company's needs? (and why)
	Support for specialist software packages, project management, BPR. All e-business services and internet integration.
	11. How is outsourcing affecting your industry? (Effect on growth? Profitability?)
	The skills are available, but the costs are very high. A high proportion of our overall IT budget now goes to external contracts. We have definitely seen a reduction in capital and recurring costs. Outsourcing has allowed us to stay ahead competitively by increasing the time scales to develop new applications.
	12. How has your attitude toward IT outsourcing changed over the past year?
	Inertia towards external service suppliers in some circles; thoughts are that we will obtain a better return on IT using in-house staff. Even though there is a general shortage of key skills; the service vendors don't necessarily have the skills either.
	13. Are you as attracted by outsourcing entire business processes as by off-loading commodity transaction processing?
	Only if they can provide edded value for enhancement and support. Improvements in change are usually never achieved. Trying to combine external and internal resources (as present) can be very difficult, but outsourcing the entire IT and business processes would be a massive decision.
	14. Have you computed the contribution made by outsourcing to your company's overall profitability? (To cost-reduction of IT depart?)
	Ultimately, the measurement has got to be reflected in the success of the business generation. Lower operating costs, greater turnover, numbers of increased transactions; do you ever know the real story????? It depends on the business model that is being adopted.
	15. Do you prefer longer or shorter contract durations? (Why?)
	As long as they are on time and within budget.
	16. Have you in mind a ranking regarding which types of outsourcing are the most costly? (Reasons?)
	• Using external resources doesn't necessarily improve costings, it merely moves them from one business unit to another. • Mainstream support of MVS and UNIX systems • Technology integration with requirement for special technical disciplines. • Bespoke [customized] applications running on AS/400s.

	17. In relation to outsourcing, how sensitive are you to the issue of control, in general, and control of proprietary data in particular?
	We introduced our own best practice.
	18. How strong is your relationship with incumbent outsourcers? (Probability of sole-sourcing new contracts?)
	Service suppliers lack the understanding of fostering relationships; they are driven by short-term objectives. There is always a perceived conflict, but we have better control of the resources that support our organization.
	19. To what extent, if any, have union relations affected your desire or ability to outsource?
	Discussions with the unions to keep jobs in-house. They are selling the long-term benefit of keeping expertise internally.
	20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?
	It does influence you if the contract has significant $ value, or it is critical to the strategy.
GARDEN WAY, INC	
	2. What is your role?
	IS Development Manager
	3. Please indicate the nature of your experience with outsourcing (IT or otherwise).
	I have final decision on all outsourcing (customized and otherwise).
	4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)
	Bundled. We manage all our outsourcing through KPMG.
	5. To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?
	Originally to reduce our headcount and look at ways of reducing our cost base. Laterally we are now looking for expertise in specific disciplines and to improve development performance. To improve the key components and business functionality. While we want KPMG to provide better service, we also want them to be more customer focused.
	6. How do you determine which outsourcing vendors to invite to bid?
	• We always use KPMG as our principle partner who will manage the overall contracts. • There are about 20 other organizations that we define and from which we source the operational services, but the contract is planned and managed by KPMG. • Single-source contract for urgency and proprietary systems support.
	7. How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?
	I would have my doubts, not really decided yet.
	8. How important is the outsourcer' ability to attract and acquire your targeted staff (as part of a proposed contract)?
	Not important.
	9. What important changes do you see at work in the outsourcing market today?
	More procurement via the Internet. Big changes in the variety and type of service; allows expansion into other areas. Greater professionalism.
	10. Which type of outsourcing fits best your company's needs? (and why)
	An application management and support role for ERP. Answer to our skill shortages; can be the most practical solution.

	11. How is outsourcing affecting your industry? (Effect on growth? Profitability?)
	Improved efficiency on the supply chain. Faster and cheaper to get our applications and services up and running.
	12. How has your attitude toward IT outsourcing changed over the past year?
	More positive; allows staff more time for other applications. Lead times for service have improved, greater responsiveness from the vendor leading to greater satisfaction all round.
	13. Are you as attracted by outsourcing entire business processes as by off-loading commodity transaction processing?
	Yes
	14. Have you computed the contribution made by outsourcing to your company's overall profitability? (To cost-reduction of IT depart?)
	Yes. We have seen the benefits of joint ventures and strategic alliances; both parties share costs and resources.
	15. Do you prefer longer or shorter contract durations? (Why?)
	Shorter contracts are easier to control and manage. They also keep costs down as more regular contract renewals maintain a more competitive environment. In longer contracts, vendors have a greater opportunity to "milk you" for higher prices.
	16. Have you in mind a ranking regarding which types of outsourcing are the most costly? (Reasons?)
	Would give a lot of thought to ERP contracts costing >$2 million
	17. In relation to outsourcing, how sensitive are you to the issue of control, in general, and control of proprietary data in particular?
	Very sensitive about the manufacturing process – would not want this to go externally.
	18. How strong is your relationship with incumbent outsourcers? (Probability of sole-sourcing new contracts?)
	Good
	19. To what extent, if any, have union relations affected your desire or ability to outsource?
	None, we are a nonunion shop
	20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?
	Great influence, size and longevity are important.
AMERICAN CRYSTAL SUGAR COMPANY	
	2. What is your role?
	IS Director
	3. Please indicate the nature of your experience with outsourcing (IT or otherwise).
	Main decision-maker in all major IT decisions.
	4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)
	We end up with a balance. We had a policy to widen the supplier base and to bring in a greater level of knowledge and expertise. Better commercial advantages in not bundling the contract
	5. To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?
	• Better service and support. • Improved staff usage and utilization. • Well suited to development and custom projects. • Relieve the workload to the existing IT team.

	6. How do you determine which outsourcing vendors to invite to bid?
	• Cost • Quality of company and their people. • Team building and management. • To manage the applications through development testing and production. • Able to meet demanding delivery requirements. • Process functional and technical skill sets.
	7. How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?
	• "Give me a name". • In a hypothetical situation, I would say that if the vendor possesses quality, service and speed in implementing a quality standardization program, then federal-only experience should not be an issue. • One or two large federal contracts can allow an organization to grow very rapidly. Companies like EDS were very heavily involved in federal contracts and it didn't really prevent the company from moving into the commercial market.
	8. How important is the outsourcer' ability to attract and acquire your targeted staff (as part of a proposed contract)?
	If we do not want to continue with a large in-house IT resource, then the supplier must fulfill that role.
	9. What important changes do you see at work in the outsourcing market today?
	• Must show tangible improvements. • Facility to increase communication. • Commitment to achieving specific goals. • Support the complete process and shape the business model.
	10. Which type of outsourcing fits best your company's needs? (and why)
	• That by which we can better satisfy our customers and users. • We want to strengthen the team at operational level and oversee the technical side of the legacy projects. • Support of the wider business units.
	11. How is outsourcing affecting your industry? (Effect on growth? Profitability?)
	• I think that we have achieved: • Improved service levels to users. • Enhanced the level of support. • Provide control and improved quality. • From a commercial point of view, we have reduced operating costs whilst experiencing very tough trading conditions.
	12. How has your attitude toward IT outsourcing changed over the past year?
	• More confident in design and reviewing operational models. • Processing and operational control have improved considerably. Account management is easier to control and manage.
	13. Are you as attracted by outsourcing entire business processes as by off-loading commodity transaction processing?
	We have very ambitious plans and want to be able to move forward much faster. We are aware of the wider capabilities (of entire outsourcing), it will make us internally more effective and improve those internal processes. It could eliminate major integration issues further down the line.

	14. Have you computed the contribution made by outsourcing to your company's overall profitability? (To cost-reduction of IT depart?)
	• Improved customer satisfaction – overall pleasing. • IT expertise at a cheaper price than it would take us to maintain personnel in-house. • Able to monitor and evaluate specific "hard success" criteria. Creation of brand awareness and loyalty. Superior levels of customer services.
	15. Do you prefer longer or shorter contract durations? (Why?)
	Through our legal dept.
	16. Have you in mind a ranking regarding which types of outsourcing are the most costly? (Reasons?)
	Performance improvement – reducing costs and improving service.
	17. In relation to outsourcing, how sensitive are you to the issue of control, in general, and control of proprietary data in particular?
	Undergoing a re-think about this. We don't want to force through unpopular policies, but we need to protect our intellectual interests.
	18. How strong is your relationship with incumbent outsourcers? (Probability of sole-sourcing new contracts?)
	Reasonably good teams who meet most of our criteria. Ambiguity is always the big problem.
	19. To what extent, if any, have union relations affected your desire or ability to outsource?
	Not really from unions, but existing staff want some form of contractual obligation (in relation to secure employment)
	20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?
	Always in the "hidden" agenda. No customer is ever going to say "we will only award this contract to a large company," but–in reality–this is commonplace.
OMEGA FINANCIAL	
	3. Please indicate the nature of your experience with outsourcing (IT or otherwise).
	Extensive. Have been involved in outsourcing for at least 10 years.
	4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)
	Yes, we can leverage the price.
	5. To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?
	Where we cannot keep talented people fully employed
	6. How do you determine which outsourcing vendors to invite to bid?
	We merged with another bank, so we are jointly using the incumbent supplier. However, we are seeking due diligence for the next contract award.
	7. How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?
	Not a problem, providing the other requirements were met.
	8. How important is the outsourcer' ability to attract and acquire your targeted staff (as part of a proposed contract)?
	Have had a delicate situation in the pest that was resolved, but it is something that we need to be careful about. Existing staff working for a large financial services company would not be too keen to move to a smaller IT services company.

	9. What important changes do you see at work in the outsourcing market today?
	Banking is changing. It now encompasses a full range of services including insurance, stockbroking, etc,. We need an outsourcing company to take us into the future. We need improved service at lower cost.
	10. Which type of outsourcing fits best your company's needs? (and why)
	Facilities Management and procurement. An efficient service that works 24 hours a day, able to improve business processes all round.
	11. How is outsourcing affecting your industry? (Effect on growth? Profitability?)
	Not measurable.
	12. How has your attitude toward IT outsourcing changed over the past year?
	Still receptive to OS.
	13. Are you as attracted by outsourcing entire business processes as by off-loading commodity transaction processing?
	Yes.
	14. Have you computed the contribution made by outsourcing to your company's overall profitability? (To cost-reduction of IT depart?)
	Overseen by our auditors. Specific cost reductions in operational overheads have been achieved; lower support and operational costs on the longer term.
	15. Do you prefer longer or shorter contract durations? (Why?)
	5-yr contracts
	16. Have you in mind a ranking regarding which types of outsourcing are the most costly? (Reasons?)
	Yes, only through experience.
	17. In relation to outsourcing, how sensitive are you to the issue of control, in general, and control of proprietary data in particular?
	Not sensitive. Have a 3rd party for control and security.
	18. How strong is your relationship with incumbent outsourcers? (Probability of sole-sourcing new contracts?)
	Very good.
	19. To what extent, if any, have union relations affected your desire or ability to outsource?
	No effect
	20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?
	Is a factor, but decisions are "horses for courses." If your volume of business is such that it represents a disproportionately high % of the vendor's revenue, then this could be a problem in terms of risk and exposure.
	ROCHESTER DEMOCRAT & CHRONICLE
	2. What is your role?
	VP-IS
	3. Please indicate the nature of your experience with outsourcing (IT or otherwise).
	I call "all the shots".
	4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)
	Prefer bundled contracts, due to the cost ratio.

	5. To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?
	No response
	6. How do you determine which outsourcing vendors to invite to bid?
	They need experience of front-end systems and vast exposure to the newspaper industry.
	7. How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?
	I would not be unreceptive, but they would need to have considerable experience of our industry (otherwise we would not get seriously involved with them)
	8. How important is the outsourcer' ability to attract and acquire your targeted staff (as part of a proposed contract)?
	Hasn't happened yet; would put it down as unimportant at present.
	9. What important changes do you see at work in the outsourcing market today?
	Much larger stable nowadays. Greater choice of vendors, more experience, more extensive knowledge and also a great deal more business process outsourcing than ever before.
	10. Which type of outsourcing fits best your company's needs? (and why)
	The type of contract is secondary to obtaining the correct skill fit. If we get the right vendor with exactly the right type of skills and service offering, we would ask them to propose alternative contract solutions to us.
	11. How is outsourcing affecting your industry? (Effect on growth? Profitability?)
	No response
	12. How has your attitude toward IT outsourcing changed over the past year?
	I am more relaxed about outsourcing.
	13. Are you as attracted by outsourcing entire business processes as by off-loading commodity transaction processing?
	Yes, if we can see that there are real beneficial gains for us.
	14. Have you computed the contribution made by outsourcing to your company's overall profitability? (To cost-reduction of IT depart?)
	No model as such, but costs come from the overall IT budget.
	15. Do you prefer longer or shorter contract durations? (Why?)
	Shorter contracts carry less risk to us. Fewer things can go wrong.
	16. Have you in mind a ranking regarding which types of outsourcing are the most costly? (Reasons?)
	No
	17. In relation to outsourcing, how sensitive are you to the issue of control, in general, and control of proprietary data in particular?
	• Not too big a problem. • Obviously the vendor will sign confidentiality clauses. • The concept of partnership is very important to us and we would never enter into a relationship with a supplier if mutual trust did not exist.
	18. How strong is your relationship with incumbent outsourcers? (Probability of sole-sourcing new contracts?)
	Good, as per Q17
	19. To what extent, if any, have union relations affected your desire or ability to outsource?
	Not a problem

	20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?
	In some ways experience has shown us that the bigger the company, the more expensive the cost. However, they would argue that the bigger the supplier, the less the risk is to the customer.
AMPHENOL	
	2. What is your role?
	Responsible for all custom development and integration services.
	3. Please indicate the nature of your experience with outsourcing (IT or otherwise).
	Have placed (awarded) many contracts. Also spent many years as project manager on large-scale outsourcing contracts.
	4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)
	No preference. The contract will reflect the service program that needs to be outsourced. Contracts can have different durations and termination dates, so even if we wanted to bundle them, sometimes it is not logistically possible.
	5. To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?
	In the early days, outsourcing was done for commercial considerations. Nowadays, we have more sophisticated reasons—specific projects, core or scarce skills.
	6. How do you determine which outsourcing vendors to invite to bid?
	Technical ability, reputation, "chemistry".
	7. How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?
	Would not bother me. We have a lot of contracts with government bodies, so we are fairly competent in this area.
	8. How important is the outsourcer' ability to attract and acquire your targeted staff (as part of a proposed contract)?
	Not important at present
	9. What important changes do you see at work in the outsourcing market today?
	I would see over the longer term more of our IT coming back in-house.
	10. Which type of outsourcing fits best your company's needs? (and why)
	Smaller development and maintenance contracts with 12 months duration.
	11. How is outsourcing affecting your industry? (Effect on growth? Profitability?)
	• If outsourcing is applied well, the results are positive and lead to improved profitsbility. • The problem seems to be that it can be very difficult to objectively assess the impact of outsourcing. • For instance, if we reduce headcount by a factor of X (as a result of the outsourcing), could we not have just reduced the number of staff anyway. • If we increased profitability, how do we know that outsourcing had anything to do with it.
	12. How has your attitude toward IT outsourcing changed over the past year?
	No, perhaps I am slightly more cynical. I certainly expect a lot more from the vendor, added-value is a must!!!!
	13. Are you as attracted by outsourcing entire business processes as by off-loading commodity transaction processing?
	No, as per Q10

	14. Have you computed the contribution made by outsourcing to your company's overall profitability? (To cost-reduction of IT depart?)
	No
	15. Do you prefer longer or shorter contract durations? (Why?)
	Short contracts of about 12 months
	16. Have you in mind a ranking regarding which types of outsourcing are the most costly? (Reasons?)
	No
	17. In relation to outsourcing, how sensitive are you to the issue of control, in general, and control of proprietary data in particular?
	Nothing sensitive here
	18. How strong is your relationship with incumbent outsourcers? (Probability of sole-sourcing new contracts?)
	Current relationships are good.
	19. To what extent, if any, have union relations affected your desire or ability to outsource?
	Not at all.
	20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?
	Tend to use smaller local companies that are cheaper and keener.
MORGAN DRIVEWAY, INC	
	2. What is your role?
	Manager of all IT
	3. Please indicate the nature of your experience with outsourcing (IT or otherwise).
	Senior role in all outsourced IT programs.
	4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)
	• Large development programs in place (and planned). • There are presumed cost advantages in bundling the services, but it can be difficult to achieve a consistent level of operational service. • We need to ensure that our commitments are met. The vendor supplying development services is not necessarily the best vendor to operate the Data Center.
	5. To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?
	• We have no expertise or business knowledge of e-commerce (which is our most recent project). • Different programs are outsourced for differing reasons, ie, access to expertise is scarce, reduce the cost of delivery service, implementing corporate intranet, etc, but I suppose the bottom line is that the cost advantage must be prominent.
	6. How do you determine which outsourcing vendors to invite to bid?
	The usual criteria of relevant experience, quality of work, proven in field and familiar with our technology.
	7. How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?
	• Not a problem per se. • But they would have to meet our criteria in terms of project management experience, able to develop Web business applications and B2B consultancy skills. • I guess that I would not want to be their FIRST customer.

	8. How important is the outsourcer' ability to attract and acquire your targeted staff (as part of a proposed contract)?
	They would be required to manage our contractors plus recruit new skills. Transfer of existing staff to the outsourcing company would be subject to discussion.
	9. What important changes do you see at work in the outsourcing market today?
	New philosophy of achieving excellence. Vendors now have a proven track record in delivery and operation of large-scale projects.
	10. Which type of outsourcing fits best your company's needs? (and why)
	• Able to utilize the best technology. • A vendor able to build a good team and be good at communications. • If they can apply themselves intelligently and support our objectives, then the type of outsourcing contract will be of secondary importance.
	11. How is outsourcing affecting your industry? (Effect on growth? Profitability?)
	• Outsourcing is already established and successful. • The nature of the product is changing more towards E-Business and Call Centre technology. • A quick response to new requirements and greater emphasis on managing the relationship. • If vendors can offer practical and sustainable business improvement, then their future looks reasonably secure.
	12. How has your attitude toward IT outsourcing changed over the past year?
	We are now looking for a partnership on the latest technologies and software solution as opposed to just getting a "low-cost" service.
	13. Are you as attracted by outsourcing entire business processes as by off-loading commodity transaction processing?
	Yes, but with the effective management of risk and how it will impact on our vision and business strategy.
	20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?
	We prefer a recognized and credible company, but stay clear of the major names because of cost.
CYBERGRAPHICS	
	2. What is your role?
	Overall responsibility for business processes
	3. Please indicate the nature of your experience with outsourcing (IT or otherwise).
	Senior part of the selection team.
	4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)
	No preference
	5. To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?
	Use consultants for special projects.
	6. How do you determine which outsourcing vendors to invite to bid?
	We normally select two vendors for shortlist. After that we consider technical merit and business acumen (and how they demonstrate their expertise)
	7. How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?
	Wouldn't matter.
	8. How important is the outsourcer' ability to attract and acquire your targeted staff (as part of a proposed contract)?
	Not an issue

	9. What important changes do you see at work in the outsourcing market today?
	• The workplace has become more mobile with advanced communications and the use of WAP. Therefore, your own IT staff does not need to be resident in-house. • I don't know if this will increase or decrease the use of outsourcing long term. • Also, there is an increased trend towards the use of Offshore service providers.
	10. Which type of outsourcing fits best your company's needs? (and why)
	IT and business consultancy, project management. We provide the resources but the outsourcing company manages them.
	11. How is outsourcing affecting your industry? (Effect on growth? Profitability?)
	Mainly in systems development and training.
	12. How has your attitude toward IT outsourcing changed over the past year?
	Not really.
	13. Are you as attracted by outsourcing entire business processes as by off-loading commodity transaction processing?
	No
	14. Have you computed the contribution made by outsourcing to your company's overall profitability? (To cost-reduction of IT depart?)
	No
	15. Do you prefer longer or shorter contract durations? (Why?)
	Shorter contracts
	16. Have you in mind a ranking regarding which types of outsourcing are the most costly? (Reasons?)
	You have a feel through experience. Data center and transactions-based outsourcing is getting less expensive. Consultancy, BPO, custom development is (or has been) increasing over the last 10 years. Some specific skills such as Oracle, SAP, Java, Active X are extortionate.
	17. In relation to outsourcing, how sensitive are you to the issue of control, in general, and control of proprietary data in particular?
	Very sensitive.
	18. How strong is your relationship with incumbent outsourcers? (Probability of sole-sourcing new contracts?)
	No responses.
	19. To what extent, if any, have union relations affected your desire or ability to outsource?
	None
	20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?
	No real influence. They must demonstrate technical ability and have track record.
MONTEFIORE MEDICAL	
	2. What is your role?
	IT Director
	3. Please indicate the nature of your experience with outsourcing (IT or otherwise).
	Recently handled the outsourced implementation of SAP.
	4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)
	Yes, but must be fixed price contracts.

	5. To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?
	• Not the objective of outsourcing for us. • It was the speed of actioning things – we needed to implement SAP "soup to nuts" and increase software development speed and quality.
	6. How do you determine which outsourcing vendors to invite to bid?
	We have a shortlist including people that we have worked with in the past. They submit their proposal and we look for the best fit.
	7. How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?
	Not a problem
	8. How important is the outsourcer' ability to attract and acquire your targeted staff (as part of a proposed contract)?
	Not important
	9. What important changes do you see at work in the outsourcing market today?
	More companies are now outsourcing. Also the variety and choice of what can be outsourced has changed.
	10. Which type of outsourcing fits best your company's needs? (and why)
	Small, defined projects.
	11. How is outsourcing affecting your industry? (Effect on growth? Profitability?)
	No response
	12. How has your attitude toward IT outsourcing changed over the past year?
	No
	13. Are you as attracted by outsourcing entire business processes as by off-loading commodity transaction processing?
	No
	14. Have you computed the contribution made by outsourcing to your company's overall profitability? (To cost-reduction of IT depart?)
	We obtained a high value economic return in terms of implementing a very sophisticated system. The benefits will be obtained internally (in that the wider implications would have been considerable, had we not outsourced it).
	15. Do you prefer longer or shorter contract durations? (Why?)
	Shorter contracts. Cost and control are the main reasons.
	16. Have you in mind a ranking regarding which types of outsourcing are the most costly? (Reasons?)
	No response.
	17. In relation to outsourcing, how sensitive are you to the issue of control, in general, and control of proprietary data in particular?
	None beyond what you would have in any other IT application service contract.
	18. How strong is your relationship with incumbent outsourcers? (Probability of sole-sourcing new contracts?)
	Good
	19. To what extent, if any, have union relations affected your desire or ability to outsource?
	None

	20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?
	• It would have some bearing in that you feel safer with the bigger companies. • It did influence us in that we wanted to use a SAP Logo Partner, which tend to be the large IT service providers and consultancies.
Dr Pepper / 7 Up	
	2. What is your role?
	Respondent is a senior VP for IT with broad experience in outsourcing.
	3. Please indicate the nature of your experience with outsourcing (IT or otherwise).
	Currently, respondent is managing three major outsourcing contracts for the company: 1. A large application management contract with CSC for SAP support on company-owned HW, using company-owned SW license. The contract is now in its third year of a five-year contract and DPSU is very satisfied with vendor performance. 2. "MIPS on Tap," a pay-as-you-go agreement with a Managed Service Provider that offers access to vendor-owned mainframes. The contract provides scaleable, flexible and cost-effective access to mainframes on an as-needed basis, obviating the need for any related capital outlay or maintenance expense. Respondent likes the ability to a fixed monthly fee with pre-determined surcharges for higher levels of usage. The vendor is Interactive Systems, Inc. of Arlington, VA [ISI]. 3. A help desk / desktop services / call center contract with Synergy for services, staffing and HW procurement. Services are provided on-site at DPSU on company-owned equipment. DPSU is very satisfied with vendor performance.
	4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)
	Respondent does NOT prefer "bundled" OS contracts because, • He does not believe that any one vendor can do everything equally well, and • He wants to buy best-of-breed applications and services. • He is willing to serve as his own IT "general contractor" to manage relationships between vendors.
	5. To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?
	Regarding motives for outsourcing and use of company capital, respondent said that the company's goal is to offload insofar as possible all routine IT work to vendors so that internal staff can be free to work on high value-added, proprietary SW projects.
	6. How do you determine which outsourcing vendors to invite to bid?
	All DPSU outsourcing contracts have been competitively sourced based on bids from 3-4 vendors. Respondent used a "discovery process" to determine which vendors to invite to bid. That required company research to determine which were the most outstanding vendors active in the market for each type of work required. He did NOT use consultants because respondent felt prepared, based on prior experience, to deal with vendors directly. He hed a model in hand to use as a point of departure to discuss the projects out to bid. In the case of CSC, the company had done prior work for DPSU and the company had been very satisfied with the vendor's performance. As for Synergy, the vendor is in its fourth year of work for DPSU. It had been brought to DPSU as a subcontractor by a previous prime. When that project didn't materialize, Synergy proposed working for DPSU as a prime on the current project, and its proposal was accepted.
	7. How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?
	When asked if we have (or will) consider inviting to bid a vendor whose experience had been entirely in the federal market, respondent said that the key criterion would be how "reference-able" the vendor's clients were. He clarified that, for "horizontal" applications, such as HP, billing, etc., he saw no particular need for a vendor to have any significant vertical industry expertise. On the

	other hand, he would not entrust an IT project, such as software application development ("vertical") for a consumer industry sales initiative to a vendor that lacked deep experience in the consumer product/beverage industry. Respondent acknowledged that vendors competing in the "horizontal" applications market were facing fierce competition and difficulty in differentiating themselves from the crowd.
	8. How important is the outsourcer' ability to attract and acquire your targeted staff (as part of a proposed contract)?
	According to respondent, CSC's ability to attract and manage successfully an important group of DPSU staff to work for the outsourcing vendor was critical to the success of the proposal and the contract. DPSU wanted to reduce headcount, but did not want to lose the accumulated knowledge of this pool of experienced workers. As turned out, CSC was able to attract and retain this staff by offering them superior opportunities for professional advancement, while at the same time making available to DPSU a very large pool of experts that DPSU would never have been able to attract for an in-house position. Respondent clarified that, if for any reason CSC as the incumbent needed to be replaced in the future, DPSU would take care either to transfer this experienced team to a new vendor, or to bring them back in-house as full-time DPSU employees. During the original contract competition, it was very important to DPSU to select a vendor that had a good reputation for, and demonstrated success absorbing customer staff as part of an outsourcing project.
	9. What important changes do you see at work in the outsourcing market today?
	• Respondent believes that there are three important trends at work today in the outsourcing field: • Both outsourcing providers and customers are much better educated than they were in the past. • Contract models are more sophisticated. • ASP model is becoming increasingly attractive; this market is likely to expand. • For example, DPSU is willing to use ASPs for horizontel applications, or even for SAP work, but company was unlikely to use an ASP for Web development work. Reason: ASP model is inappropriate for work that needs to be highly customized. It is, by nature, a model for delivery of standard, low-cost applications that can be used and re-used by many companies.
	10. Which type of outsourcing fits best your company's needs? (and why)
	11. How is outsourcing affecting your industry? (Effect on growth? Profitability?)
	Effect of Outsourcing on Consumer Industry The beverage industry has grown typically through acquisitions—mainly by acquiring rival brands. Outsourcers are expediting the process by facilitating the integration of dissimilar IT infrastructures. The IT business differs from the process manufacturing business. The bridge could provide increasing opportunity for BPO vendors able to take over responsibility for manufacturing operations (including IT) while leaving the marketing function to the customer (for example, as the result of an an acquisition). While customers still look to outsourcing as a way to lower specific costs, they no longer expect outsourcing to lower their level of total IT spending. What customers gain in greater flexibility, especially the ability to re-deploy in-house resources on higher-value-added project work that is inherently proprietary. Also, there is no question but that customers are attracted to outsourcers due to the IT skills shortage. This may be less of a problem at present, but it has certainly been a factor in the past and was a key driver of outsourcing initiatives. Respondent summarized this point by saying simply, "CSC becomes an HR machine that feeds [us] staff." In his opinion, CSC's core competency is not technical, it is the ability to provide people to the IT industry.
	12. How has your attitude toward IT outsourcing changed over the past year?
	No response

	13. Are you as attracted by outsourcing entire business processes as by off-loading commodity transaction processing?
	No response
	14. Have you computed the contribution made by outsourcing to your company's overall profitability? (To cost-reduction of IT depart?)
	Yes. DPSU has operating budget objectives and annual targets. Respondent's experience with outsourcing to date has been that vendors have enabled DPSU to exceed its budget targets even while coping with an increasing workload. This was particularly impressive because the original budget targets had been built on aggressive estimates of cost-savings.
	15. Do you prefer longer or shorter contract durations? (Why?)
	No response
	16. Have you in mind a ranking regarding which types of outsourcing are the most costly? (Reasons?)
	Types of Outsourcing and Cost When asked which types of outsourcing services were most expensive to the customer to obtain, respondent gave the following ranking from "most" to "least" expensive. 1. Strategic systems development, applications development and maintenance. 2. ASP model, managed services 3. Help desk, call center, desktop services. These require less skill AND supply exceeds demand. (DPSU prefers on-site provision of services rather than remote.)
	17. In relation to outsourcing, how sensitive are you to the issue of control, in general, and control of proprietary data in particular?
	No response
	18. How strong is your relationship with incumbent outsourcers? (Probability of sole-sourcing new contracts?)
	No response
	19. To what extent, if any, have union relations affected your desire or ability to outsource?
	No response
	20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?
	No response

Exhibit D-4

Tabulation of User Interview Survey Responses by Question

Companies with Experience in IT Outsourcing	
2. What is your role?	
Montefiore Medical	IT Director
Cyber-graphics	Overall responsibility for business processes
Morgan Driveway, Inc	Manager of all IT
Amphenol	Responsible for all custom development and integration services
Rochester Democrat & Chronicle	VP-IS
Omega Financial	IT Manager
American Crystal Sugar Company	IS Director
Garden Way, Inc	IS Development Manager
Hologic, Inc	Overall director of all IT
Eaton Corp	Overall IS responsibility
Dr Pepper / 7 Up	Respondent is a senior VP for IT with broad experience in outsourcing.
3. Please indicate the nature of your experience with outsourcing (IT or otherwise).	
Montefiore Medical	Recently handled the outsourced implementation of SAP.
Cyber-graphics	Senior part of the selection team.
Morgan Driveway, Inc	Senior role in all outsourced IT programs.
Amphenol	Have placed (awarded) many contracts. Also spent many years as project manager on large-scale outsourcing contracts.
Rochester Democrat & Chronicle	I call "all the shots".
Omega Financial	Extensive. Have been involved in outsourcing for at least 10 years.
American Crystal Sugar Company	Main decision-maker in all major IT decisions.
Garden Way, Inc	I have final decision on all outsourcing (customized and otherwise).
Hologic, Inc	Have been involved in several outsourcing arrangements in many mixed environments
Eaton Corp	Varied, used extensively for development and ERP work. Some e-business, Website design and some related development.

DR PEPPER / 7 UP	Currently, respondent is managing three major outsourcing contracts for the company: 1. A large application management contract with CSC for SAP support on company-owned HW, using company-owned SW license. The contract is now in its third year of a five-year contract and DPSU is very satisfied with vendor performance. 2. "MIPS on Tap," a pay-as-you-go agreement with a Managed Service Provider that offers access to vendor-owned mainframes. The contract provides scaleable, flexible and cost-effective access to mainframes on an as-needed basis, obviating the need for any related capital outlay or maintenance expense. Respondent likes the ability to a fixed monthly fee with pre-determined surcharges for higher levels of usage. The vendor is Interactive Systems, Inc. of Arlington, VA [ISI]. 3. A help desk / desktop services / call center contract with Synergy for services, staffing and HW procurement. Services are provided on-site at DPSU on company-owned equipment. DPSU is very satisfied with vendor performance.
4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)	
Montefiore Medical	Yes, but must be fixed price contracts.
Cyber-graphics	No preference
Morgan Driveway, Inc	• Large development programs in place (and planned). • There are presumed cost advantages in bundling the services, but it can be difficult to achieve a consistent level of operational service. • We need to ensure that our commitments are met. The vendor supplying development services is not necessarily the best vendor to operate the Data Center.
Amphenol	No preference. The contract will reflect the service program that needs to be outsourced. Contracts can have different durations and termination dates, so even if we wanted to bundle them, sometimes it is not logistically possible.
Rochester Democrat & Chronicle	Prefer bundled contracts, due to the cost ratio.
Omega Financial	Yes, we can leverage the price.
American Crystal Sugar Company	We end up with a balance. We had a policy to widen the supplier base and to bring in a greater level of knowledge and expertise. Better commercial advantages in not bundling the contract
Garden Way, Inc	Bundled. We manage all our outsourcing through KPMG.
Hologic, Inc	In an ideal world, we would go with as much bundled as possible. We have a large contract with ADP, but we still have the need to place 2-3 other individual contracts with other service vendors
Eaton Corp	No, we prefer to award specific contracts for a discrete piece of work.
Dr Pepper / 7 Up	Respondent does NOT prefer "bundled" OS contracts because, • He does not believe that any one vendor can do everything equally well, and • He wants to buy best-of-breed applications and services. • He is willing to serve as his own IT "general contractor" to manage relationships between vendors.
5. To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?	
Montefiore Medical	Not the objective of outsourcing for us. It was the speed of actioning things – we needed to implement SAP "soup to nuts" and increase software development speed and quality.
Cyber-graphics	Use consultants for special projects.
Morgan	We have no expertise or business knowledge of e-commerce (which is our most recent

Driveway, Inc	project). Different programs are outsourced for differing reasons, ie, access to expertise is scarce, reduce the cost of delivery service, implementing corporate intranet, etc, but I suppose the bottom line is that the cost advantage must be prominent.
Amphenol	In the early days, outsourcing was done for commercial considerations. Nowadays, we have more sophisticated reasons--specific projects, core or scarce skills.
Omega Financial	Where we cannot keep talented people fully employed
American Crystal Sugar Company	Better service and support. Improved staff usage and utilization. Well suited to development and custom projects. Relieve the workload to the existing IT team.
Garden Way, Inc	Originally to reduce our headcount and look at ways of reducing our cost base. Laterally we are now looking for expertise in specific disciplines and to improve development performance. To improve the key components and business functionality. While we want KPMG to provide better service, we also want them to be more customer focused.
Hologic, Inc	The primary reasons were that we had a mixed environment of DEC/Compaq, Solaris and Unisys. Control of this became very difficult and cumbersome, so we started to outsource different elements of this. We did have the objective to reduce the main overhead of the service cost and to be able to complete other (new) IT projects faster.
Eaton Corp	Recoverable costs from departmental budgets.
Dr Pepper / 7 Up	Regarding motives for outsourcing and use of company capital, respondent said that the company's goal is to offload insofar as possible all routine IT work to vendors so that internal staff can be free to work on high value-added, proprietary SW projects.
	6. How do you determine which outsourcing vendors to invite to bid?
Montefiore Medical	We have a shortlist including people that we have worked with in the past. They submit their proposal and we look for the best fit.
Cyber-graphics	We normally select two vendors for shortlist. After that we consider technical merit and business acumen (and how they demonstrate their expertise)
Morgan Driveway, Inc	The usual criteria of relevant experience, quality of work, proven in field and familiar with our technology.
Amphenol	Technical ability, reputation, "chemistry".
Rochester Democrat & Chronicle	They need experience of front-end systems and vast exposure to the newspaper industry.
Omega Financial	We merged with another bank, so we are jointly using the incumbent supplier. However, we are seeking due diligence for the next contract award.
American Crystal Sugar Company	• Cost • Quality of company and their people. • Team building and management. • To manage the applications through development testing and production. • Able to meet demanding delivery requirements. • Process functional and technical skill sets.
Garden Way, Inc	We always use KPMG as our principle partner who will manage the overall contracts. There are about 20 other organizations that we define and from which we source the operational services, but the contract is planned and managed by KPMG. Single-source contract for urgency and proprietary systems support.

Hologic, Inc	• Proven record, expertise. Must be a solution provider. Knowledgeable in our application types and operating environment. Proven success on similar types of outsourcing projects. • Expertise in Web-enabled financial software.
Eaton Corp	• We work from an existing list of preferred (known) vendors to which we add and remove. • Generally an outsourcing contract is awarded to a company with which we have an already established relationship.
Dr Pepper / 7 Up	• All DPSU outsourcing contracts have been compatitively sourced based on bids from 3-4 vendors. Respondent used a "discovery process" to determine which vendors to invite to bid. That required company research to determine which were the most outstanding vendors active in the market for each type of work required. • He did NOT use consultants because respondent felt prepared, based on prior experience, to deal with vendors directly. He had a model in hand to use as a point of departure to discuss the projects out to bid. • In the case of CSC, the company had done prior work for DPSU and the company had been very satisfied with the vendor's performance. As for Synergy, the vendor is in its fourth year of work for DPSU. It had been brought to DPSU as a subcontractor by a previous prime. When that project didn't materialize, Synergy proposed working for DPSU as a prime on the current project, and its proposal was accepted.
7. How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?	
Montefiore Medical	Not a problem
Cyber-graphics	Wouldn't matter.
Morgan Driveway, Inc	Not a problem per se. But they would have to meet our criteria in terms of project management experience, able to develop Web business applications and B2B consultancy skills. I guess that I would not want to be their FIRST customer.
Amphenol	Would not bother me. We have a lot of contracts with government bodies, so we are fairly competent in this area.
Rochester Democrat & Chronicle	I would not be unreceptive, but they would need to have considerable experience of our industry (otherwise we would not get seriously involved with them)
Omega Financial	Not a problem, providing the other requirements were met.
American Crystal Sugar Company	"Give me a name". In a hypothetical situation, I would say that if the vendor possess quality, service and speed in implementing a quality standardization program, then federal-only experience should not be an issue. One or two large federal contracts can allow an organization to grow very rapidly. Companies like EDS were very heavily involved in federal contracts and it didn't really prevent the company from moving into the commercial market.
Garden Way, Inc	I would have my doubts, not really decided yet.
Hologic, Inc	In theory it would not prevent us. Our current situation is that we have contracts to be outsourced. We want to remove that responsibility from us to a partner vendor to allow the vendor and ourselves to focus on our technical strengths.
Eaton Corp	Not really applicable. They would have to meet the criteria (as per Q6)

Dr Pepper / 7 Up	When asked if we have (or will) consider inviting to bid a vendor whose experience had been entirely in the federal market, respondent said that the key criterion would be how "reference-able" the vendor's clients were. He clarified that, for "horizontal" applications, such as HP, billing, etc., he saw no particular need for a vendor to have any significant vertical industry expertise. On the other hand, he would not entrust an IT project, such as software application development ("vertical") for a consumer industry sales initiative to a vendor that lacked deep experience in the consumer product/beverage industry. Respondent acknowledged that vendors competing in the "horizontal" applications market were facing fierce competition and difficulty in differentiating themselves from the crowd.
8. How important is the outsourcer' ability to attract and acquire your targeted staff (as part of a proposed contract)?	
Montefiore Medical	Not important
Cyber-graphics	Not an issue
Morgan Driveway, Inc	They would be required to manage our contractors plus recruit new skills. Transfer of existing staff to the outsourcing company would be subject to discussion.
Amphenol	Not important at present
Rochester Democrat & Chronicle	Hasn't happened yet; would put it down as unimportant at present.
Omega Financial	Have had a delicate situation in the past that was resolved, but it is something that we need to be careful about. Existing staff working for a large financial services company would not be too keen to move to a smaller IT services company.
American Crystal Sugar Company	If we do not went to continue with a large in-house IT resource, then the supplier must fulfil that role.
Garden Way, Inc	Not important.
Hologic, Inc	Important in that they manage the human resources. We had problems in recruitment and retention of staff, so this is an essential part of the project.
Eaton Corp	Not really important. We tend to outsource contracts when we lack sufficient internal resources. Our in-house staff either assists these contracts in secondary role, or is assigned a new piece of work (totally unrelated). Transfer of staff has not occurred to date.
Dr Pepper / 7 Up	According to respondent, CSC's ability to attract and manage successfully an important group of DPSU staff to work for the outsourcing vendor was critical to the success of the proposal and the contract. DPSU wanted to reduce headcount, but did not want to lose the accumulated knowledge of this pool of experienced workers. As turned out, CSC was able to attract and retain this staff by offering them superior opportunities for professional advancement, while at the same time making available to DPSU a very large pool of experts that DPSU would never have been able to attract for an in-house position. Respondent clarified that, if for any reason CSC as the incumbent needed to be replaced in the future, DPSU would take care either to transfer this experienced team to a new vendor, or to bring them back in-house as full-time DPSU employees. During the original contract competition, it was very important to DPSU to select a vendor what had a good reputation for, and demonstrated success absorbing customer staff as part of an outsourcing project.
9. What important changes do you see at work in the outsourcing market today?	
Montefiore Medical	More companies are now outsourcing. Also the variety and choice of what can be outsourced has changed.

Cyber-graphics	The workplace has become more mobile with advanced communications and the use of WAP. Therefore, your own IT staff does not need to be resident in-house. I don't know if this will increase or decrease the use of outsourcing long term. Also, there is an increased trend towards the use of Offshore service providers.
Morgan Driveway, Inc	New philosophy of achieving excellence. Vendors now have a proven track record in delivery and operation of large-scale projects.
Amphenol	I would see over the longer term more of our IT coming back in-house.
Rochester Democrat & Chronicle	Much larger stable nowadays. Greater choice of vendors, more experience, more extensive knowledge and also a great deal more business process outsourcing than ever before.
Omega Financial	Banking is changing. It now encompasses a full range of services including insurance, stockbroking, etc,. We need an outsourcing company to take us into the future. We need improved service at lower cost.
American Crystal Sugar Company	• Must show tangible improvements. • Facility to increase communication. • Commitment to achieving specific goals. • Support the complete process and shape the business model.
Garden Way, Inc	More procurement via the Internet. Big changes in the variety and type of service; allows expansion into other areas. Greater professionalism.
Hologic, Inc	Some services are easier to contract out now. Operational duties are spreading into new IT areas especially CRM. Outsourcing is now an acceptable process and customers are more intuitive.
Eaton Corp	More selective. The market is becoming more discrete, with organizations having greater specialization. I think that there is a decrease in the "larger all-encompassing" projects. User companies lack some of the management tools internally, the vendor must proactively manage the customer (as well as the project). Outsourcing is moving away from maintenance of products and support of users towards working on new architecture and solution development.
Dr Pepper / 7 Up	Respondent believes that there are three important trends at work today in the outsourcing field: • Both outsourcing providers and customers are much better educated than they were in the past. • Contract models are more sophisticated. • ASP model is becoming increasingly attractive; this market is likely to expand. • For example, DPSU is willing to use ASPs for horizontal applications, or even for SAP work, but company wa unlikely to use an ASP for Web development work. Reason: ASP model is inappropriate for work that needs to be highly customized. It is, by nature, a model for delivery of standard, low-cost applications that can be used and re-used by many companies.
10. Which type of outsourcing fits best your company's needs? (and why)	
Montefiore Medical	Small, defined projects.
Cyber-graphics	IT and business consultancy, project management. We provide the resources but the outsourcing company manages them.
Morgan Driveway, Inc	• Able to utilize the best technology. • A vendor able to build a good team and be good at communications. • If they can apply themselves intelligently and support our objectives, then the type of outsourcing contract will be of secondary importance.

Amphenol	Smaller development and maintenance contracts with 12 months duration.
Rochester Democrat & Chronicle	The type of contract is secondary to obtaining the correct skill fit. If we get the right vendor with exactly the right type of skills and service offering, we would ask them to propose alternative contract solutions to us.
Omega Financial	• Facilities Management and procurement. • An efficient service that works 24 hours a day, able to improve business processes all round.
American Crystal Sugar Company	• That by which we can better satisfy our customers and users. • We went to strengthen the team at operational level and oversee the technical side of the legacy projects. • Support of the wider business units
Garden Way, Inc	An application management and support role for ERP. Answer to our skill shortages; can be the most practical solution.
Hologic, Inc	Support for specialist software packages, project management, BPR. All e-business services and internet integration.
Eaton Corp	Smaller independent companies that provide specific services. Help desk, Internet Web services, production of documentation, training, raw coding and programming. Not purely a support arrangement; they need to provide stability in an older operating environment.
11. How is outsourcing affecting your industry? (Effect on growth? Profitability?)	
Cyber-graphics	Mainly in systems development and training.
Morgan Driveway, Inc	• Outsourcing is already established and successful. • The nature of the product is changing more towards E-Business and Call Centre technology. • A quick response to new requirements and greater emphasis on managing the relationship. • If vendors can offer practical and sustainable business improvement, than their future looks reasonably secure.
Amphenol	• If outsourcing is applied well, the results are positive and lead to improved profitability. • The problem seems to be thet it can be very difficult to objectively assess the impact of outsourcing. • For instance, if we reduce headcount by a factor of X (as a result of the outsourcing), could we not have just reduced the number of staff anyway. • If we increased profitability, how do we know that outsourcing had anything to do with it.
Omega Financial	Not measurable.
American Crystal Sugar Company	I think thet we have achieved: Improved service levels to users. Enhanced the level of support Provided control and improved quality. From a commercial point of view, we have reduced operating costs whilst experiencing very tough trading conditions.
Garden Way, Inc	Improved efficiency on the supply chain. Faster and cheaper to get our applications and services up and running.
Hologic, Inc	The skills are available, but the costs are very high. A high proportion of our overall IT budget now goes to external contracts. We have definitely seen a reduction in capital and recurring costs. Outsourcing has allowed us to stay ahead competitively byincreasing the time scales to develop new applications.
Eaton Corp	Not measurable in commercial business terms. Outsourcing is an essential link with our in-house technical delivery teams.

	We have improved time scales for on-going development and achieved better quality at a reasonable cost.
Dr Pepper / 7 Up	*Effect of Outsourcing on Consumer Industry* • The beverage industry has grown typically through acquisitions—mainly by acquiring rival brands. Outsourcers are expediting the process by facilitating the integration of dissimilar IT infrastructures. • The IT business differs from the process manufacturing business. The bridge could provide increasing opportunity for BPO vendors able to take over responsibility for manufacturing operations (including IT) while leaving the marketing function to the customer (for example, as the result of an an acquisition). • While customers still look to outsourcing as a way to lower specific costs, they no longer expect outsourcing to lower their level of total IT spending. What customers gain in greater flexibility, especially the ability to re-deploy in-house resources on higher-value-added project work that is inherently proprietary. • Also, there is no question but that customers are attracted to outsourcers due to the IT skills shortage. This may be less of a problem at present, but it has certainly been a factor in the past and was a key driver of outsourcing initiativas. • Respondent summarized this point by saying simply, "CSC becomes an HR machine that feeds [us] staff." In his opinion, CSC's core competency is not technical, it is the ability to provide people to the IT industry.
12. How has your attitude toward IT outsourcing changed over the past year?	
Montefiore Medical	No
Cyber-graphics	Not really.
Morgan Driveway, Inc	We are now looking for a partnership on the latest technologies and software solution as opposed to just getting a "low-cost" service.
Amphenol	No, perhaps I am slightly more cynical. I certainly expect a lot more from the vendor, added-value is a must!!!!
Rochester Democrat & Chronicle	I am more relaxed about outsourcing.
Omega Financial	Still receptive to OS.
American Crystal Sugar Company	More confident in design and reviewing operational models. Processing and operational control have improved considerably. Account management is easier to control and manage.
Garden Way, Inc	More positive; allows staff more time for other applications. Lead times for service have improved, greater responsiveness from the vendor leading to greater satisfaction all round.
Hologic, Inc	Inertia towards external service suppliers in some circles; thoughts are that we will obtain a better return on IT using in-house staff. Even though there is a general shortage of key skills; the service vendors don't necessarily have the skills either.
Eaton Corp	Little. We are committed to a business transformation program and outsourcing is part of that building block for the future.
13. Are you as attracted by outsourcing entire business processes as by off-loading commodity transaction processing?	
Montefiore Medical	No
Cyber-graphics	No
Morgan Driveway, Inc	Yes, but with the effective management of risk and how it will impact on our vision and business strategy.
Amphenol	No, as per Q10

Rochester Democrat & Chronicle	Yes, if we can see that there are real beneficial gains for us.
Omega Financial	Yes.
American Crystal Sugar Company	We have very ambitious plans and want to be able to move forward much faster. We are aware of the wider capabilities (of entire outsourcing), it will make us internally more effective and improve those internal processes. It could eliminate major integration issues further down the line.
Garden Way, Inc	YES
Hologic, Inc	Only if they can provide added value for enhancement and support. Improvements in change are usually never achieved. Trying to combine external and internal resources (as present) can be very difficult, but outsourcing the entire IT and business processes would be a massive decision.
Eaton Corp	Not at all. Our policy towards outsourcing is (as per Q10)
14. Have you computed the contribution made by outsourcing to your company's overall profitability? (To cost-reduction of IT depart?)	
Montefiore Medical	We obtained a high value economic return in terms of implementing a very sophisticated system. The benefits will be obtained internally (in that the wider implications would have been considerable, had we not outsourced it).
Cyber-graphics	No
Amphenol	No
Rochester Democrat & Chronicle	No model as such, but costs come from the overall IT budget.
Omega Financial	Overseen by our auditors. Specific cost reductions in operational overheads have been achieved; lower support and operational costs on the longer term.
American Crystal Sugar Company	• Improved customer satisfaction – overall pleasing. • IT expertise at a cheaper price than it would take us to maintain personnel in-house. • Able to monitor and evaluate specific "hard success" criteria. Creation of brand awareness and loyalty. Superior levels of customer services.
Garden Way, Inc	Yes. We have seen the benefits of joint ventures and strategic alliances; both parties share costs and resources.
Hologic, Inc	Ultimately, the measurement has got to be reflected in the success of the business generation. Lower operating costs, greater turnover, numbers of increased transactions; do you ever know the real story????? It depends on the business model that is being adopted.
Eaton Corp	We have been able to reduce our internal headcount and not have to increase new-skill recruitment. We have also been able to better control the overall IT overhead and budget. We are maximizing the returns on our original IT investment; bringing operational benefits to the company.
Dr Pepper / 7 Up	Yes. DPSU has operating budget objectives and annual targets. Respondent's experience with outsourcing to date has been that vendors have enabled DPSU to exceed its budget targets even while coping with an increasing workload. This was particularly impressive because the original budget targets had been built on aggressive estimates of cost-savings.
15. Do you prefer longer or shorter contract durations? (Why?)	
Montefiore Medical	Shorter contracts. Cost and control are the main reasons.
Cyber-graphics	Shorter contracts

Amphenol	Short contracts of about 12 months
Rochester Democrat & Chronicle	Shorter contracts carry less risk to us. Fewer things can go wrong.
Omega Financial	5-yr contracts
American Crystal Sugar Company	Through our legal dept.
Garden Way, Inc	• Shorter contracts are easier to control and manage. • They also keep costs down as more regular contract renewals maintain a more competitive environment. • In longer contracts, vendors have a greater opportunity to "milk you" for higher prices.
Hologic, Inc	As long as they are on time and within budget.
Eaton Corp	Our contracts have always tended to be short and we don't see this changing.
16. Have you in mind a ranking regarding which types of outsourcing are the most costly? (Reasons?)	
Cyber-graphics	• You have a feel through experience. Data center and transactions-based outsourcing is getting less expensive. • Consultancy, BPO, custom development is (or has been) increasing over the last 10 years. • Some specific skills such as Oracle, SAP, Java, Active X are extortionate.
Amphenol	No
Omega Financial	Yes, only through experience.
American Crystal Sugar Company	Performance improvement – reducing costs and improving service.
Garden Way, Inc	Would give a lot of thought to ERP contracts costing >$2 million
Hologic, Inc	• Using external resources doesn't necessarily improve costings, it merely moves them from one business unit to another. • Mainstream support of MVS and UNIX systems • Technology integration with requirement for special technical disciplines. • Bespoke [customized] applications running on AS/400s.
Eaton Corp	No
Dr Pepper / 7 Up	*Types of Outsourcing and Cost* When asked which types of outsourcing services were most expensive to the customer to obtain, respondent gave the following ranking from "most" to "least" expensive. 1. Strategic systems development, applications development and maintenance. 2. ASP model, managed services 3. Help desk, call center, desktop services. These require less skill AND supply exceeds demand. (DPSU prefers on-site provision of services rather than remote.)
17. In relation to outsourcing, how sensitive are you to the issue of control, in general, and control of proprietary data in particular?	
Montefiore Medical	None beyond what you would have in any other IT application service contract.
Cyber-graphics	Very sensitive
Amphenol	Nothing sensitive here

Rochester Democrat & Chronicle	• Not too big a problem. • Obviously the vendor will sign confidentiality clauses. • The concept of partnership is very important to us and we would never enter into a relationship with a supplier if mutual trust did not exist.
Omega Financial	Not sensitive. Have a 3rd party for control and security.
American Crystal Sugar Company	Undergoing a re-think about this. We don't want to force through unpopular policies, but we need to protect our intellectual interests.
Garden Way, Inc	Very sensitive about the manufacturing process – would not want this to go externally.
Hologic, Inc	We introduced our own best practice.
Eaton Corp	Very sensitive.
18. How strong is your relationship with incumbent outsourcers? (Probability of sole-sourcing new contracts?)	
Montefiore Medical	Good
Amphenol	Current relationships are good.
Rochester Democrat & Chronicle	Good, as per Q17
Omega Financial	Very good.
American Crystal Sugar Company	Reasonably good teams who meet most of our criteria. Ambiguity is always the big problem.
Garden Way, Inc	Good
Hologic, Inc	Service suppliers lack the understanding of fostering relationships; they are driven by short-term objectives. There is always a perceived conflict, but we have better control of the resources that support our organization.
Eaton Corp	Relationship is good. We always have prior working knowledge and exposure with the vendor, so our risk is minimized.
19. To what extent, if any, have union relations affected your desire or ability to outsource?	
Montefiore Medical	None
Cyber-graphics	None
Amphenol	Not at all.
Rochester Democrat & Chronicle	Not a problem
Omega Financial	No effect
American Crystal Sugar Company	Not really from unions, but existing staff want some form of contractual obligation (in relation to secure employment)
Garden Way, Inc	None, we are a nonunion shop
Hologic, Inc	Discussions with the unions to keep jobs in-house. They are selling the long-term benefit of keeping expertise internally.
Eaton Corp	Not an issue.

20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?	
Montefiore Medical	It would have some bearing in that you feel safer with the bigger companies. It did influence us in that we wanted to use a SAP Logo Partner, which tend to be the large IT service providers and consultancies.
Cyber-graphics	No real influence. They must demonstrate technical ability and have track record.
Morgan Driveway, Inc	We prefer a recognized and credible company, but stay clear of the major names because of cost.
Amphenol	Tend to use smaller local companies that are cheaper and keener.
Rochester Democrat & Chronicle	In some ways experience has shown us that the bigger the company, the more expensive the cost. However, they would argue that the bigger the supplier, the less the risk is to the customer.
Omega Financial	Is a factor, but decisions are "horses for courses." If your volume of business is such that it represents a disproportionately high % of the vendor's revenue, then this could be a problem in terms of risk and exposure.
American Crystal Sugar Company	Always in the "hidden" agenda. No customer is ever going to say "we will only award this contract to a large company," but--in reality--this is commonplace.
Garden Way, Inc	Great influence, size and longevity are important.
Hologic, Inc	It does influence you if the contract has significant $ value, or it is critical to the strategy.
Eaton Corp	Doesn't really bother us. We tend to avoid the large players as we get better service from smaller companies.

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D

Appendix

A
Operational Services Market Forecast Summary

Following is a summary of INPUT's operational services U.S. market forecast for the period 2000-2005.

Exhibit D-1 presents detailed outsourcing market forecasts. Annotations follow.

Exhibit D-1

U.S. Operational Services Market, 2000-2005

	Market Forecast (U.S. $ Billions)				
	1999	Growth 1999-2000 (%)	2000	Growth 2000-2005 (%)	2005
U.S. Market for Operational Services					
IT Outsourcing	40.0	*19*	47.7	*19*	115.9
Business Process Operations	9.6	*30*	12.5	*29*	45.0
Processing Services	42.2	*14*	48.1	*15*	98.8
Total Operational Services	**91.8**	***18***	**108.3**	***19***	**259.7**

Source: INPUT

Annotations:

- "Infrastructure Services" is being used for the first time in this forecast report as a replacement for the prior term "Platform Operations," which becomes one of two components of the Infrastructure Services market. This market has been divided this year into traditional, mainframe-oriented platform operations and the faster-growing, "Internet/Web Managed Services" sub-segment. The inflection point between these two market segments will occur in 2005, at which time Internet/Web Managed Services segment is expected to be larger than the legacy IT Platform Operations segment. Toward the end of the forecast period, a price/performance curve effect will result in lower levels of spending purchasing ever higher levels of performance.

- This segment includes Internet Data Centers operating on long-term contracts.

- The high forecast rate of growth for the Internet sub-segment will peak during the 2000-2005 period. At the end of the period, the two segments will begin to merge again as all IT infrastructures become totally integrated with the Internet and the distinction between the two segments loses importance.

- "IT Application Services" include legacy IT applications that may or may not include Internet-enabled functions. In the future, virtually all applications will be Internet-enabled. As with Platform Operations, toward the end of the forecast period the distinction between "legacy" and "Internet/Web" applications will become moot; at a certain point, the Internet will become the legacy.

- "Internet/Web Applications Service – vendor-owned software" comprises software sold on either a license or pay-as-you-go rental basis by software developers directly to users. While INPUT foresees rapid growth in this sub-segment, exemplified by Oracle, software developers are unlikely to want to depend entirely on direct sales, even when delivered cost-effectively over the Internet. Proliferating demands for ancillary services are likely to dissuade them from foregoing the participation of channel partners and Value-Added Resellers (VARs). As a result, INPUT foresees a moderation in the rate of growth of this market segment by the end of the forecast period as many vendors return to their core competencies. Increasingly, this market will become dominated by the simple delivery of package products, such as Microsoft's proposed direct delivery of its Office Suite of applications on a rental basis directly to consumers. Businesses that are unable or unwilling to use one-size-fits-all package software and that require customization will return to VARs and/or traditional systems integrators.

- The "Internet/Web Applications Services – Third-party software (ASP)" sub-segment will continue to experience rapid growth over coming years, but this growth will moderate toward the end of the forecast period for several reasons: competitive pressures will force many so-called ASPs to specialize. As they do, much of their business will be more properly classified as Business Process Outsourcing or processing services. As price competition becomes intense, this market will divide clearly into low-margin, high-volume commodity software distributors and higher-margin, higher value-added resellers.

- INPUT forecasts a strong CAGR of 19% in the Distributed Systems segment, which subsumes the prior category of "Desktop Services." Due to rapid changes in technology underway, the "desktop" is becoming mobile. As it loses its fixed location, spending in this segment will be fueled by the urgent need for outsourced management of a wide array of portable computing and Internet-enabled hand-held devices. Future INPUT forecasts will provide estimates of market size for the most important of these types of portable desktops.

- The "IT Network Management" of the Network Management market includes both legacy and Internet-related components. This segment will be heavily affected by the transformation underway among large telecom vendors. Price points will drop, pricing will become critically important; toward the end of the forecast period, this segment will merge with the "Internet Network Management" segment.

- Processing services differ from outsourcing services primarily on the basis of contract tenure (outsourcing contracts are for one or more years) and by level of responsibility: processing vendors take no responsibility for the customer's software application or business process.

- E-commerce and the proliferation of a wide variety of electronic exchanges will fuel growth of vendors of processing services in the Applications Services market. Utility and other commodity processing services will grow more slowly, partly as a result of unfavorable pricing and partly as a result of technological changes that render some of the services that utility processors perform obsolete.

- "Input/output storage services" include print/scan, CD-ROM and Storage Area Network services. These are forecast to grow somewhat more slowly than the higher value-added segments of the market.

- "Other" processing includes performance monitoring, security services, authentication and related services.

- The legacy utility processing services market will shrink due to the growing dominance of Internet-enabled applications.

Exhibit D-2

U.S. Outsourcing Services Market (incl BPO), 2000-2005

	Market Size ($Millions)							CAGR 00-05 (%)
	1999	2000	2001	2002	2003	2004	2005	
U.S. Market for Outsourcing Services								
IT Technology Outsourcing	*40,010*	*47,700*	*58,350*	*71,000*	*85,400*	*100,800*	*115,900*	*19%*
Infrastructure Services	8,700	9,550	11,000	12,750	14,800	17,800	20,650	17%
IT (Platform) Operations	8,250	8,700	9,100	9,250	9,300	9,300	9,150	1%
Internet/Web Managed Services	450	850	1,900	3,500	5,500	8,500	11,500	68%
Applications Services	**16,580**	**19,650**	23,750	**28,450**	**34,000**	**38,800**	**42,950**	**17%**
IT Applications Services	15,800	18,200	20,750	23,450	26,700	29,000	30,000	11%
Internet/Web Applications Services - vendor owned software	430	800	1,500	2,500	3,500	4,400	5,550	47%
Internet/Web Applications Services - 3rd Party software (ASP)	350	650	1,500	2,500	3,800	5,400	7,400	63%
Distributed Systems (Desktop Services)	**6,134**	**7,550**	**9,200**	**11,050**	**12,700**	**15,000**	**17,700**	**19%**
Network Management	**6,700**	**8,500**	**11,200**	**14,500**	**18,400**	**22,400**	**26,400**	**25%**
IT Network Management	6,150	7,500	9,100	11,000	13,000	15,000	17,000	18%
Internet Network Management	550	1,000	2,100	3,500	5,400	7,400	9,400	57%
Applications Software Management	**1,900**	**2,450**	3,200	**4,250**	**5,500**	**6,800**	**8,200**	**27%**
IT Applications	1,750	2,150	2,600	3,250	4,000	4,800	6,000	23%
Internet/Web Applications	150	300	600	1,000	1,500	2,000	2,200	49%
Business Process Operations	*9,600*	*12,500*	*16,000*	*20,500*	*26,500*	*35,000*	*45,000*	*29%*
Business Process Operations - Standard	8,575	11,050	13,850	17,300	21,550	27,150	32,500	24%
Electronic Business Process Operations (eBPO)	1,025	1,450	2,150	3,200	4,950	7,850	12,500	54%
Total Outsourcing Services ***(IT Technology Outsourcing and Business Process Operations)***	49,610	60,200	74,350	91,500	111,900	135,800	160,900	22%

Source: INPUT

Exhibit D-3

U.S. Processing Services Market, 2000-2005

	Market Size ($ in Millions)							CAGR 00-05 (%)
	1999	2000	2001	2002	2003	2004	2005	
U.S. Market For Processing Services								
Applications Services (Transaction Processing)	32,828	36,862	40,074	45,173	51,532	58,904	68,116	*13%*
IT Applications Services	28,100	31,000	32,000	34,000	36,000	38000	40000	*5%*
Internet/Web Applications Services	1,500	1,575	2,363	3,544	5,316	7,300	10,000	*45%*
Electronic Business Applications Services	3,228	4,287	5,711	7,629	10,216	13,604	18,116	*33%*
Internet Based	965	1,523	2,510	4,015	6,440	10,500	15,700	*59%*
Non-Internet Based (EC and EDI)	2,263	2,765	3,201	3,614	3,776	3,104	2,416	*-3%*
Infrastructure Services (Utility Services)	3,190	4,210	6,636	8,698	11,884	15,275	18,875	*35%*
IT Services	1,030	1,100	1,000	900	900	875	875	*-4%*
Internet/Web Processing Services (Internet Data Centers, etc.)	2,160	3,110	5,636	7,798	10,984	14,400	18,000	*42%*
Other Processing Services	6,200	7,005	8,040	9,155	10,300	11,150	11,800	*11%*
Input/Output/Storage Services	5,600	6,300	7,000	7,900	8,850	9,500	10,000	*10%*
Other	600	755	1,040	1,255	1,450	1,650	1,800	*19%*
Total Processing Services	42,218	48,127	54,750	63,025	73,716	85,329	98,791	*15%*

Source: INPUT

Exhibit D-4

Vertical Industry Market Breakdown, U.S. Outsourcing Market, including BPO 2000-2005

	US $m 1999	Growth 1999-2000	2000	2001	2002	2003	2004	2005	Growth 2000-2005
Total U.S. Outsourcing Market (incl. BPO)	**49,610**	*21%*	60,200	74,350	91,500	111,900	135,800	160,900	*22%*
Banking & Finance	10,418	*18%*	12,341	15,614	19,215	22,940	28,246	33,789	*22%*
Business Services	6,006	*15%*	6,923	8,625	10,797	12,869	15,210	17,377	*20%*
Discrete Manufacturing	3,229	*32%*	4,274	5,428	6,771	7,833	8,827	10,941	*21%*
Education	741	*6%*	783	1,190	1,739	2,798	3,409	4,666	*43%*
Federal Government*	2,481	*21%*	3,010	3,420	4,026	4,700	5,160	6,597	*17%*
Health Services	4,073	*17%*	4,756	5,576	6,588	7,945	9,506	10,760	*18%*
Insurance	6,945	*21%*	8,428	10,260	12,627	15,442	18,876	21,641	*21%*
Miscellaneous Industries	1,642	*17%*	1,926	2,454	3,111	4,252	5,160	5,310	*22%*
Process Manufacturing	2,406	*33%*	3,191	4,015	5,033	6,266	7,876	9,171	*24%*
Retail Distribution	2,253	*34%*	3,010	3,792	4,758	5,931	7,333	8,689	*24%*
State & Local Government	893	*45%*	1,294	1,710	2,562	3,605	5,160	6,436	*38%*
Telecommuni-cations	3,616	*17%*	4,214	5,279	6,405	7,609	9,234	11,102	*21%*
Transportation	2,728	*13%*	3,070	3,718	4,575	5,371	6,790	8,045	*21%*
Utilities	1,355	*29%*	1,746	1,933	1,922	2,630	3,395	4,505	*21%*
Wholesale Distribution	893	*35%*	1,204	1,338	1,373	1,511	1,670	1,834	*9%*

Source: INPUT

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E

Appendix

A

IBM CEO Lou Gerstner's keynote address: "Next Generation E-business, " at the eBusiness Conference and Expo in New York City on December 12, 2000.

The focus of Lou's address was the major business and technical trends emerging in the next generation of e-business.

Transcript of Lou Gerstner's remarks follows:

The last time that I was on this stage was exactly four years ago today delivering the keynote at Internet World in December of 1996. And I'm tempted to say it's been an interesting four years, but why skip back to the primordial days of the Internet? The events of this year alone have been plenty interesting all by themselves.

Of course, 2000 will be remembered for the dot-com shakeout and with it, the overturning of the belief in the media and in the boardrooms that if you weren't "dot-com" you were "dot-toast."

We also saw the brief fascination with B2B marketplaces -- e-marketplaces -- many of them still alive only in press releases. And just the other week, The New York Times was wondering if there really was something called the "New Economy."

So, lots of twists and turns, fortunes made and lost -- the kind of high business drama that used to play out over years and decades has been compressed into months and quarters. How exhilarating! What sport!

But I suspect that many of you who don't work inside the information technology industry -- and even some of you who do -- are asking: "Excuse me? Was this all just fools gold?" Is e-business and the Internet just a digitally remastered version of client/server? Another paperless office?

The checkless society revisited? A collusion between the I/T industry, which wants to sell boxes, and the media, which wants to sell papers?

All of this was running through my mind as I prepared for this talk. And I feel I owe you, if not an explanation, at least a perspective. After all, I was one of the first to say the Net was going to take its place alongside all the other great, world-altering technologies like electricity and manned flight.

I think what's happened with e-business parallels what's happened with those other transformational technologies. First, there's a period of wild enthusiasm -- intoxicating optimism that the new technology is going to rewrite the laws of competition and economics, going to create whole new wealth, wipe out old industries, create new ones. Predictably that fever passes -- only to be replaced by significant disillusionment. People open their eyes. They don't see new industries. They don't see radically new business life forms. And they say: "Bah, forget it."

That passes too, and the world finally gets down to the important work of taking the technology and integrating it into the structure and fabric of society and business. And that's where we are today with e-business. In its first phase -- you all remember well -- a lot of confusion about what the Net would be.

Remember all the commotion about "content"? "Content is king. I've got to own content. I've got to partner to get content." Why? Because people thought the Net was all about online magazines, online sports scores, digital artwork. Then the first real killer app arrived: consumer e-commerce. The race to sell books, groceries, airline tickets, toys, videos, pet food -- you name it -- over the Net.

And then, after we all got tipsy on Internet retailing, we lurched over to the next drunken binge -- B2B e-commerce.

And once again, something important, something real, got obscured by simplistic schemes: competitors commingling their supply chains or even taking the supply chains public,divorced from their basic company.

And what was the driving force behind much of this frenzy? It was the desperate, aching desire to be seen as leaders in building "The New Economy." The New Economy. That's a very interesting concept. What would constitute a New Economy? It might have new currencies. We could call them e-bills or e-bucks. Instead of musty old metrics like revenue and profit, we'd measure things on the basis of "eyeballs" and "stickiness." Instead of bona fide customers and genuine loyalty, we'd have hits, clicks, page views and downloads.

What a wonderful world! And some people really believed in it. But I think most people now realize that the business world doesn't work that way. Too many people failed to remember that the Internet is a technology. It is a tool. Yes, a very powerful one, but it didn't change the fundamental behavior of consumers: such as their desire for choice; like wanting to inspect the product and possibly return the product.

Despite the fact that a lot of Internet retailers burst upon the scene proclaiming whole new business models, in reality, their business was built on a centuries-old value proposition -- lower price. The trouble was they didn't have a business and economic model that could sustain these lower prices while generating returns. And when they couldn't subsidize those models with easy access to capital -- welcome back to earth. So where are we? Today, e-business is just business -- real business. And real business is serious work. After the hype, after the IPO alchemists have had their 15 minutes, it's time to understand that we've come to the hard part. And the winners -- the people who stick with it and do the work -- understand that this next phase of e-business is going to be all about two things: Integration and Infrastructure. And that's what I want to talk about this morning.

First, integration. IBM has believed from the very beginning that the Net was going to be about the transformation of every important transaction and relationship. Not just one -- not just e-commerce -- otherwise, we wouldn't have invested $1 billion building this category we call e-business.

Now, what transactions and what relationships are important to businesses and institutions? There are many.

Interactions on the front end, yes, with customers, but also with people who want to invest with you and people who want to work for you.

Interactions at the back end: across the supply chain, transactions that connect an enterprise to markets and to industries.

There are vital internal transactions: order processing, fulfillment, logistics, manufacturing and employee processes.

And finally, all those relationships companies want to have with their products: appliances, industrial machinery, consumer electronics -- so the company can provide after-sale service and also understand how these products are performing in the marketplace and then make them better.

Now, five years ago we asserted that every one of these processes and relationships would be transformed by the Net. But if you think about it, we've actually only seen transformation of one business process so far:

business-to-consumer commerce. That's okay, because if nothing else, it ignited everyone's interest.

But now a lot of companies have discovered that taking orders over a Web site is only a very tiny piece of what's needed to complete a successful sale. e-commerce triggers a chain reaction throughout the rest of the enterprise: across pricing systems, inventory, logistics, credit, and distribution and on out to the supply chain.

So now, the e-business leaders understand that the e-business transformation must sweep across all of these core business processes. This is driving huge investments today in applications for supply chain management, e-procurement, customer relationship management, knowledge management.

And while all of these processes are being transformed, something else is going on. They're being connected. They're being fused together. They're being integrated within the enterprise. This is a very important, difficult and significant issue for CEOs. The fundamental organization and governance models of corporations is being challenged. Historically, in many institutions, every one of these business processes was a standalone operation. But to get the real benefits of e-business -- the speed, the cycle time, the customer responsiveness -- these internal processes and applications must be integrated. Without that integration, the lifeblood of e-business -- customer data, pricing information, inventory levels, supply management -- cannot flow throughout the business. The integrating technology, by the way, is the easy part. The middleware software to do that is available today. The hard part is for the business leaders to make the commitment to reconceptualize their management systems and organization models. And I can assure you that is hard, hard work.

So, in this next phase of e-business, the goal now for CEOs and other business leaders is to go beyond e-commerce. The goal is to build a fully integrated enterprise -- a fully realized e-business, the integrated e-business. Let me give you an example: Whirlpool. The core processes: They have consolidated 45 different fulfillment and financial systems and then e-enabled their workforce.

On the back end, a supply chain portal to connect trading partners, sellers, distributors and back office operations. On the front end, the same portal is available to individual consumers that use it to order small appliances and accessories.

And finally, transforming their relationships with their products: refrigerators, washers and dryers all being outfitted with a little intelligence and a Web connection. The first of these products comes to the market next year.

That's what I mean by an integrated e-business: end to end, every relationship and interaction. And as I said, this model represents a full frontal assault on the prevailing mantra of organizational theory: decentralization is good; centralization is evil. Now, I happen to believe in decision making being pushed to the lowest possible level. But I will say this categorically: In a networked world you cannot operate in a fully decentralized mode. The Net is an integrating medium. It makes it possible -- it makes it imperative -- to unify processes and information that in most institutions were splintered in the rush to decentralization over the last few decades.

That leads to the second important development in this next generation of e-business: infrastructure. This is about where and how the work of computing gets done. Today, we all know that in a networked world the heavy lifting of computing isn't going to be done by PCs or game consoles or, for that matter, your washing machine. e-business workloads are going to be managed and processed on transaction and Web servers, on middleware, on storage devices. And interestingly, workloads will be managed in the network itself -- somewhere between the end user that initiates a transaction and all the gear in the traditional data center.

That's why, somewhat amazingly, "infrastructure," -- a term that's been associated for 50 years with roadway and pipes and concrete -- has suddenly become trendy. Look how many technology companies claim to be an "Internet infrastructure" company these days. But I'm not sure everyone agrees on what an e-business infrastructure should look like, how it should be built and what the requirements are.

So, let me share with you three aspects of e-business infrastructure that we think are going to be very important.

First, e-business infrastructure is "end-to-end" infrastructure. Until now, "end-to-end computing" meant the desktops at one end and the servers at the other -- all within the same enterprise. But think about what "end to end" means in the e-business world that's coming toward us.

At one end, you've got every supplier, every distributor, regulatory agencies; licensing boards, tax authorities, all outside your firewalls.

At the other end, the explosion of devices. Yes, 700 million personal computers by the year 2003. But they will be dwarfed by other kinds of networked access devices: personal digital assistants, Net-enabled cell phones, game consoles. We've all seen the forecasts. Within the next few years there's going to be a billion wireless appliances connected to the Net. Mobile e-commerce is going to be a $100 billion marketplace by the year 2003. But what we call "pervasive e-business" won't stop at the integration of new kinds of end user access devices. Coming up right behind all these new end user devices will be a trillion or more connected "things" -- things we'd never think of as "computers" but which will be doing a little computing and maybe a little storage.

This pervasive world is with us already: Whirlpool's smart appliances; Medtronics is working on pacemakers that will have Internet addresses; very soon your car will be a client device on wheels. So, that's what we mean by "end-to-end business infrastructure."

The second aspect of infrastructure that's really important is standards. I'm not going to say very much about standards because if you understand "end to end" and what it really means, the need for standards-based computing is very easy to understand. The infrastructure must be open, and it must be based on cross-industry standards so you can connect to those millions of people and businesses wherever they are and connect to those billions of devices whatever they are.

That's why the fight for open standards is worth fighting. That's why XML has got to remain open. That's why we're betting a big piece of IBM's future on Linux. We're going to invest nearly $1 billion in Linux next year. Fifteen hundred IBM developers are dedicated to Linux-enabling our products and services -- and not just for applications that run on a wristwatch, which we've built by the way.

We're moving Linux into commercial production environments. Today we announced that we will install a supercomputer-scale Linux cluster -- the largest Linux installation in the world -- at Shell International Exploration and Production. Keio University in Japan is integrating two campus networks supporting 15,000 users with Linux. Last week Telia, the largest telecommunications company in Scandinavia, announced it's going to run its core business applications and consumer Internet services on a mainframe running Linux. And along with Intel, NEC and HP, we've already announced a huge Open Source Development Lab in Portland, Oregon -- an independent, non-profit resource to give the open source community a place to test enterprise-class Linux software. Why? Because we're convinced that Linux can do for business applications what the Internet did for networking and communications: Deliver on the promise of truly open, interoperable, any-to-any computing.

Linux shipment growth is expected to increase more than any other server operating environment over the next few years. It's growing at twice the rate of NT, and there are some estimates that say Linux will cross over and become more prevalent than NT by 2004.

This is a big issue for every server company. It's going to be interesting to see if three or four years from now, anybody with a proprietary UNIX system will still have a meaningful position in the industry. In fact, the movement to standards-based computing is so inexorable, that I believe Sun -- and for that matter, EMC and Microsoft -- are running the last big proprietary plays we'll see in this industry for a long time to come.

A final point on infrastructure, which some of you are well aware of. The infrastructure technology that exists today isn't ready. Now, I know it's not fashionable in the computer industry to point out limitations of technology, but the fact is, the infrastructure today cannot handle what's coming. I've seen projections of 1,000-fold increases in Internet traffic in the next few years, and that's probably reasonable. Inside IBM, we talk about 10 times more connected people, 100 times more network speed, 1,000 times more devices and a million times more data. Whatever it is, very soon this networked world is going to be several of orders of magnitude bigger and more complicated than anything we know today.

So we're headed for a wall. Customers can't just roll in processors and storage fast enough to avoid meltdowns when usage spikes, or to deal with this cacophony of devices, or fend off viruses or hacker attacks, or handle translations on the fly. People are good, but they're not that good.

All of this -- the load balancing, the traffic management, the security, the transcoding -- all of it has to happen in real time -- naturally, spontaneously -- based on far greater levels of intelligence that are built right into the network.

And by "intelligent" I'm not talking about computers that can write the next Ninth Symphony. I'm talking about intelligence that, for example, we take for granted in our own bodies. We walk up three flights of stairs and our heart rate increases. So does our oxygen intake. When we plop down into a chair, our bodies adjust. It's hot, we perspire. It's cold, we shiver. We don't tell ourselves to do these things. They just happen. We need something similar for e-business. It's a much more natural, spontaneous, almost autonomic kind of computing.

Let me give you an example from the ultimate extreme of high-end computing. Last year IBM launched a $100 million project to build a new class of computer: a system 100 times more powerful than today's biggest supercomputer. We call it Blue Gene -- G-E-N-E -- because the first application is going to be to attack the mystery of protein folding in biology. Now, computing on this scale involves millions of linked processors working together, so that at any point in time we know that some of them will be failing. They'll "die" just like at any given moment of any day cells in our bodies are dying, replaced and flushed from the system. The system works around it and doesn't skip a beat. That kind of autonomic, self-healing system is exotic, but within a few years it will be commonplace in all kinds of mainstream commercial applications.

Let me mention one more aspect of infrastructure. We hear a lot about it: scalability. We're building for a day when our e-Servers are virtually impossible to outgrow. We're almost there now. Not just "always on" or available or reliable -- you can get that with today's technology, for example when usage spikes in response to a retailer's holiday promotion, the server automatically shifts resources to handle it. That's important, but it's not enough.

So our e-Servers extend that kind of capability to cooperate with Cisco networks. When the loads increase, the network gear doesn't just indiscriminately spray transactions at the server; it picks the ones the customer wants handled first with the best response and the highest quality. Buyers go first -- browsers wait.

By the way, this illustrates the importance of the network equipment company and the I/T companies coming together more closely than we have to date to build an open standards-based view of this e-business infrastructure.

There's a final aspect of e-business's future I'd like to mention because it's going to be big. I think that five or 10 years from now we're going to look back on this as one of the really game-changing developments.

It's the trend we call e-sourcing. Now, you know what outsourcing is. It helps customers convert fixed cost into variable cost. It lets them focus on their business and lets somebody else focus on the complexities of I/T. e-sourcing is the logical extension of outsourcing. It capitalizes on the intersection of several historical developments: the massive build-out of broadband; the rise of standards-based computing; and the escalating requirements of e-business infrastructure that we've just talked about. Now, don't get me wrong, there are going to be lots of customers that are going to continue to run their own information technology operations for a long time to come: own the servers, own the middleware, own the applications, own the storage devices and manage all the staffs.

But we know today that an increasing numbers of customers are going to buy I/T as a utility-like service over the Net. They will e-source information technology from a variety of third-party players: today's telcos, traditional I/T providers like IBM Global Services, as well as from some new entrants. These e-sourcing providers are already building the data centers of the future: massive "server farms" -- mega-plexes with acres of servers and storage with the kind of advanced infrastructure attributes I described a moment ago. We've seen this kind of shift to service providers before -- for example, in the build-out of the power grid. When electric turbines first came about decades ago, if your business needed electricity you built your own generating plant. There weren't many options. By the same token, for the past 40 years if a business wanted information technology, they bought it, owned it and managed it. Now there will be an alternative.

We're already seeing the early stages of the e-sourcing trend in Web hosting, in storage hosting, in application service provision, in computing-on-demand schemes. That may be where it starts, with companies offering these co-location services -- a kind of kennel for computers. But customers want more than that. They want service providers who can provide sophisticated load balancing, security, storage, network management and application management.

Today, e-sourcing is about a $6 billion business, most of it in simple Web hosting. But by 2003, it's projected it's going to be a $55 billion market. And as it takes off almost all of the growth is going to be in the higher value-added segments.

So e-sourcing is not a simple business. It's more than a fancy control room and raised floors that stretch to the horizon. It will require experience in managing highly complex systems, and it will have high technology content. It is as much the domain of the computing service providers as the network providers.

At IBM, we're building on a traditional outsourcing business that will generate about $14 billion in revenue this year. We already manage 175 data centers worldwide, 25 of them dedicated e-business centers. On top of that, we're going to invest $4 billion over the next three years and open 50 more e-business hosting centers.

But nobody will go it alone -- not in a business this complex. So we're working with network and facilities partners like AT&T, Qwest and NTT. We're working with software and services providers like Akamai, Siebel, i2 and Ariba. And we're working with the wireless providers like Nokia and Motorola.

I believe that the shift to e-sourcing will fundamentally alter the go-to-market models of the computer industry. Over time, we will sell more and more products to a smaller and smaller number of mega-customers, who will "resell" computing services. By the end of this decade, 20 or 30 of these mega-customers -- including our own Global Services business-- could consume 25 percent of our output. It could happen. If this is the way the industry is moving -- and we think it is -- we really are on the verge of a fundamental restructuring of both the industry's economics and its competitive dynamics.

So far we've been talking about all the business and the technical possibilities in this next generation of e-business. But I hope as we think about what can be, we understand that what's possible is not predestined.

As with the advent of every world-altering technology from the printing press, to nuclear energy, to television, the arrival of the networked world is raising serious public policy issues.

Societies are going to have to establish predictable, trusted approaches to issues like Internet taxation, trade rules and protection of intellectual property. But I will tell you that paramount among all these policy issues is privacy. This one is not going away. And if we do not act responsibly, we run the risk of choking off this amazing but very young and very fragile economic engine.

I go back to the outset of my remarks. One of the hard lessons we've learned over the past year is that the Internet has not rewritten the laws of economics and competition. Well, it also hasn't rewritten the fundamental laws of consumer behavior either. We know that trust is a fundamental element of every positive brand experience. It's fundamental to all consumer behavior, to the willingness to buy and to brand loyalty. All of it is based on trust.

Now, we also know what a lot of consumers do when they go to a Web site and are asked to fill in their name, address, age, income levels and all that. They say they're Albert Einstein with an income of $5 and an e-mail address of E=MC squared. Worthless data. What are customers really saying when they do that? They're saying they don't trust the security of the site, and they don't trust that the owner of the site is going to respect their privacy and not abuse or sell their personal data. So this is a "confidence" issue. It's not a technical issue.

And while serious -- very serious -- the privacy issues we're dealing with today are trivial compared to what's ahead. What are the implications for individual privacy in a world where millions of people are driving Internet-enabled cars that have their movements monitored at all times? What happens to privacy for millions of people with Internet-enabled pacemakers? And forget about the debate over who has access to medical records. Who has access to real-time data on your heartbeat, blood pressure and cholesterol levels? Your doctor? Your insurance company?

The answer here must begin with a responsible marketplace. Through our policies and our practices, industry has to send an unambiguous message that tells people: "You can trust us. You have choices. They will be respected. And you'll know in advance how any information that you give us will be used."

Getting a workable privacy framework in place is going to require leadership at all levels, including government. It will require thoughtful examination of what kind of public policies -- including legislation -- should be implemented.

Let me ask you to do just one thing when you leave here. Go back to your organization and find out if you've designated a privacy czar -- a senior executive with the clout to drive a real privacy policy through your organization. At IBM, we named ours a few weeks ago. We weren't the first, but we won't be the last. And I think that in itself is important. We -- all of us -- we've all come a long way in the last four or five years. We've lived through a wild ride of experimentation: meteoric ascents and spontaneous combustion; new models tried, some validated, some tossed onto the slag heap of Internet Chapter 1. It's my hope that even in those things that didn't work we learned -- so that we proceed to the next phase of e-business with a level of maturity, reason and stability that was absent for much of the period we just passed through. And I hope one of the lessons that we take with us is that the world that we are building is far more important than one of the computer industry's long-standing obsessions.

Simply put, what we're doing here is not about building some utopian world of personal convenience, of perpetual relaxation and leisure. That's not what's important. Carmakers aren't investing billions in telematics just so that you can talk to your steering wheel and ask your intelligent house to fill your intelligent bath -- all so you can have a hot soak four minutes earlier. Applications like that are fun, and I guess they'll improve modern life a little bit. But that's not the economic imperative for making this historic investment, this historical transition.

There are far, far more meaningful, more profitable and more important aspects of e-business before us. In the commercial world for sure, and we've talked about those, but also to deliver better education to more of the world's people; to create opportunities to close the divide between rich and poor -- the information haves and have-nots; to decode the molecular mysteries of our bodies to develop better life-saving drugs; and, yes, very definitely yes, improve democratic institutions and processes for all people, in all states, for all nations. All of that is within our reach.

When I look back on the past five years I think that, for a lot of people, the omnipresent "e" in e-business came to stand for "easy" more than anything else: easy life, easy money, easy business. But I think we all know better today. I, for one, have never been more excited, and more optimistic about e-business -- and that has everything to do with the wacky period we've just come through, a necessary learning experience in hindsight. And looking forward, the opportunity is still there to improve business, to improve the lives of people, to make the world a more tolerant, prosperous and secure place and address the most intractable challenges we all care about as businesspeople, as parents and as citizens.

These are the challenges worthy of our time, our investments and our best thinking.

Breaking the Barrier: Federal to Commercial IT Outsourcing Markets

Albert Nekimken, VP-Research
INPUT, Chantilly, VA
March 2001
anekimken@input.com

About INPUT

- Founded in 1974--a Web-based IT market research and marketing services firm
- Offers IT buyers and vendor support through subscriptions and custom projects.
- PUBLIC-SECTOR MARKET services
  - ❒ IMPACT IT opportunity database
  - ❒ Electronic Government
  - ❒ Agency Profiles
  - ❒ MyINPUT
- CUSTOM RESEARCH--global commercial and U.S. public-sector

Table of Contents

- Project Overview
- Principal Findings
- Key questions
- Breaking Down Barriers
- Conclusion and Recommendations

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Project Overview

Project Overview

- Phase 1 - Should DynCorp enter the U.S. commercial IT outsourcing market?
- Phase 2 - If yes, what needs to be done?
- Phase 3 - How should the plan be implemented?

Project Overview (cont.)

Phase 1 included--

- **In-depth User (6) and Vendor (22) survey interviews undertaken for DynCorp only**
- **Other proprietary INPUT survey data**
- **INPUT's proprietary IT outsourcing market forecast, 2000-2005**
- **Secondary research**

Principal Findings

Good planning + Great Potential = Excellent Profitability from Commercial IT Outsourcing

Principal Findings

- The IT <u>outsourcing</u> market is growing faster than other market segments
- The *commercial* market is growing much faster than the *federal* market (and is more profitable)
- <u>Diversification is a win-win proposition</u>: experience gained in the commercial market appeals to federal buyers

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Principal Findings (cont.)

- Commercial customer bias against federal outsourcers is surprisingly light
- Vertical industry expertise is critically important
- Truly “horizontal” applications may not exist

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Principal Findings (cont.)

- Top-tier outsourcing vendors are highly vulnerable to price competition
- IT outsourcing can be a "foot in the door" to additional, even more profitable long-term business
- DynCorp can leapfrog over barriers by partnering with larger vendors and outsourcing consultants

Key Questions

Knowing the right questions to ask takes experience and courage

Key Questions:

- Why move into the U.S. commercial IT outsourcing market?
- How does the commercial market compare to the federal market?
- Where is the commercial market going?
- What do commercial customers want?
- How can DynCorp overcome barriers to entry?

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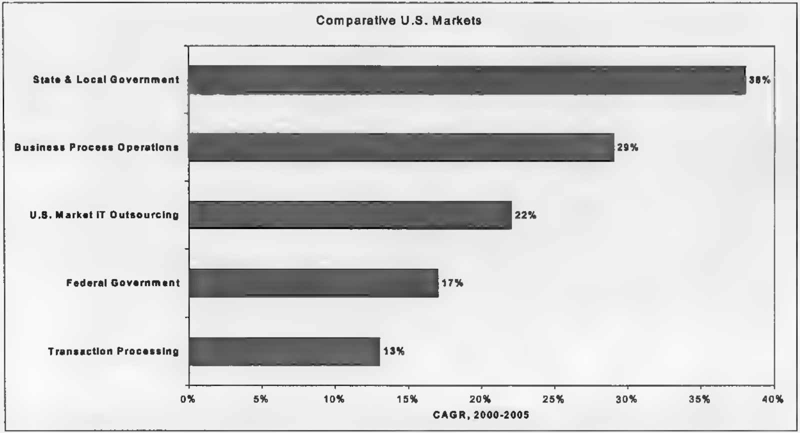
Why move into the U.S. commercial IT outsourcing market?



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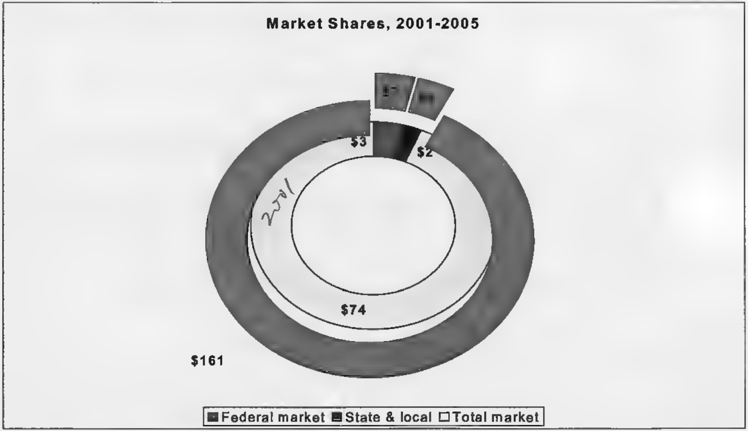
How does the commercial market compare to the federal market?



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Where is the commercial market going?

- Operational services market is splitting up into traditional and Internet-centric segments
- "We don't want to deal with technology. You handle it. Make this stuff work."
- Demand for Web-based application services to show robust growth
- Demand for Internet-centric infrastructure and network services to outstrip other segments

What do commercial customers want?

- **If federal buyers are difficult, commercial buyers are skeptical**
- **Commercial buyers are increasingly willing to outsource a wide range of functions *(the driver: inability to attract or retain sufficient in-house IT staff)***
- **Loyalty to outsourcing vendor incumbents continues to erode; buyers are receptive to scrappy newcomers**

How can DynCorp overcome barriers to entry?

- Overcome lack of commercial name recognition by partnering
- Invent and dominate a new market niche
- Specialize aggressively in either horizontal, or vertical industry applications

How can DynCorp overcome barriers to entry? (cont.)

- Leverage federal experience by promoting skills best appreciated by commercial buyers:
  - ✓ security expertise,
  - ✓ strong program management,
  - ✓ high-level SLAs
- Conserve capital by favoring remote services
- Build technical staff by creating attractive, long-term career paths for transfers

Breaking Down Barriers

Winners vendors: ACS, SAIC, CSC

Loser vendors: CACI, UNISYS, OAOT

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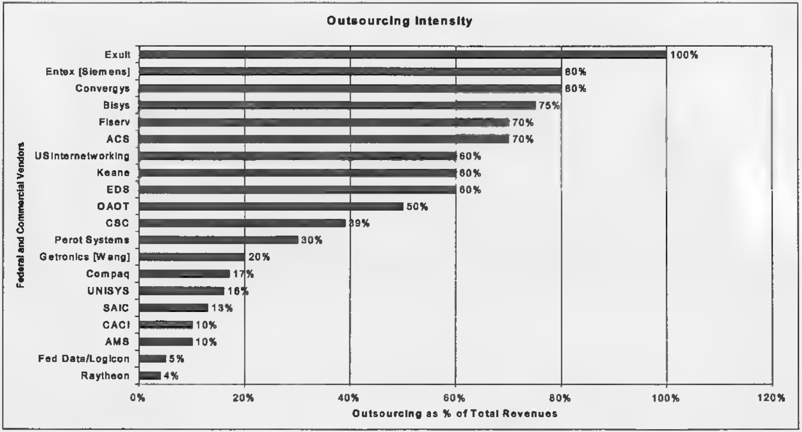
IT Outsourcers Vary in Business Mix



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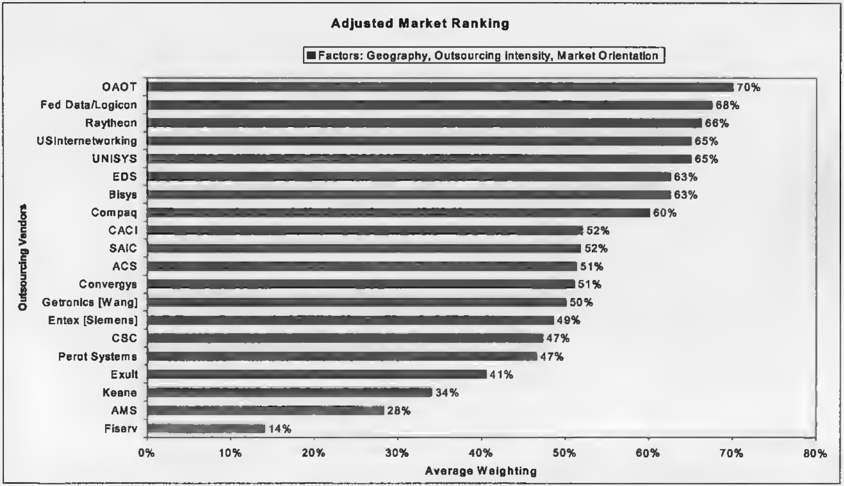
Outsourcers Weighted by Factor



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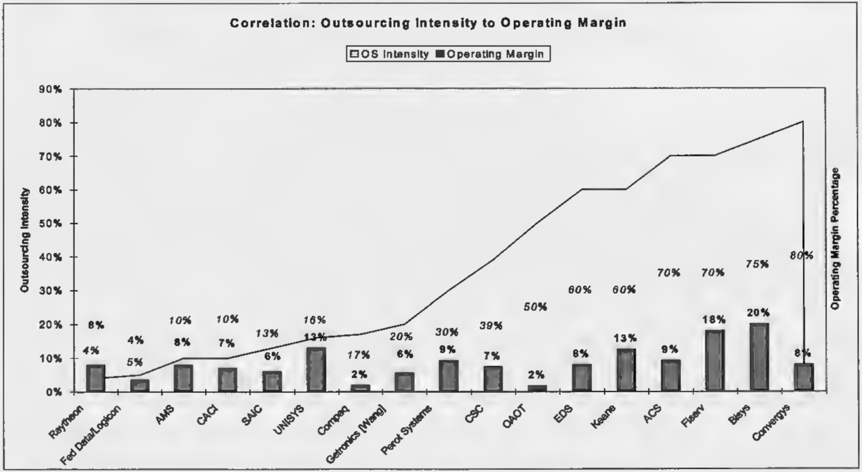
Operating Margins Rise Parallel with Outsourcing



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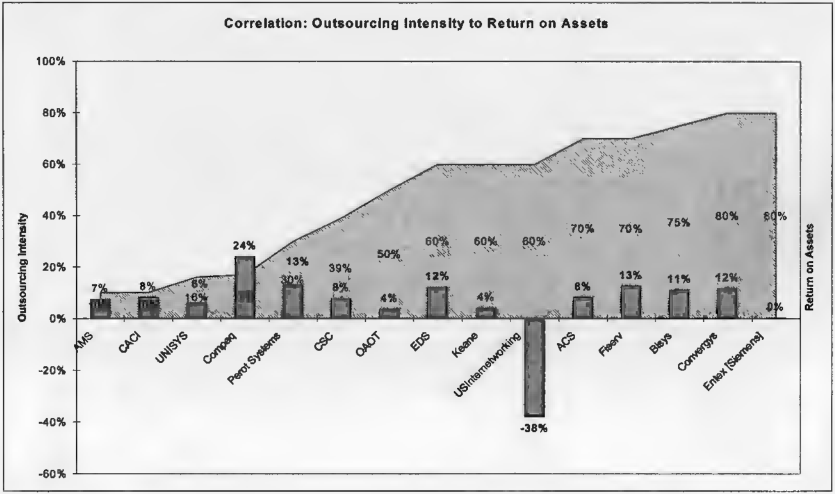
Difference in ROA? Inconclusive



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Conclusion and Recommendations

Go for it! --but plan wisely!

Conclusions

- The most profitable IT vendors are diversifying their sources of revenue by being active in as many markets as possible
- Expanding the number and diversity of customers in itself promotes greater efficiency
- There is no substitute for demonstrated vertical industry expertise; hence, no shortcut to achieving credibility

Recommendations

- Assess technical, financial, organizational and sales resources honestly prior to attacking the commercial market
- *Develop a realistic short and long-term business plan*
- Achieve internal commitment to success based on cooperation
- *Avoid overpromising and underperforming*

CYNDC1 User Survey Results

February 1, 2001

10 completed

EATON CORPORATION **216 523 4903**

Curt Chandler MIS Manager

Q1/Yes

Q2/Overall IS responsibility

Q3/Varied, used extensively for development and ERP work.
Some e-business, Website design and some related development.

Q4/No, we prefer to award specific contracts for a discrete piece of work

Q5/Recoverable costs from departmental budgets.

Q6/We work from an existing list of preferred (known) vendors to which we add and remove. Generally an outsourcing contract is awarded to a company to which we have an already established relationship.

Q7/Not really applicable. They would have to meet the criteria (as per Q6)

Q8/Not really important. We tend to outsource contracts which we do not have the resources internally. Our in-house staff either assist these contracts in secondary role or they are assigned a new piece of work (totally unrelated). Transfer of staff has not occurred to date.

Q9/More selective. The market is becoming more discrete, with organisations having greater specialisation. I think that there is a decrease in the "larger all-encompassing" projects. User companies lack some of the management tools internally, the vendor must proactively manage the customer (as well as the project). Outsourcing is moving away from maintenance of products and support of users towards working on new architecture and solution development..

10/Smaller independent companies who provide specific services. Helpdesk, Internet Web services, production of documentation, training, raw coding and programming.
Not purely a support arrangment, they need to provide stability in an older operating environment.

Q11/Not measurable in commercial business terms. Outsourcing is an essential link with our in-house technical delivery teams. We have improved timescales for on-going development and achieved better quality at a reasonable cost.

Q12/Little. We are committed to a business transformation programme and outsourcing is part of that building block for the future.

Q13/Not at all. Our policy towards outsourcing is (as per Q10)

Q14/We have been able to reduce our internal headcount and not have to increase new-skill recruitment. We have also been able to better control the overall IT overhead and budget. We are maximising the returns on our original IT investment; bringing operational benefits to the company.

Q15/Our contracts have always tended to be short and we don't see this changing.

Q16/No

Q17/Very sensitive.

Q18/Relationship is good. We always have prior working knowledge and exposure with the vendor, so our risk is minimised.

Q19/Not an issue.

Q20/Doesn't really bother us. We tend to avoid the large players as we get better service from smaller companies.

HOLOGIC INC **781 999 7300**

Dave Rudzinski Director of IS

Q1/Yes

Q2/Overall director of all IT

Q3/Have been involved in several outsourcing arrangments in many mixed environments

Q4/In an ideal world, we would go with as much bundled as possible. We have a large contract with ADP, but we still have the need to place 2-3 other individual contracts with other service vendors

Q5/The primary reasons were that we had a mixed environment of DEC/Compaq, Solaris and Unisys. Control of this became very difficult and cumbersome, so we started to outsource different elements of this. We did have the objective to reduce the main overhead of the service cost and to be able to complete other (new) IT projects faster.

Q6/Proven record, expertise. Must be a solution provider. Knowledeable in our application types and operating environment. Proven success on similar types of outsourcing projects.
Expertise in web-enabled financial software.

Q7/In theory it would not prevent us. Our current situation is that we have contracts to be outsourced. We want to remove that responsibility from us to a partner vendor to allow the vendor and ourselves to focus on our technical strengths.

Q6/Important in that they manage the human resources. We had problems in recruitment and retention of staff, so this is an essential part of the project.

Q9/Some services are easier to contract out now. Operational duties are spreading into new IT areas especially CRM. Outsourcing is now an acceptable process and customers are more intuitive.

Q10/Support for specialist software packages, project management, BPR.
All e-business services and internet integration.

Q11/The skills are available, but the costs are very high. A high proportion of our overall IT budget now goes to external contracts. We have definitley seen a reduction in capital and recurring costs.

Outsourcing has allowed us to stay ahead competitively by increasing the timescales to develop new applications.

Q12/Inertia towards external service suppliers in some circles; thoughts are that we will obtain a better return on IT using inhouse staff. Even though there is a general shortage of key skills; the service vendors don't necessarily have the skills either.

Q13/Only if they can provide added value for enhancement and support. Improvements in change are usually never achieved. Trying to combine external and internal resources (as present) can be very difficult, but outsourcing the entire IT and business processes would be a massive decision.

Q14/Ultimately, the measurement has got to be reflected in the success of the business generation. Lower operating costs, greater turnover, numbers of increased transactions; do you ever know the real story????? It depend on the business model that is being adopted.

Q15/As long as they are on time and within budget.

Q16/Using external resources doesn't necessarily improve costings, it merely moves them from one business unit to another.

- Mainstream support of MVS and UNIX systems
- Technology integration with requirement for special technical disciplines.
- Bespoke [customized] applications running on AS/400s.

Q17/We introduced our own best practice.

Q18/Service suppliers lack the understanding of fostering relationships; they are driven by short-term objectives. There is always a perceived conflict, but we have better control of the resources that support our organisation.

Q19/Discussions with the unions to keep jobs in-house. They are selling the long-term benefit of keeping expertise internally.

Q20/It does influence you if the contract has significant $ value, or it is critical to the strategy.

GARDEN WAY INC **518 233 4300**
Don Steele IS Development Manager
Dsteele@garden.com

Q1/Yes

Q2/ IS Development Manager

Q3/I have final decision on all outsourcing (bespoke and otherwise)

Q4/Bundled. We manage all our outsourcing through KPMG.

Q5/Originally to reduce our headcount and look at ways of reducing our cost base.. Laterally we are now looking for expertise in specific disciplinesand to improve development performance. To improve the key components and business functionality. Whilst we want KPMG to provide better service, we also want them to be more customer focussed.

Q6/We always use KPMG as our principle partner who will manage the overall contracts.

- There are about 20 other organisations which we define and source the operational services from, but the contract is planned and managed by KPMG.
- Single source contract for urgency and proprietory systems support.

Q7/I would have my doubts, not really decided yet.

Q8/Not important

Q9/More procurement via the Internet. Big changes in the variety and type of service; allows expansion into other areas. Greater professionalism.

Q10/An application management and support role for ERP. Answer to our skill shortages; can be the most practical solution.

Q11/Improved efficiency on the supply chain. Faster and cheaper to get our applications and services up and running.

Q12/More positive; allows staff more time for other applications. Lead times for service have improved, greater responsiveness from the vendor leading to greater satisfaction all round.

Q13/Yes

Q14/Yes. We have seen the benefits of joint ventures and strategic alliances; both parties share costs and resources.

Q15/Shorter contracts are easier to control and manage.

- They also keep costs down as more regular contract renewals maintain a more competitive environment.
- In longer contracts, vendors have a greater opportunity to "milk you" for higher prices.

Q16/Would give a lot of thought to ERP contracts costing >$2 million

Q17/Very sensitive about the manufacturing process – would not want this to go externally.

Q18/Good

Q19/None, we are a non-union shop

Q20/Great influence, size and longevity are important.

AMERICAN CRYSTAL SUGAR COMPANY 218 236 4420

Marty Erbes IS Director

Q1/Yes

Q2/IS Director

Q3/Main decision maker in all major IT decisions

Q4/We end up with a balance. We had a policy to widen the supplier base and to bring in a greater level of knowledge and expertise. Better commercial advantages in not bundling the contract

Q5/

- Better service and support.
- Improved staff usage and utilisation.
- Well suited to development and bespoke projects.
- Relieve the workload to the existing IT team.

Q6/

- Cost
- Quality of company and their people.
- Team building and management.
- To manage the applications through development testing and production.
- Able to meet demanding delivery requirements.
- Process functional and technical skill sets.

Q7/"give me a name". In a hypeothetical situation, I would say that if the vendor possess quality, service and speed in implementing a quality standardisation programme, then federal-only experience should not be an issue. One or two large federal contracts can allow an organisation to grow very rapidly. Companies like EDS were very heavily involved in federal contracts and it didn"t really prevent the company from moving into the commercial market.

Q8/If we do not want to continue with a large in-house IT resource, then the supplier must fulfil that role.

Q9/

- Must show tangible improvements.

- Facility to increase communication.
- Commitment to achieving specific goals.
- Support the complete process and to determine the business model.

Q10/

- That by which we can better satisfy our customers and users.
- We want to strengthen the team at operational level and oversee the technical side of the legacy projects.
- Support of the wider business units

Q11/I think that we have achieved:

- Improved service levels to users.
- Enhanced the level of support
- Provide control and improved quality.
- From a commercial point of view, we have reduced operating costs whilst experiencing very tough trading conditions.

Q12/More confident in design and reviewing operational models.
Processing and operational control have improved considerably. Account management is easier to control and manage.

Q13/We have very ambitious plans and want to be able to move forward much faster.
We are aware of the wider capabilities (of entire outsourcing), it will make us internally more effective and improve those internal processes. It could eliminate major integration issues further down the line.

Q14/

- Improved customer satisfaction – overall pleasing.
- IT expertise at a cheaper price than it would take us to maintain personnel in-house.
- Able to monitor and evaluate specific "hard success" criteria.Creation of brand awareness and loyalty. Superior levels of customer services.

Q15/Through our legal dept.

Q16/Performance improvement – reducing costs and improving service.

Q17/Undergoing a re-think about this. We don't want to force through unpopular policies, but we need to protect our intellectual interests.

Q18/Reasonably good teams who meet most of our criteria. Ambiguity is always the big problem.

Q19/Not really from unions, but existing staff want some form of contractual obligation (in relation to secure employment)

Q20/Always in the "hidden" agenda. No customer is ever going to say "we will only award this contract to a large company," but--in reality--this is commonplace.

OMEGA FINANCIAL **814 231 7680**

Dan Mertz MIS Director Dmertz@omes.com

Q1/Yes

Q3/Extensive. Have been involved in outsourcing for at least 10 years.

Q4/Yes, we can leverage the price

Q5/Where we cannot keep talented people fully employed

Q6/We merged with another bank, so we are jointly using the incumbent supplier. However, we are seeking due-diligence for next contract award.

Q7/Not a problem, providing the other requirements were met.

Q8/Have had a delicate situation in the past that was resolved, but it is something that we need to be careful about. Existing staff working for a large financial services company would not be too keen to move to a smaller IT services company.

Q9/Banking is changing. It now encompasses a full range of services including insurance, stockbroking, etc,. We need an outsourcing company to take us into the future. We need improved service at lower cost.

Q10/

- Facilities Management and procurement.
- An efficient service that works 24 hours a day, able to improve business processes all round.

Q11/Not measurable

Q12/Still receptive to OS

Q13/Yes

Q14/ Overseen by our auditors. Specific cost reductions in operational overheads have been achieved; lower support and operational costs on the longer term.

Q15/5yr contracts

Q16/Yes only through experience

Q17/Not sensitive. Have a 3rd party for control and security

Q18/Very good

Q19/No effect

Q20/Is a factor, but decisions are "horses for courses". If your volume of business is such that it represents a disproportionately high % of the vendor's revenue, then this could be a problem in terms of risk and exposure.

ROCHESTER DEMOCRAT & CHRONICLE **716 232 7100**

Mitzi Bainbridge VP-IS

Q1/Yes

Q2/VP-IS

Q3/I call "all the shots".

Q4/Prefer bundled contracts, due to the cost ratio.

Q5/ No respone

Q6/They need experience of front-end systems and vast exposure to the newspaper industry.

Q7/I would not be unreceptive, but they would need to have considerable experience of our industry (otherwise we would not get seriously involved with them)

Q8/Has'nt happened yet; would put it down as unimportant at present.

Q9/Much larger stable nowadays. Greater choice of vendors, more experience, more extensive knowledge and also a great deal more business process outsourcing than ever before.

Q10/The type of contract is secondary to obtaining the correct skill fit. If we get the right vendor with exactly the right type of skills and service offering, we would ask them to propose alternative contract solutions to us.

Q11/No response

Q12/I am more relaxed about outsourcing.

Q13/Yes, if we can see that there are real beneficial gains for us.

Q14/No model as such, but costs come from the overall IT budget.

Q15/Shorter contracts carry less risk to us. Fewer things can go wrong.

Q16/No

Q17/Not too big a problem.

- Obviously the vendor will sign confidentiality clauses.
- The concept of partnership is very important to us and we would never enter into a relationship with a supplier if mutual trust did not exist.

Q18/Good, as per Q17

Q19/Not a problem

Q20/In some ways experience has shown us that the bigger the company, the more expensive the cost. However, they would argue that the bigger the supplier, the less the risk is to the customer.

AMPHENOL **607 563 5141**

Doug Lasher Systems Development Manager

Q1/Yes

Q2/responsible for all bespoke development and integration services

Q3/Have placed (awarded) many contracts. Also spent many years as project manager on large-scale outsourcing contracts.

Q4/No preference. The contract will reflect the service programme that needs to be outsourced. Contracts can have different durations and termination dates, so even if we wanted to bundle them, sometimes it is not logistically possible.

Q5/In the early days, outsourcing was done for commercial considerations. Nowadays, we have more sophisicated reasons; specific projects, core or scarce skills.

Q6/Technical ability, reputation, "chemistry".

Q7/Would not bother me; we have a lot of contracts with government bodies, so we are fairly competent in this area.

Q8/Not important at present

Q9/I would see over the longer term more of our IT coming back in-house.

Q10/Smaller development and maintenance contracts with 12 months duration.

Q11/

- If outsourcing is applied well, the results are positive and lead to improved profitability.
- The problem seems to be that it can be very difficult to objectively assess the impact of outsoucing.
- For instance, if we reduce headcount by a factor of X (as a result of the outsourcing), could we not have just reduced the number of staff anyway.
- If we increased profitability, how do we know that outsourcing had anything to do with it.

Q12/No, perhaps I am slightly more cynical. I certainly expect a lot more from the vendor, added value is a must!!!!

Q13/No, as per Q10

Q14/No

Q15/Short contracts of about 12 months

Q16/No

Q17/Nothing sensitive here

Q18/Current relationships are good

Q19/Not at all

Q20/Tend to use smaller local companies who are cheaper and keener.

MORGAN DRIVEWAY INC **219 295 2200**

Ryan Cox IS Manager

Q1/Yes

Q2/Manager of all IT

Q3/Senior role in all outsourced IT programmes

Q4/

- Large development programmes in place (and planned).
- There are presumed cost advantages in bundling the services, but it can be difficult to achieve a consistent level of operational service.
- We need to ensure that our commitments are met. The vendor supplying development services is not necessarily the best vendor operate the Data Centre.

Q5/

- We have no expertise or business knowledge of e-commerce (which is our most recent project).
- Different programmes are outsourced for differing reasons, ie, access to expertise is scarce, reduce the cost of delivery service, implementing corporate intranet, etc, but I suppose the bottom line is that the cost advantage must be prominent.

Q6/The usual criteria of relevant experience, quality of work, proven in field and familiar with our technology.

Q7/Not a problem per se. But they would have to meet our criteria in terms of project management experience, able to develop Web business applications and B2B consultancy skills. I guess that I would not want to be their FIRST customer.

Q8/They would be required to manage our contractors plus recruit new skills. Transfer of existing staff to the outsourcing company would be subject to discussion.

Q9/New philosophy of achieving excellence. Vendors now have a proven track record in delivery and operation of large-scale projects.

Q10/

- Able to utilise the best technology.
- A vendor who can build a good team and be good at communications.
- If they can apply themselves intelligently and support our objectives, then the type of outsourcing contract will be of secondary importance.

Q11/

- Outsourcing is already established and successful.
- The nature of the product is changing more towards E-Business and Call Centre technology.
- A quick response to new requirements and greater emphasis on managing the relationship.
- If vendors can offer practical and sustainable business improvement, then their future looks reasonably secure.

Q12/We are now looking for a partnership on the latest technologies and software solution as opposed to just getting a "low-cost" service.

Q13/Yes, but with the effective management of risk and how it will impact on our vision and business strategy.

RAN OUT OF TIME, SO WE JUMPED TO Q20

Q20/We prefer a recognised and credible company, but stay clear of the major names because of cost

CYBERGRAPHICS **901 369 4400**

Jerry Young Director of Business Systems

Q1/Yes

Q2/Overall responsibility for business processes

Q3/Senior part of the selection team.

Q4/No preference

Q5/Use consultants for special projects.

Q6/We normally select 2 vendors for shortlist. After that we consider technical merit and business acumen (and how they demonstrate their expertise)

Q7/Would'nt matter

Q8/Not an issue

Q9/

- The workplace has become more mobile with advanced communications and the use of WAP. Therefore your own IT staff do not need to be resident inhouse.
- I don't know if this will increase or decrease the use of outsourcing long term.
- Also there is an increased trend towards the use of Offshore service providers.

Q10/IT and business consultancy, project management. We provide the resources but the outsourcing company manages them.

Q11/Mainly in systems development and training.

Q12/not really.

Q13/No

Q14/No

Q15/Shorter contracts

Q16/You have a feel through experience. Data centre and transactions based outsourcing is getting less expensive. Consultancy, BPO, bespoke development is (or has been) increasing over the last 10 years. Some specific skills such as Oracle, SAP, Java, Active X are extortionate

Q17/Very sensitive

Q18/ No responses

Q19/None

Q20/No real influence. They must demonstrate technical ability and have track record.

MONTEFIORE MEDICAL **718 405 4397**

Ken Kinkopf Director of IS

Q1/Yes

Q2/IT Director

Q3/Recently handled the outsourced implementation of SAP

Q4/Yes, but must be fixed price contracts.

Q5/Not the objective of outsourcing for us. It was the speed of actioning things – we needed to implement SAP "soup to nuts" and increase software development speed and quality.

Q6/We have a shortlist including people that we have worked with in the past. They submit their proposal and we look for the best fit.

Q7/Not a problem

Q8/Not important

Q9/More companies are now outsourcing. Also the variety and choice of what can be outsourced has changed.

Q10/Small defined projects.

Q11/No response

Q12/No

Q13/no

Q14/We obtained a high value economic return in terms of implementing a very sophisticated system. The benefits will be obtained internally (in that the wider implications would have been considerable, had we not outsourced it).

Q15/Shorter contracts. Cost and control are the main reasons

Q16/ No response

Q17/None beyond what you would have in any other IT application service contract.

Q18/Good

Q19/None

Q20/It would have some bearing in that you feel safer with the bigger companies. It did influence us in that we wanted to use an SAP Logo Partner, who tend to be the large IT service providers and consultancies.

CYNDC1

Questionnaire No. # 1

Printed: 01/08/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❒ Vendor ❒ Telephone
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: Litton/PRC

Address: ____

City/State: ____

Zip: ____

Telephone: ____

Fax #: ____

WWW

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐

Interviewer Initials ☐☐☐

Interview Date. ☐☐|☐☐|☐☐

QC Initials ☐☐☐

QC Date ☐☐|☐☐|☐☐

Data Entry Initials ☐☐

Data Entry Date ☐☐|☐☐|☐☐

Company Type: ____

Annual Revenue: ____

Employees: ____

Total IS Budget: ____

Total # IS Staff: ____

Respondent(s):

Name Mac Oxford Title: VP - Seat Mgmt / Mark Bus Dev

Phone/Ext. ____ Email oxford_mac@prc.com

Role in Project: ____

Referrals:

ref. Hal Wilson

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- ❒ Federal Government
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

____

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

   yes
   ____

   Collect related demographics

2. What is your role? led bus devel efforts for corp - also dir of ops

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

   def or gov

   Comment project mgr rights to him (capture / mgmt)
   OS = ~~[illegible]~~ $175 mil annually staff augment
   (25-30%) Asset takeover

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

   Comment * ISEAT mgmt * network mgmt * storage on demand
   * help desk OS * appl. mgmt (we own)
   many public sect - 95% federal. operate

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

   Comment effort to diversify → sect mgmt state / local would attract - storage act [illegible] comm market

   Asset takeover - only one contract $15 mill (GSA sect mgmt)

   STORAGE on demand - few $ mill → expect growth

Jim Fry - head

decision to go into comm market?

- look at dual use technology
- tried storage bus over past year -
- found that our skill set appl. to comm clients -
- see better exp. potential in comm

how transfer?

- we are 7-8 yr struct on comm basis (?)
- website diff. from outsource prc. comm - spend

effort not to push fed exp.

- pursue OEM part in both fed & comm. market
- want to fill niches in OEM lineup

- avoid compet with major IBM, CSC, EDS, etc.

Barrier to entry? fed bus

- name recog - trust (Brand franchise)
- dep more on better name - bus contact
- compl diff. way to generate bus Ex. fed [illegible]
- ie. ex. fixed price ~~contract~~

CYNDC1 desktop is labor intensive Questionnaire No. ___________

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments Ex Sentiment → efforts to get foot in door is commodity → leads to better margin < networks, STORAGE

Better margin → do more remote work in network & storage.

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments don't need to commit moving to common market → can use GM capital, many sources of finance

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

(2 level) Finance Risk Staff B-Asset ↑ of so, also out of business

Comment Key capital risk? yes, but risk of good partnerships

failure not on hardware, will be necessary service

– exp. on cust will almost never ask us to put yr go – to will buy out.

8. What important changes do you see at work in the outsourcing market today?

Comment:

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments network ~~OS~~ OS little BPO –

remote STORAGE

↓ desktop

would enter market with low margin (6-8%) profit

Comm = 1-3% ≈ 2%

– ~~(T)~~ hope to move to 10-12% profit.

Fed

own group = 20% of Rev.

Staff TRAINING probs?

- not so critical to own group.

(Anne - diff to personnel

Biggest obstacle?
to TRANSITION -

- (1) Comm wanted broad diff to pick vertical
identify prod. custm

(2) sales staff → need new, comm oriented.
Sales staff

(ii). Systems for comprt low cost ⇒ high margin
exp. for command.

- SLA will vary.
- service level - fed → expectations are increasing

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments help desk ~~storage on demand~~ = cust. who doesn't want to buy new storage, want vendor to put own equip on site & operate

11. What process do you use for computing the cost of contract bidding?

Some comm verticals – banking, utilities (gas), chemicals, health care, entertainment
key to success? data/storage farm – done at remote site → less competition: we want front in one door, out remote storage

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

Sophisticated models?

Comm market → understand that vendor/cust have a partnership → cust expects vendor to be profitable
– more diff. in Fed mark → ~~[illegible]~~ easier for change to cost reflect money in Fed market
FAR – used as excuse not to charge

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

no market for model for est profit –

Yes – generally high market. → name recog will cost $$ → late → cost lower
~~late not same exp~~ entertainment – profits in Fed, higher in comm.

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

15. What is your policy toward dealing with unions? (How important?)

Comment ____

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment ____

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment ____

____

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ____

____

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment

____

____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

____

____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ________________________________

Phone #: ________________________________

Email Address: ________________________________

Thank you for your time and consideration.

Questionnaire No. #2
Printed: 01/08/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❒ **Vendor** ❒ **Telephone**
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: Outs Institute
Address: ______
City/State: ______
Zip: ______
Telephone: ______
Fax #: ______
WWW

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐|☐☐|☐☐
QC Initials ☐☐☐
QC Date ☐☐|☐☐|☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐|☐☐|☐☐
Company Type: ______
Annual Revenue: ______
Employees: ______
Total IS Budget: ______
Total # IS Staff: ______

Respondent(s):
Name Jose Cunningham Title: Mang Dir + VP Global Sales
Phone/Ext. ______ Email dcunningham@outsourcing.com.
Role in Project: ______

Referrals:
1609 16th St. NW. — [home office]
Wash DC 20009

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- ❒ Federal Government
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

OS inst? Nedin?

- Private -> since 93
- own URL - outsourcing
- purpose: want to be primary resource for outs. -> prof. assoc.
- most Forbes, etc. print studies
- central clearinghouse, host events, together with DCF
- outs. Index
- no paid membership / DB of 24,000 Buyers, Sellers + "influencers"
- income: < consulting / marketing assistance
- size of staff 18 people -> Frank [Frank] Smith M. Corbett
seeking VC funding.
- Accelerate treated as a dotcom startup [Portal]

Typical 8-15% of deal spent on marketing

OS rec. $ from trans. fee for winning business to vendors [6 months]

Introduction

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A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

____

Collect related demographics

2. What is your role?

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment selling IT OS since 1982 – BDM – State contr – Fed Servi

Slotkin Unisys → ATT Sol. → CapGemini → out – PSINet →

– also e-com task force [E+Y Consult.] Reg.

3a. Also, what proportion of your company's business, if any, is the U.S. federal market.

Comment

Import that Fed + Commer OS mgmt totally separate

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

Bechtel Fluor – Site mgmt

Ikon Xerox Pran. Cms

Fin Serv, Fac mgmt? Manuf. (Signal. Supply Ch.)

Comment

IT OS = 50% of outs
– 2nd largest → facility mgmt, RE
– HR mgmt

former Pres of Unisys Federal Services

Victor Millar – co-founder of Andersen Consulting

now CEO of VC fund – Columbus Newport

started
9/(?) Slotkin trained in fed. sector → Univ. Dep. fed. gov.

Benefits of Fed Mark. exp

know all details → (1) Program management experience (greater under fed. than prof.)

ex. B-5 profit (2) Books are open to insp. Fed audit (open)

(3) rigorous Min margins
- under in private → unclear where profit is (until) ...

(4) Good exp [illegible] for Fed ag. reviews

[FIGM a great benefit]

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments moving more upstream → BPO. showed offer more complete services

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments Deals are down between people → Sol. & mgmt. critical, proj. mgrs are pre-selected - deals. very exp. → comes from Fed exp

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

methodology comes from exp. project mgmt. [illegible]

Comment

capital → not an issue → leases mgmt → vendor & committed → avoid borrow. (signif to mgmt.)

very important - 7 day pool [illegible]

8. What important changes do you see at work in the outsourcing market today?

Comment: cust/vendor → jt venture, least import. to Sol. Find Anchor client

structure sig.

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments

fed/comm OS bidding?

fed - long contr. - very detail

comm → smaller contr SLA with details, as bus. changes → change appendix

ex EDS was good at contr.

Comm side would benefit for fed exp.

Grow to present Fed exp. to Comm. buyer
Survivors who have moved from Fed to Comm
→ CSC LMS Litton
- strong, generally making deals happen

- how to overcome resistance?
explain what you did on Fed Sector →
scale - scope of project
- CSC - labor intensive ... exp in Fed.
- in Comml - 200-300 staff transfers - in Fed
gov - these are very common
- lack of clients not knowledge < should be able to leverage Fed.
what are our people doing

- avoid splashy advertising
- speak at conferences
But need new sales team → build relationships
Fed: vendor/gov usually contentious
Comm: greater speed, new developments, clout of top exec

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

    Comments

    ____

    ____

11. What process do you use for computing the cost of contract bidding?

    ____

    ____

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

    ____

    ____

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

    ____

    ____

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

    ____

    ____

15. What is your policy toward dealing with unions? (How important?)

    Could be an issue
    should try
    to avoid.

illegal to ~~entertain~~ other entertain in ~~Comm~~ Fed.

Comment

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment

17. What changes are you seeing in customer motives for outsourcing IT?

Comment

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ____________________

Phone #: ____________________

Email Address: ____________________

Thank you for your time and consideration.

Questionnaire No. #3
Printed: 01/08/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❒ **Vendor** ❒ **Telephone**
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: CSC
Address:

City/State: Fairview Park, VA
Zip:
Telephone:
Fax #:
WWW

Project Code/Catalog No. ☐☐☐☐☐☐☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐☐☐☐☐
QC Initials ☐☐☐
QC Date ☐☐☐☐☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐☐☐☐☐
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

Respondent(s):
Name Wayne Kelly Title: Asst to Pres. Fed Sector - Milt Cooper
Phone/Ext. 641-2570 Email wkelly@csc.com
Role in Project:

Referrals:

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- ❒ Federal Government
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

Introduction

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A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

   ____

   Collect related demographics

2. What is your role?

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

   Comment ____

   ____

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

   Comment 25% – down to 23 → target at about 25%
   public sector = 50 county, State of MD, PA, NY,
   est. 28-30 total US public

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing? HC.
   [illegible] Jim [illegible], Fin, aerospace, def.

   Comment ____

CSC – success in fed, less success in fed mkt. w/ Gen Dyn. contract.
– Key to success: strong Prog mgmt, SW devel. ability to deal with complex tech, security

client serv. / etc.
- 18 yrs exp - Fed = 70% of CSC bus. - OS type
+ FAC. mgmt.
- also exp in knowing client of cust - Fed agency
- Sight of comm side → transfer of expertise → seeded
- Transfer to Comm market?
- Rigor in prog mgmt, ability to deal with complex issues discipline [Carnegie Mellon model] → TRANSF to comm. was cogent → DuPont
-

Companies lost e-comm capability — need partners — become partners.

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments client wants more comprehensive [ex. LOGMT — army] first fed OS — would transfer of [illegible] servants → modernize trans proc → world. entp arch — SCM

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments Trust very important Fed ≠ various fed clients must understand client's business — Provide better value proposition

understand agency mission and leadership

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment public co — need to provide stakeholders with ret. → more [illegible] on risk. Exp. lets us gauge risk.

— we have a sept — world / → proj. mgmt. to compute cost / profit.

8. What important changes do you see at work in the outsourcing market today?

Carnegie Mellon SW develop → leads to new business

Comment:

— need rigorous process, ex. Regis engine, air traffic control, NASA

Fed: retirement [illegible]; various: we see as import. allies ex. IBS, Proj. Mgrs = 47 yrs exp → ongoing TRAINING ⇒ CO TRAIN in-house also — need to recruit outside staff

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

? OS = 38% of total [illegible]

Comments Fed appl mgmt Comm (bundling)

interest in sol. that helps bus.

[illegible] Desktop — ~~costing~~ more val in Comm.

* last 3 yrs → CSC very well posit. to leverage comm capabil to Feds → if not, wouldn't ~~have~~ won IRS, ARMY Logistics Contracts

Sole sourcing?

- if you have a "solutions provider" -
- work done under task orders → these are not necessary competitive

Fed Express - talked about for some time -

---

* exper. with SLA very important → perf.-based CONTRACTING

* Imp. to work closely with client.

---

market changes: ex base generation, 20 yr exp

unions have great political power

new admin?

more $ -

Sources DOD

reality will set in

more going to privatization!

nts. certain functions

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

    Comments

    ____

    ____

11. What process do you use for computing the cost of contract bidding?

    ____

    ____

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

    ____

    ____

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

    Lots of ~~text~~ task order bus, smaller deals — common bid. market groundwork etc. except exp.

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

    not out of a barrier — if qualified, CSC has exceptional record on transfers, Army Wholesale Logistics — 1800 fed transfer (hired [illegible] 30,000) → spl posit.

Protests? very few fed. protests, This was CSC policy; we protested Boeing deal because award based on best value bus — best value criteria were unclear

15. What is your policy toward dealing with unions? (How important?)

9% of care low — needed to settle the issue

Comment ____

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market?
What would you need to do to become ready?

Comment ____

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment driven by value potential; cust doesn't know how to cope with tech → doesn't know how to use it → need best solutions →

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ____

____

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment

____

____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

____

____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ______________________________

Phone #: ______________________________

Email Address: ______________________________

Thank you for your time and consideration.

Questionnaire No. # 4
Printed: 01/08/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❒ Vendor ❒ Telephone
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: Lockheed Martin
Address: 12506 Lake Underhill Rd

City/State: Orlando
Zip: 32825
Telephone: (407)-306-1762
Fax #:
WWW

Fed Bus Sever Entity.

Project Code/Catalog No. ❒❒|❒❒❒|❒❒❒❒
Interviewer Initials ❒❒❒
Interview Date. ❒❒|❒❒|❒❒
QC Initials ❒❒❒
QC Date ❒❒|❒❒|❒❒
Data Entry Initials ❒❒
Data Entry Date ❒❒|❒❒|❒❒
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

Respondent(s):
Name Ned Cooper Title: VP - STRAT. Develop
Phone/Ext (407) 306-1762 Email ned.cooper@lmco.com
Role in Project:

Referrals:

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- ❒ Federal Government
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

____

Collect related demographics

2. What is your role? (PHS)

3. Please indicate the nature of your experience with outsourcing (IT or otherwise). enterprise sw - partner

Comment look after alliances, Started in insurance → dev

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

Comment Zero federal, 100% commercial

LM → integ Bus Sol and comm → Fed IT outs - ISS - and Sys Sys - fed Serv. Ward

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

Fin Serv.; utilities (trans, dereg. dereg of power), cred. inst. manuf.

Comment less than $ 1 Bill

LM total revenue → OS small 20 - $ bill ext.

Serv OS co.

Comm 50%
Fed 50%

BPO → state & local Gov - little for comp

IT

Trans Proc - ? no

$ 400 mill

We are building a - Mrs Center -
moved to remote ops mgmt -
for clients who don't want to own

- also, just sell sys. solution like SCM

- we don't build ahead of more (with unused capacity) - want to stay just about

- exp in US & South Am

(1) Outfitting/unused cap. risk -

- Fed → Comm - Schedule
cycle starts in Comm (ex Fed - 8 yrs)
Comm deals → 120 days ex. Gateway

Fed Mgmt:

OS like M&A

- Gov is better buyer - know how to deal with outs
service - has senior exec mgrs. Comm → OS often given to junior IT person.
- reject deals if not. reasonable - ex if
Co. has never done OS, doesn't use consultant or
buyers. → chance of loss of deal is higher → quality of RFP is lower

 PAC mkt 81 / IT utility Best growth in BPO

Questionnaire No. ________

– customers are selective in IT

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments both – chosen not to org. around vertical, → we target large organizations; co wants to buy service → don't want to transf assets + facilities

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other? depends on who makes decis? – Bus Gov → BPO Bus Process by the client

Comments Somewhat fin, mainly ORG.

need $ – cap. int. bus; most cap outlay is lease – (ASP) little risk (or equip can be reused)

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment

Yes – need $ to pay. OR, you do remote deployment → still exp. staff

8. What important changes do you see at work in the outsourcing market today?

Comment:

Fed → move away from custom (bespoke) to common OS – firm ~~+ equip.~~

Govm – consultants are adv. brokers → spend 5% of OS deal in manage.

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments would like to do high end high value added ~~e bus (but usually from the TRANSACTION) – usually broken in pieces~~

– Infrast. mgmt → still profitable (no differentiation!)

need vendor management skills

~~have to separate co. for compet.: don't pursue an oblig that → hard for 100's of mill.~~

IBM, EDS, CSC –

We are big enough to do and, but can give attention

IBM - no deal is big for IBM - even $1 bil

}10 - 500 mil - our sweet spot - com

anyone on agenda

- we are more accessible - full team funding

ADV

name recognition

Delivery skills - Serve, Fed, Com - tech talent

(we can get ahold of staff from anywhere

w/i LM, or outs. -> use formal

subcontract, intercomp transf

or hire internally) [cause internal conflict]

- we hire off the street

- we have strong chief tech officer -

Bus Acq Skills - these are transferable -

Fed Com

- diff in Finance & Acct Syst -

nomenclature is different -

- use diff. staff, can transfer (not all are

successful - more nasty -> Com to Fed

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments

____

____

11. What process do you use for computing the cost of contract bidding?

in-house model used.

______________________________ ex early year - lower margin

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

need to try to take business case into account - with year deals → 2 of compl. accounts - some use pricing out. we make bid pricing based on previous total, est. work

most TRANS - part of OS mark.. 12 player unknown

13. How burdensome are the overall ~~sales & marketing costs~~ associated with winning new outsourcing contracts? (Federal vs commercial?) ex Fed

Comm prop are cheaper FAR $750 deal - prop. took 3 yr.

we spent within $

$350 mil Comm - 12 ppt slides (must know who decision makers are)

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

we don't take Gov wage bus → is ~~force~~ de...

OS Fund OS Exch.

JBI TRANS. Part. - KPMG

went to conferences → struct. TRANSACT

15. What is your policy toward dealing with unions? (How important?)

Fed - ex Mitre pays RFP

want to do deal big enough
to chin. small company
— above $1 bill — only a few players

1) — don't need marketing
— don't need 100 sales
— only need contact to
visit these few

zero to $1 bill in 4-5 yrs

ex Exact → zero to $3 bill in
one year — no sales force

Fremont large ISO — single large
contract annually.

— can get in big & quick
— no geo sales force —
price premium commands premium — don't
have to spend a lot
— same cost to chase dozen deals

to what extent are customers price sensitive ?

Comment [illegible] Fed proc — [illegible] prices →

[illegible] [illegible] [illegible] target [illegible]

[illegible] → if price important you are [illegible]

16. How ready is your organization to bid on contracts in the federal (or commercial) market?
What would you need to do to become ready?

Comment ____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment used to do it for cost svs — 1980's + became talent [illegible] today — strictly on time to market (act has no other act)

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment important to size of deal — spending related to % of revenue — but all of our deals come to consult ($2500 per day)

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment ____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment ____

Consultants are trying to set up new marketplace

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ______________________________

Phone #: ______________________________

Email Address: ______________________________

Thank you for your time and consideration.

Questionnaire No. #5
Printed: 01/08/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❒ Vendor ❒ Telephone
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: CSC (V)

Address: ______

City/State: Fairview Park, VA

Zip: ______

Telephone: ______

Fax #: ______

WWW

Comm outs. expert.

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐

Interviewer Initials ☐☐☐

Interview Date. ☐☐|☐☐|☐☐

QC Initials ☐☐☐

QC Date ☐☐|☐☐|☐☐

Data Entry Initials ☐☐

Data Entry Date ☐☐|☐☐|☐☐

Company Type: ______

Annual Revenue: ______

Employees: ______

Total IS Budget: ______

Total # IS Staff: ______

Respondent(s):

Name Jim Selwood Title: Dir of Bus Develop

Phone/Ext. 703-641-3065 Email jselwood@csc.com

Role in Project: ______

Referrals:

______

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- ❒ Federal Government
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

CYNDC1 **Questionnaire No. ________**

Introduction

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A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

____

Collect related demographics

2. What is your role?

Facilities mgmt — BPO. Fed done elsewhere. BPO or commercial done here

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment Sr. mgmt. the "capture side" of OS. We have centralized all capture activ. more plus — diff. from Fed OS. Bring in vertical expertise, ex Fed, Health C., Fin Serv.

3a. Also, what proportion of your company's business, if any, is the U.S. federal market.

Comment ____

____

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

Comment good opps — Fin Serv. — banking, ins., other — mid 90 to pres a little act. (Y2K); consolidation, but depressed by Y2K. FS/banking opportunity — now a sideline OS standardized process — Appl. mgmt (app & infra). Cust. want vendor to bring data center, run & operate. Owned use hardware for colocation & do work for other clients

Fin Serv

(4) Cust. want to grow → exist. infrast. can't support growth, esp. people and facilities.

- on Fin Serv coast HQ in US, global but US workload
- Offshore App - India? proposed yet, not implemented

(2)

Manuf. - ex. (electronics / discrete -

We see more & more global oppty —

now co. - US → global operations

- Size of deals larger, number smaller

CO w/ $5 bill → high → Fort. 500 - global co — are US mm of US oppty - as well elsewhere also

- mid-tier ($1 bill / $5 bill) ex. J.Crew < 20 30 IT spending

- can't get resources

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments we do web hosting, Appl. mgmt and — ex HC, RM lending provider process → last years → trend to downmarket

— computed all the time

all are strengths

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

all important

Comments name recog. → should spend more? hist. prosp. spend w/ growth

CSC pitch to the thought leadership → need to get door open to CSC brand

Fed market is totally different

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment It is not a problem (for CSC); ex. CM, could be successful — but can't succeed as uniqs

ACS CSC — not at disadv. — WorldStore (storage). or Exodus — startups — hurt to use equity.

8. What important changes do you see at work in the outsourcing market today?

Comment: ① global capability — ② more midmarket

9. Top down, which types of outsourcing can you do most profitably? (Reasons?) 05 — best value — best at total (infrast. → desktop + appl. — legacy in development of new)

Comments

— become business partner — ex Airport Future time

Demand management (business benefit) — end of all apps

ex Kronos

ex Market — SEI cap. mat. model; best practice ... level 3

TRANSITION — fed to comm: took from fed exp — the discip. + ongoing process mgmt (10 18 yr exp) — we adapted it to comm market → use same process globally to do business ex

ENG + Global process — mission critical Fed exp.

Partnership takes time → must work your way up → no shortcut to "trusted advisor".

— V

but Parts might - don't respond to RFP w/o - get + know client first

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments

depend on Granularity to spread word about vendor

11. What process do you use for computing the cost of contract bidding? we do sol- develop design sol → cost of implement then price → we do cost build up → (others do cost savings to promise)

- most contracts → base charge for base volume - (build variability into agr in advance) - vol ch. before contract signed

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

13. How burdensome ? are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

Bus develop Costs higher on Comm side - more travel.

Fed. all in single locat; fed proposal prep costs higher

- we manage costs carefully → all exp carefully considered - don't let be burden

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

never happened - high acceptance rate of offer.

Secret to success? good people - welcoming - there has always been a flow of staff - pavilines can advance -

15. What is your policy toward dealing with unions? (How important?)

have some - CSC manages union agr → they stay w/ client

IBM - AmEx — small business alliance

Questionnaire No. ________

Comment ________

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment ________

17. What changes are you seeing in customer motives for outsourcing IT?

Comment 90's — cost → then lack of resources → will come back to cost → need standard of environment (will come)

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment multi-tier we are pursuing — diff model → ex: Lenovo… is diff. want specialize go to top decision maker

$1 bil
Fort 500 > $5 bil

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment fed heritage of security: work for classified environment. This was deal clincher at Natl… concern that management will suffer inability to bring bus back

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment ________

Ratio: scale "pursuit model" — marketing as % of TCV

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Name/Title: ______________________________

Phone #: ______________________________

Email Address: ______________________________

Thank you for your time and consideration.

Questionnaire No. #6
Printed: 01/08/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❒ Vendor ❒ Telephone
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: Kenne
Address: Ten City Sq.

City/State: Boston
Zip:
Telephone:
Fax #:
WWW

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐|☐☐|☐☐
QC Initials ☐☐☐
QC Date ☐☐|☐☐|☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐|☐☐|☐☐
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

~~DIA~~ (617) ~~577~~ - 241-9200

Respondent(s):
Name Tim Barry Title: VP - outs - Com + Fed
Dir - North Carolina - Switch (919) 567-7593
Phone/Ext. 617-241-9200 Email Timothy_C_barry@kenne.com
Role in Project:

Referrals:

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications ✓
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- ❒ Federal Government
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

referral to: Larry Vale - VP inv. relat. - Tony Perez

Tel. 241-9200

CYNDC1 **Questionnaire No.** ___________

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1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

____

Collect related demographics

2. What is your role?

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment indust – 20 yr, consulting Bkg. Wang → 10 yr ago – Keane → managed OS projects → Corp – int. & ext clients; OS Pract. sales & ~~dev.~~ delivery.

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

Comment OS = 50% [Comm = 80%, Fed = 20%] – direction? might mix: Fed unit = 10–15% of total business.

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

Comment Fed (State & Local)

– Keane opty in Fin Ser, ins, Manuf. (utilities → possib. but nominal)
Comm

Telco – perm.

Some consultants ? charge "success fees"
for bus (interest → try to facilitate
deal → Everett → become
monetary exchange - go.

- clients aware of cost

- consultants - don't take
resp for client decision

(6) - success in promoting our differentiation
may produce reluctance → sometimes
cust. insist - influence

- client wait
- ST3 visible at ASSOC, industry conf.

use of consultants?
2 constellation. need for good scale & market
- proc. can be very useful → strong rep with
| Event
| Bankers
| TPI
Them → pers relationships
, Outs. Inst.

- need to convince ? of our value → 100% refer → co
play / constellations

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments much high comfort – OS large dept. function → take for mgmt (with partner for this)

6. How would you categorize the most important barrier to entering a new market, financial? No Technical? Marketing? Organization? Staffing? Management? Other?

Comments name recog. & reputation: $100 mill Fed unit key STRAT → partner (govt mgmt SKR); need to infl. industry funds

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment don't need govt $ – most of any staff – build cost into deal; even infra. data center segment → vendors continued to do it (has been commoditized – sign. ch govt margins)

8. What important changes do you see at work in the outsourcing market today?

Comment: govt getting more more sophist → using outside consultants) OS more accepted → pres. to improve SLA

Chall: bus. value → mktg & measurement – fed market has taken more diversity → comm. catch up – legacy maint = commodity (profit → not attr)

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

high margin high value Comments | conduct of serv – new devel + maint. govt | also planned based, STRAT & plan

| data cent OS NT

Special – govt mgmt, devel OS cont devel → e-sol.

Plan – commodity, STRAT. Based – e-sol., web-enabled
Manage – full govt OS, devel one data center mgmt – some Fed desktop (

(1) ... (2) ... → Staff on site or nearby remote

(7) have won deals in SDR of HR
Solution. strong. SI

(8) — wants to be in both markets?
Fed. wants to commercialize solutions
Comm cont → not sp. registered with Fed
CMM compl. → appre goals/methods/
process.

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

    Comments

    ____

    ____

11. What process do you use for computing the cost of contract bidding?

    ____

    ____

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

    ____

    ____

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

    ____

    ____

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

    ____

    ____

15. What is your policy toward dealing with unions? (How important?)

Comment ____

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment ____

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment ____

____

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ____

____

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment

____

____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

____

____

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Name/Title: ____________________

Phone #: ____________________

Email Address: ____________________

Thank you for your time and consideration.

Questionnaire No. 7

Printed: 01/08/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❒ **Vendor** ❒ **Telephone**
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: Rz Ofen
Address: 801 Crstl DR

City/State: Linthicum, MD
Zip:
Telephone:
Fax #:
WWW

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐|☐☐|☐☐
QC Initials ☐☐☐
QC Date ☐☐|☐☐|☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐|☐☐|☐☐
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

Respondent(s):

410-981-6089

Name LARRY Phillips Title: SR Bus Mgr. – Dir Bus Devl (NSA Prog)
Phone/Ext. Email larry.m.phillips@hrb.com
Role in Project:

Referrals:

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- ❒ Federal Government
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

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A. Recipient Qualification

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   ____

   Collect related demographics

2. What is your role?

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

   Comment has been obs + partic. – gov agencies at Raytheon – [illegible] Goodfellow, co-others (all on Fed side) no comm exp.

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

   Comment Raytheon – [illegible] bus – less than 5% → all Fed. 05

   ____

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

   Comment IT outsrc overall great potential (fed or comm) – focus on sp. intellig agencies – all watching Goodfellow

Supercomputers will be outdated in 4-5 years.
- now parallel processors → now better
- (public → within NSF + 1.5 year program. Based on privatization funds)

- now only a workforce reduction
- other agencies looking → may go back to privatized model
- NSA has internal public, funds.
- long lead times makes trad. stuff outsource out of date
- push decision making process too slow

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments If privacy, cust. NSA ... procurement to keypayment (privatiz to outs)

OS = people → given to vendor & that employs them as before - better

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments all the above - fed / intell. → sec. security barriers - catch 22 - to have empl. with cur. clearance - must have contract can't get contract unless already cleared

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment no probl. → OS no prob; if privatization → no constraint - ~~award offer to incremental/buy out with profit of bus~~ savings (this avoids actual cash outlay)

8. What important changes do you see at work in the outsourcing market today?

Comment: Anti-outs? maintain static contracts will lead to disaster - A-76 → ..., cost processing to degrade (Cognizance fed report); fed empl jobs security cont. import probl. - skills shortage and grow more acute → doesn't want to wait to outs. fed cust incapable of foreseeing Tech develops at rapid envir.

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments

(simplify ... procurement)   AP - "private" more profitable (pos. & ...)

(E) ev. company that does fed bus - wants comm. lucrative comm market with more competit. (cutthroat) - sim fed staff more collegial - comm vendors - more profitable - no GSA schedule - $75 fed → $200-300 per hr. comm

(c) Obs. – marketing ✓ sales counts $$ ⇒ new
sales force → contract / prospect –

convince comm cust to do bus with comm.

– ~~not~~ very diff to break into comm market → must
emphasize tech skills, transf. technology.
– moving – comm tech doesn't care about your Fed
– comm cust. perceive their tech req. to be on Fed
tougher.

– Fed gov doesn't know how to write eff SLA "
ex: help desk = SLA that gov wanted put out → every call
ans with 10 sec of ring – vendor rated on speed
customer conv. ; No metric for effectiveness
of answer. (vendor get working to answer → still
get paid)

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments

____

____

11. What process do you use for computing the cost of contract bidding?

Breakeven to the 1-2 yrs into contract → can benefit from economy of scale
organized at front up front can profit must greater
~~FDIC~~ → over costs — spread to market $$
(Fixed for x Fixed dur.)
cost plus

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

Sophis. model exist → can track profit

____

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

Market & selling → costs main proposal diff. to contained
- Keeping such costs at remainder → in comm side? market
* costs must be better focused; need target segments (careful consid cons... evident comm... cust needs)

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

- no probs. So far - at end of contract, any guarantee is only for 2 yrs. → need to weed out slackers
- large # of fed workers no compel dem to compete in comm market

15. What is your policy toward dealing with unions? (How important?)

(Parts of benefits — derive built into contracts)

Comment ______________________________

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment ______________________________

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment ______________________________

____

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ______________________________

____

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment

____

____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

____

____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ______________________________

Phone #: ______________________________

Email Address: ______________________________

Thank you for your time and consideration.

CYNDC1 ✓ Questionnaire No. #8
Printed: 01/08/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❒ Vendor ❒ Telephone
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: ACS Gov Sol. Grp
Address: 1 Curie Ct.
Rockville

City/State:
Zip:
Telephone:
Fax #:
WWW

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐|☐☐|☐☐
QC Initials ☐☐☐
QC Date ☐☐|☐☐|☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐|☐☐|☐☐
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

Respondent(s):
Name Howard Green Title: Dir - Bus Devel. - Civil Progs
Phone/Ext. Email howard.green@acs-ssg.com
dot
Role in Project:

Referrals:
Jean Murphy - VP Bus Develop - (Fed) (Com)
Susan Grenache - VP App Sol. - Phoenix
Suzanne
Tel. [602] - 760 - 1802

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- ❒ Federal Government
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

home tel
Tel [520] 458-1488
Nancy Minn
X1712

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.) Fed Rev Total

Collect related demographics 3 in Civil Sol — IT Sol = 300-400 mil, ACS Dept = $100+ mil, Bus App Syst = $100-200 mil = IT (Civil / DoD) Fed / State ch

2. What is your role?

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment Pres – 2 year at ACS. Prior at RUL/Wang → captured Mgt Svcs Mgt and GDIN. Most exp in DoD SSDs – elect warfare. no comment.

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

Comment Fed Civil Focus 2/3 Comm Total Rev.

#4 in US, 1/3 gov ← all OS

$2 Bill ann in OS

B. Priority Questions

State & local = gov sol ($600 mill. ann — + other = gov + stat & loc $700 mill

4. In which vertical industries to you see the best growth potential for IT outsourcing? Fed

in Fed Comment target agencies that best match goals. (where can compete technical – which have budget? where level playing field)

Top category in netw security – NASA – biggest integr contract – $400 mill ann, seat mgmt = 300,000 seats under mgmt.

(6) Barriers to entry — Fed

- must be incumbent at agency to get into door
- hard to get to know people - can't walk the halls
- access is issue
- change in contract. policy - good, but makes easy to renew incumbents
- Govt doesn't want to do full competition
- Select contractors are onerous —
- Streamlining = award to incumbent, diff to unseat
- policy of size not top tier, not small minority "middle is tough" → want sole source
- no boom in Fed spending - Dep. Network?

Barr - Fed to Comm -
* marketing. a diff. animal - need new people must have contacts
- way to enter market → Buy a company → need a window, a platform
- comm system have brought comm clients to visit Fed → led to deal close

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments a wear Services co → want to move up; provide bodies – want to sell solutions

want to build in ODIN

ex: Sent mgmt (GSA – not everything, ODIN – NASA – many centers, etc did compet – multi vendor, mult civil servants

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments works closely with commercial side – compare notes → if marketing cards would benefit from cooperation. Comm culture provides best prac; fed provides → prog mgmt, fed disc → methods

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment litton – biggest contract, $10 mill – at ACS, olma 2

proposal money – can team with leasing companies – finances – more in IT world, not defense. In IT, top tier → no prob. lower tier →

8. What important changes do you see at work in the outsourcing market today?

Comment: * changes in fed. contract method → harder to win bus. from incumbent

– aggregat – big reg into megacontracts → hurts medium & small contracts (need to team) → prime select. to share

Prov OS = people

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

NMCI = size? This was drive quickly.

DOD = PC-base no custom system

Comments least ① infrast serv – sent mgmt, desktop networking – soft develop staff serv ②

Sw develop → faster

Profit = how mgm how strategize

if team → much lower prop. prep costs, lower inc pipeline

not much enf of small bus. enforcement

"e-company" → big effect on fed mkt → Wall St. decides what stock is worth → is losing steam

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments

11. What process do you use for computing the cost of contract bidding?

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

* 13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?) ACS - 3,000 - 4000 - IT Tech. Sol. of 65G

Bus level -> 15 staff, 12 more on Proposal

- proposal costs on Comm side - more inv. in marketing

compens. higher Fed comp + ~~Sal~~ Fed - 80 - 120 + 20% bonus -

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?) Com 0 - 80K - Sal. 2% of sell bonus

15. What is your policy toward dealing with unions? (How important?)

Comment ____________________

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment ____________________

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment ____________________

____

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ____________________

____

19. In relation to outsourcing, how sensitive are your customers to tbe issue of control, in general, and control of proprietary data in particular?

Comment

____

____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

____

____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ________________________________

Phone #: ________________________________

Email Address: ________________________________

Thank you for your time and consideration.

CYNDC1

Questionnaire No. # 9
Printed: 01/08/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❒ Vendor ❒ Telephone
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: Applicant -
Address: 313 Constitution DR
Menlo Park, CA
94025

City/State:
Zip:
Telephone: 650-475-8000
Fax #:
WWW

Project Code/Catalog No. ☐☐-☐☐☐-☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐/☐☐/☐☐
QC Initials ☐☐☐
QC Date ☐☐/☐☐/☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐/☐☐/☐☐
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

Respondent(s):
Name Andy Sayre Title: VP Tech Marketing (Prod Mgr)
Phone/Ext. 650-475-8137 Email asayre@applicant.com
Role in Project:

Referrals:

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- ❒ Federal Government
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

CYNDC1 Questionnaire No. # 9

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

____

Collect related demographics
– differentiator: don't have legacy baggage (infra. ind, staff consultants)
– new org. → align with partners

2. What is your role?

(ASP)

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment Bkg, IT mgmt, Syst. integ. – midmarket – infrastructure, middleware
appl. + Applicant – wants to do in "backoffice" – offer service only

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

Comment No, fed market experience

____

changing market – self selecting

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

Comment _______________

start-ups
AT&T / Verizon Data Ser (data centers + hw mgmt, enterprise
appl. OS → appl. level – core of appl. specialists →
case Mid markets
Mid market – $1 bill
growing co.

Dynamic market
growth, ind

*

Decision: Public sector market?

Reason to ~~not~~ to go to public

Common
- want to effect change in organization
-

in public - too much bureaucracy, too diff to achieve implement.

competition – brings to commoditization, price low – vendor. Types

Horiz – standard apps across

Bus/Svc. Focus – no BPO

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments growth in very sp. vert. vendor apps – that address bus/svc.

mkt: "speak cust language" – tailored service (ex. PeopleSoft) – high-tech many

Proprietary SW? No, have prop. pkg, templates

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments Look at new vertical market? resource issue need subj. & app & support staff – team together

Cap time people effort

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Agilera – now OS, doing IDC

Comment

now – new deep pocket partn. – cap market shut down last year

cap scaling/ASP market huge challenge; ASP need scale for eff.

– need signif amount up front – breakeven after 2-3 qtrs of operation on 3-5 yr contract

8. What important changes do you see at work in the outsourcing market today?

Comment: Darwinizing process – co. able to get money can build to scale – pricing also signif. – need consolidation to occur – no signif. cust downside

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments ASP dependable like utility – e-mail, help

SLA – monthly; pos/don't diff for ~~si on RAD~~ OS –

cust must be satisfied each month.

key to attract new vertical? incentivize cust – new core cust. We have process for attracting a new market.

BPO – take over function & prov. tools for an overall bus function

Generic, horiz

– apps e-mail – standard

ASP – management services

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

    Comments

11. What process do you use for computing the cost of contract bidding?

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

15. What is your policy toward dealing with unions? (How important?)

Comment ______________________________

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment ______________________________

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment ______________________________

____

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ______________________________

____

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment

____

____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

____

____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ____________________

Phone #: ____________________

Email Address: ____________________

Thank you for your time and consideration.

Questionnaire No. #10
Printed: 01/08/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ☐ Vendor ☐ Telephone
- ☐ User ☐ On-Site
- ☐ Other ☐ Mail

Company: Getronics
Address: 7910 Westpark Dr
McLean, VA

City/State:
Zip:
Telephone:
Fax #:
WWW

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐|☐☐|☐☐
QC Initials ☐☐☐
QC Date ☐☐|☐☐|☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐|☐☐|☐☐
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

(came from Wang) (prior - VP - contracts comm. of group)

Respondent(s):
Name Bob Martin Title: VP - outsourcing - Federal Market
Phone/Ext. 703-827-6415 Email bob.martin@getronicsgov.com
Role in Project:

Referrals:

Industry (User Interviews Only):

- ☐ Discrete Mfg.
- ☐ Process Mfg.
- ☐ Transportation
- ☐ Utilities
- ☐ Telecommunications
- ☐ Retail
- ☐ Wholesale
- ☐ Banking/Finance
- ☐ Insurance
- ☐ Medical
- ☐ Services
- ☐ Education
- ☐ Federal Government
- ☐ State & Local Government
- ☐ Other Industry
- ☐ Consumer/Home
- ☐ Cross-Industry

cemdy Sr. (9 people)

Secure fed market org

(legacy of Wang)

ex Netw Security Center of Excellence

- E-~~Center~~ Center of Excel

"fed" - State & local

more

parallel 3 commercial

(3)

we monitor compl of contract, take care of special projects

Proj. Mgr for contract report to Gradhen gp. div - we

maintain cont. force -> Monitor bus basic - regs for

Sent organd

- Parallel center of Ex. for non-Sent orgnd (Any one technical

This is a bus model activity

(incl. all tech. function

- gov group has own B of D, proxy board - gp. indep.

from Amit-Getr.

Getronics: 500,000 worker contr. globally

Success in Sent orgnd -> ability to leverage econ. of scale

cont offered outsource - (down) - need bus. continuity

Comm vs fed: Cio of comm entr. = uniqued as govt agency. (can be fired more easily)

CYNDC1 Questionnaire No. #10

(Wang - '96, 14 yrs PRC)

Comm - VP contr reg on comm side

Introduction

IT infr support

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You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

(have contract weekly - have sep mission —

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

Comment. OS? yes, grow

co-develop best practices
- leverage license (enterprise)
- share develop support (SW; tools)

Collect related demographics

Fed ex = 16 yrs - out (sys/comm) - came back to

2. What is your role? Fed - just before DINS + Seat mgmt

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

(Fed)

Comment Center of Excell. for Seat Mgmt (daily with specifics) resp. for devel. innovative Seat mgmt sol + communication as req.

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

Comment $3-4 bill govt. Rev

Gov Sol grp = $400 mill - about 10%

— aim at $1 bill 7 5-6 yrs (organic only.)

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

Comment

Govt. Gov Sol (Fed)

Seat mgmt - 10-15%
labor/services - 80%
(non-OS)

- Monitor does Biz proposal support
Sales people. Bus devel → aligned by agency

Grant mgmt = unique Fed term

(some Fed cust. grant "grant mgmt" is a way to buy hardware)
– Hw lease cap acct
gov for O+M acct

T+M appr. is contrary to the best interest of gov or taxpayer

Grant mgmt → will evolve, become more comprehensive – → BPO – HR, Fin
other

– agencies are putting out pieces → agencies will evolve
common concept "grant mgmt" – is 4-5 yrs be

DC VP 4.5 y

– if vendor owns assets – pays 86
property tax

if Fed, own – None

– vendor will lease; gov buys down cap acct. IT

→ renewal. 15-20% cost markup; growth has little of ^ assets

must "repeal" of Fed into CONTRACT – would use existing contract vehicles
GSA Schedule

same appr. to commercial
*, 180' Bid zero initial margin, end up profitable to perform.

5. Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments getting seat mgmt is like getting camel's nose under tent 10-25% increments – 2% for prog. recover seat mgmt contr – as the incumbent

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments another rel. on partner for core comps of seat mgmt → you must have your own core comp. → agency a moving target (staffing want sophisticated growth) – not sig. barriers

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business? Leasing firms avail – cap no prob.

Comment tool inv – a hurdle → agency transit – D250 → $1 mill – up front agency problem

"leasing is incremental"

8. What important changes do you see at work in the outsourcing market today?

Comment: – about to be massive Fed retirements → no repl. → new recruits will want better HW

– next two yrs catchup – results of seat →

– unions? TRAC – cont, can't be stopped

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments Seat

– good growth potential in seat mgmt

unions – have exp in non-seat contracts → confrontation not necessary but union has int. in incr headcount

(6) – primo can be outreache. On Comm side,

IT OS   3-of 4 primo bad mgmt subcontr – problem

Bad managmt IT [cost sharing / processes / tool / people] } these may not be compatible with Sub-partner

– Comm market for IT OS then pot.

move fed/com → engg → main diff // bus dev. / Sales

– Bus. process Serv   TCO-expert on comm side

[ITAR 9.5 - cmf of ent / mixes TCO]

IT can be compet weapon → cust < IT vendor / core compet.

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments Seat - mgmt

11. What process do you use for computing the cost of contract bidding?

tinkered widget → no good cost model - really like DNA + each deal different - pricing is an art (no precise data)

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

take hits commons → Seat pricing, seat includes orig. serv levels, high-low refresh rates, ref to serv. ~~cost to be negotiated~~ ~~(try not to change price~~

* 13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

not much diff. - big diff. cost of seat contr - opp to bid/serv contr (a bounty contract) - GSA seat orgs contr. - streamlined less than 6 - ~~term~~ - 6-9 months

Seat: min $200k prop cost

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

vendor: can't be everything to everyone - Need to use same tool set for sign'f period time

15. What is your policy toward dealing with unions? (How important?)

Don't want to be in SW business

Sol → Prop. partner

will assemble best of breed tools

1) - decision quick fast
impl. of [illegible] comm. can be quicker

- Sales ≤ Comm. > can be more exp.
fed ↙ agency - easy to identify.

- cont

- marketing is diff. concerned firms
can help

-

" NO press at [illegible] → succeeded - open
competition → no pre-exist relat.
(GSP wants this worded)

Comment ______

______

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment ______

______

17. What changes are you seeing in customer motives for outsourcing IT?

Comment ______

______

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ______

______

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment

______

______

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

______

______

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ______________________________

Phone #: ______________________________

Email Address: ______________________________

Thank you for your time and consideration.

Questionnaire No. #11
Printed: 01/18/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❒ **Vendor** ❒ **Telephone**
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: Suzanne Grenache
Address: 1420 West Placita Del Rey
Tuscon, AZ 85737
City/State:
Zip:
Telephone: (520) 498-1586
Fax #: (same)
WWW

AG

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐|☐☐|☐☐
QC Initials ☐☐☐
QC Date ☐☐|☐☐|☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐|☐☐|☐☐
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

Respondent(s):
Name Suzanne Grenache Title: NA
Phone/Ext. Email legacySEG@earthlink.net
Role in Project:

Referrals:

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- ❒ Federal Government
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

Collect related demographics

Provided competencies IT - (Also classified s/w develop) clearfield govt, appl sol for new bus ACS fed govt, appl sol for new bus & exist installed base - 20 yr DEC appl. devel

2. What is your role?

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment joined CSC from allied Signal - Dir of IT (bus unit) → CSC as Acct exec. Def Syst Seg → Hughes → Raytheon Missile, Naval - Full service IT OS and appl

3a. Also, what proportion of your company's business, if any, is the U.S. federal market.

Comment

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

Comment ASP - good potential; top tier, exp. vendor can work all verticals; many facets of work are generic; we can leverage exp. in one vert and indust. Clients expect ref-clients in same industry. Clients always insist their needs are unique, = based on tech bkg - little signif diff. between verticals

ASP - appr. can be very closely targeted to
a sp. industry.

Fed to Gov'm

(6) talk of achievement
Sales staff? Same - Sales & market must be able to
show underst. of technology staff - underst how
probs are solved

If Sales likely too thin - (sales conf) will likely be successful
Danger of sell-something company can't deliver

- Sales people must understand what company can really
deliver

Co - must make investment in specialization & depth

Greatest potential - don't hybridize infrast. + (on)
Bus. & process - pick either infrastructure
ATP

on limited org. to support

CYNDC1 Questionnaire No. #11

→ mobile trends / modernize

5. Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments both happen → vendors need to work on fundamentals both; tending to win and worry about deliv-key of both out's. consultants insist on perceptual agr.

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Fed to comm → comm clients not impressed by Fed work – Comments Fed gov't aligning with commercial (Standardization) Comm to Fed – complexity of contract & bidding / protocols, security proofs

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment not a const for CSC, yes for ACS, Co had to give quality prop – due to inability to feed capital ex. grow in planned way (capital is only one factor)

8. What important changes do you see at work in the outsourcing market today?

Comment: next step → BP & gov't greater than real – Resist. by client → dim control. (Threat to headcount). – clients look for SLA, penalty – but no hist. evid that this perf had ever been reached, may not be possib.

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

most $$$ – e-comm solutions
Comments $$ gov't. mgmt & develop (need exp. in top ERP sol)
$ – call cent, data cent, TP

Smart vendor can exp excellent gov't – ASP (serv. deterior, prices raised) – danger: grow too fast, costs rise – altho all OS intended to save money – reallocate, etc.

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments

11. What process do you use for computing the cost of contract bidding?

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

ok to say (no)

(B+P costs)
13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

Fed. process more complex - easy to waste money if you don't target your market & great. where can you add value?
OS consultants → making it harder - OS ~~inquiring~~. some consult. not vendor friend - can run up costs

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

it makes consult look better if he brings in fewer vendors to show rather than 3

15. What is your policy toward dealing with unions? (How important?)

mostly self-deception both sides

Comment ______________________________

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market?
    What would you need to do to become ready?

Comment ______________________________

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment ______________________________

____

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ______________________________

____

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment

____

____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

____

____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ______________________________

Phone #: ______________________________

Email Address: ______________________________

Thank you for your time and consideration.

Questionnaire No. #12
Printed: 01/08/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ☐ Vendor ☐ **Telephone**
- ☑ **User** ☐ On-Site
- ☐ Other ☐ Mail

Company: Dr Pepper / 7 UP
Address: 5301 Legacy DR
Plano, TX 75024

City/State:
Zip:
Telephone: 972-673-7924
Fax #:
WWW

Martha Eickman
Admin (972)-673-7828

Respondent(s):
Name ART FINO Title: SR VP - Inf. Services
Phone/Ext. 972-673-7924 Email 972-673-7380 FAX Email: art_fino@dpsu.com
Role in Project:

Referrals:

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐|☐☐|☐☐
QC Initials ☐☐☐
QC Date ☐☐|☐☐|☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐|☐☐|☐☐
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

Industry (User Interviews Only):

- ☐ Discrete Mfg.
- ☐ Process Mfg.
- ☐ Transportation
- ☐ Utilities
- ☐ Telecommunications
- ☐ Retail
- ☐ Wholesale
- ☐ Banking/Finance
- ☐ Insurance
- ☐ Medical
- ☐ Services
- ☐ Education
- ☐ Federal Government
- ☐ State & Local Government
- ☐ Other Industry
- ☐ Consumer/Home
- ☐ Cross-Industry

Introduction

The purpose of this survey is to determine how customer attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of customer attitudes and preferences in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

____

Collect related demographics

2. What is your role?

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment have 3 sep. OS contr in place (1) CSC - appl mgmt & SAP support (2) MIPS in vall - server mainfr → mainfr ... MSP (pay monthly on volume) (3) OS agr in place for helpdesk desktop 1800 ... of Rsup - synergy. - prod staff. - Dev - free

B. Priority Questions

4. Do you prefer comprehensive ("bundled") OS contracts? (If so, why?)

Comment No,

5 To what extent are you inclined to outsource based on a need to reduce your capital outlays and/or headcount?

Comments where there are 3 diff. serv providers — usually no "is good at X other good at Y" — goal: maintain routine gsn — use internal staff to higher value-added.

6. How do you determine which outsourcing vendors to invite to bid?

Comments Corporate sourcing — disc process → do down own nearly recent. Consultants? No, each case diff → urgency, tool model in place for deal; general & vertical, industry (4) extremely referenceable; mgmt. - partner

license -> DOJ Retains license -
lowered charge.
- same reg. many years ago

Synergy -> in forth yr.

Key to success: effective contr. with flexibility - an
knowledge
excellent management.

mainframe ASP < switched 2 [illegible] -> found opportunity
for big cost saving

IBM global -> ISI internet sup T inc
A selling tour.

Sales meeting proposal
for non-SAP
[illegible] segments

 suppt to diff. comm. cs for competition

7. How receptive would you be to a bid from an outsourcing vendor whose experience was almost entirely in the federal sector?
depends on function – in infrastr, IT service, help desk etc. Presence there is, across industry; exception: part gps. – if any why use fed. exp

8. How important is the outsourcer' ability to attract and acquire your targeted staff (as part of a proposed contract)?
– CSC did involve staff transf + was very important. wanted to ret. knowledge have of existing staff; needed compet vendor, who was able to absorb staff?? staff retention issue, gave incent to remaining brought per staff.

Bryant sys CSC contract very successful

9. What important changes do you see at work in the outsourcing market today?
① prov & cust are more educated
Comments ② models more sophisticated
③ ASP – will use more → could do SAP as ASP
~~agr – But might not provide good web gps.~~
consultants? More focused role → specialized would use to find ASP

C. Additional Questions

10. Which type of outsourcing fits best your company's needs? (and why)

11. How is IT outsourcing affecting your industry? (Effect on growth? Profitability?)
① Bev industry? have typ prom Arrangs – cored org, brand – manuf process diff → could use BPO vendor → split manuf & marketing
② IT – prov. act. gps. – spending doesnt decline
shifts strategy? NOT NOW – WAS Key driver

12. How has your attitude toward IT outsourcing changed over the past year?
more positive – freed → choice

CSC knows HR working that feeds staff "CSC's core compet is provid. people to IT industry."

13. Are you as attracted by outsourcing entire business processes as by offloading commodity transaction processing?

14. Have you computed the contribution made by outsourcing to your company's overall profitability? (To cost-reduction of IT depart)

Comment gfr – gp. budget objective → had annual targets have exceeded targets which inc. workload. ~~Do~~ measure month + annual. Budget and exceeded target savings

15. Do you prefer longer or shorter contract durations? (Why?)

Comment

16. Have you in mind a ranking regarding which types of outsourcing are the most costly? (Reasons?)

Comment (1) START syst devel / appl. maint.
(2) appl SP → being managed resource
(3) help desk → less skill required - supply. on-site preferred.

17. In relation to outsourcing, how sensitive are you to the issue of control, in general, and control of proprietary data in particular?

Comment

18. How strong is your relationship with incumbent outsourcers? (Probability of sole-sourcing new contracts?)

    Comment

    ____

    ____

19. To what extent, if any, have union relations affected your desire or ability to outsource?

    Comment

    ____

    ____

20. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

    Comment

    ____

    ____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ______________________________

Phone #: ______________________________

Email Address: ______________________________

Thank you for your time and consideration.

Questionnaire No. #13

Printed: 01/18/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ☐ **Vendor** ☐ **Telephone**
- ☐ User ☐ On-Site
- ☐ Other ☐ Mail

Company: Entex IT Services.

Address:

City/State: Ryebrook, NY

Zip:

Telephone:

Fax #:

WWW

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐

Interviewer Initials ☐☐☐

Interview Date. ☐☐|☐☐|☐☐

QC Initials ☐☐☐

QC Date ☐☐|☐☐|☐☐

Data Entry Initials ☐☐

Data Entry Date ☐☐|☐☐|☐☐

Company Type:

Annual Revenue:

\# Employees:

Total IS Budget:

Total # IS Staff:

(worked for Siemens in Europe)
(came to org. last yr)

Respondent(s):

Name Terry Edney Title: SVP STRATegy

Phone/Ext. 914-935-3562 Email terry.edney@entex.com

Role in Project:

Referrals:

Industry (User Interviews Only):

- ☐ Discrete Mfg.
- ☐ Process Mfg.
- ☐ Transportation
- ☐ Utilities
- ☐ Telecommunications
- ☐ Retail
- ☐ Wholesale
- ☐ Banking/Finance
- ☐ Insurance
- ☐ Medical
- ☐ Services
- ☐ Education
- ☐ Federal Government
- ☐ State & Local Government
- ☐ Other Industry
- ☐ Consumer/Home
- ☐ Cross-Industry

CYNDC1 Questionnaire No. #13

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of tbis survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

Collect related demographics

2. What is your role?

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment planning, strategy → not dir. involv. in prop. preparation → Fed & Comm (all treated as single entity)

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

Comment Public Sector = State & Fed = (10%, ...)

Commercial Sect = 90%

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

Comment Fin Serv. (ins); health care [big pres. US] driven not in most

- sales not org. by industry

* integration with Siemens? Entex is wholly owned sub of Siemens Bus Serv

— how reach prospects? target Fort. 100-500 → SBS → IT Serv. (Entex)

Size of cust (rev) < act. cust 50% Fort 100 ↓ Cust

IT intensity

(not all in manuf.) (less IT intensive)

(looks for 25-3,000 seats + → complex site)

Entry: desktop → network serv focus now

TARGET mkt

Entry: Selon IT Spend

$100-500 million spenders

- $1 bill + in few

- we work on account based list of prospects → two some geogr. + industry (plan for increased penetration)

- Sales focus on company.

Entry approach: very diff for what is done Engrs
- in Eur, more geo cover with geo Staff - not on-site staff.
- in U.S. Entex has, large on-site staff.

CYNDC1 Questionnaire No. ~~#7~~

- wireless LAN? more activ in Europe (mobile network - more advd + complete)
- momentum in US? Syps in future

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

① cust. want basic ops. reliance on delivery

Comments upmarket → is happening

② move to fewer headcount - e-bus.

- want value of service - stake

more resp. (out ent. cost sav. issue / remove mgmt burden)

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments less barrier to basic. serv (reason for commodity)

future tech expertise + ops cap. (cust. less concerned about vent without exp, in Fed need to prove cred. of good market

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment

no

8. What important changes do you see at work in the outsourcing market today?

Comment: move by cust. look for more complete servic → fewer vendors (reduce # of suppliers, prime/subs) less headcount - e-bus transition worse competition. (small - large more subs cont labor - Gov. Wage

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

$$$ Comments ① network mgmt, consulting.
(2) break-fix

- In Fed market, part as both subs + prime.

A
b - dep on industry analyst opinion

Entex

- name recog is problem.
  - Siemens → grow both credentials

- use consultants? not much contract so far
(-name ref. in Energy Inst. → Siemens)
- not an experience due to type of bus

off harden
screen

CYNDC1 **Questionnaire No.** #13

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments desktop services → netw. mgmt.

11. What process do you use for computing the cost of contract bidding?

size of bids smaller → costs (sales) smaller, large bids are decided by top mgmt. Don't go in cold with new bus. Usually - take over a piece of bus → expand.

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

- process: key is def. of work to be done - review mgmt proposal on contract - audit - con offer want on volume basis. Staff: more of our people in Europe. - key skill req. - start of Proj: Mgr. (rather in Europe)

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

diff desktop & netw from "complete" - data cent contracts - nat. gov bids can be expensive in Europe (much longer in Europe) < commission at moment.

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

not at all

Try to redeploy staff geographically -

- ret. rate is very good

15. What is your policy toward dealing with unions? (How important?)

Comment ______________________________

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment ______________________________

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment ______________________________

____

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ______________________________

____

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment

____

____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

____

____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information: Name/Title: ____________________ Phone #: ____________________ Email Address: ____________________

Thank you for your time and consideration.

Questionnaire No. #14
Printed: 01/18/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❒ **Vendor** ❒ **Telephone**
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: US Interworking
Address:

City/State: Annapolis, MD
Zip:
Telephone:
Fax #:
WWW

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐|☐☐|☐☐
QC Initials ☐☐☐
QC Date ☐☐|☐☐|☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐|☐☐|☐☐
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

former with Input.

Respondent(s):
Name Dick Tenhorst Title: VP - Public Sector
Phone/Ext. Email
Role in Project:

Referrals:

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- ❒ Federal Government
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

USi - doesn't target vertis —
except. Public Sect.

(But) have some spec. industry-g perf.
solution - ex Broadvision for Retail
RepubSoft in Ensurance.

USi
relat to Primes in Fed Sector?

- USi has chosen to partner with big integrators —
(They don't want to make big inv. in HW)
- and PwC, EDS etc have multiple cont - give
us great exposure (Publics contr tend to
be larger)
- no profit harvest

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

USI – glo regions – [illegible] VP [illegible] who have terr. div → within region → focus on vertical

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

____

Collect related demographics – want to focus and market on verticals

2. What is your role? bus. develop – sales role – staffing for [illegible] pursuing & signing new clients + higher education

3. Please indicate the nature of your experience with outsourcing (IT or otherwise). [Prim – broad comm exp]

Comment in US bus since 1974 → CSC; Then ASP offering quite diff. ex. CSC, EDS etc will go in and take over ent. IT infrast < focus on sp. apps.

View market by app.

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

Comment most bus in public sect → fed. (6 client, + NY Port Auth) → [illegible] focus on state of MD

– ASP → more attr to public sect. [illegible] due to retirements, esp app specific

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

Comment Finance, health care, ins. → public sect. * Retail

– "USI is being wooed by big SI vendors" – as #1 – ASP → [illegible] for ERP SW

public sect = 5-10% of total USI Rev. (have 2 Pub sect accounts)

Retail: B&M & [illegible] now accept need for e-com STRAT

ERP = SAP, Lawson, Oracle 4

have gone to cut through
partner →
AVS!
- some premise

* fed to comm → more diff. acct.
Remm: mindset, diff. sys.
- needs big investment in fed market
vendor mindset in comm → cong to
"just crumbs" in comm
internal fin market

(6) barriers to entry -
Barriers to Fed market → longer sales
cycle in Fed.
- need separate sales team (comm salesm
need re-orient. to Wash)
- relationships important - pers contr. with integrators
relat - more import in Fed. market → relat always
import. but diff in comm
State govt → all personal relat.
Name recognition? Benefit mkt sect. for comm
recognition. specialized + name recog

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing? — also true in public sector

Comments both comm & Pub sect - we are mov. upward → market.
apps. Same client - house app integ with legacy system written with AC, CSC, Stic in State of MD contr

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments we don't see same public sect capabilities as commercial → many are moving to fed. market (USi has glog. adv.) - we can address security issue (comfort & feel on capability)

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment large barrier to entry b/c of demise of other ASP
- ASP bus is cap. intensive
- has lost no business for this reason

8. What important changes do you see at work in the outsourcing market today? better market recog of ASP & USi → better, quicker accept in comm
- now, 208 clients total (2 yr period) = $400 million Fed - Comm
First govt client - 2Q '99 → 2nd govt - 3Q, 99 → rest 3, 4Q of 2000

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments

___

___

use of consultants in comm market?
"I don't like" diff to manage - like direct sales force model
- we do rely on OS consult. to bring us into deals & want more in-house sales force
must be able to close

(8) major agencies want to use OS model —
justice, [illegible]. AG

- no effort yet of ANTI-OS initiatives in Wash/Fed
- many written programs → Fed could run gpl. systems
eg PeopleSoft → is labor-intensive

- USi doesn't [illegible] to take over entire Data Center

* DOD? - not yet
- current sales staff more on civilian

comm.
USi → green to all verticals → easy to say you will spending, but can't spend in too many

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments
Increasing move to "verticalizing" sales force & product → this is a trend – USG contract to sell entire prod.

11. What process do you use for computing the cost of contract bidding?

____

____

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

____

____

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

____

____

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

____

____

15. What is your policy toward dealing with unions? (How important?)

Customization ?

Comm

under control
- came to take longer
than 120 days

Fed/gov
gov client → few with
big integration →

80/20 rule

~~every~~ implementation ~~[illegible]~~ clients → large cust. is
can't help all not cost effect.

Comment ______________________________

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment "customer at 'Smartsource' service provider power"

17. What changes are you seeing in customer motives for outsourcing IT?

Comment $ctA - attr idea for comm v Fed cust. (core vs non-core) - need to educate cust at times

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ______________________________

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment ______________________________

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment ______________________________

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ______________________________

Phone #: ______________________________

Email Address: ______________________________

Thank you for your time and consideration.

Questionnaire No. #15
Printed: 01/18/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❒ Vendor ❒ Telephone
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: Keane
Address:

City/State: Boston
Zip:
Telephone:
Fax #:
WWW

Project Code/Catalog No. □□|□□□|□□□□
Interviewer Initials □□□
Interview Date. □□|□□|□□
QC Initials □□□
QC Date □□|□□|□□
Data Entry Initials □□
Data Entry Date □□|□□|□□
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

Respondent(s):
Name LARRY VALE Title: VP Ext. communications
Phone/Ext. 617-241-9200 Email
Role in Project:
Referrals: also resp for Ind. Analyst Relations; investor relations

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- ❒ Federal Government
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

   ____

   Collect related demographics

2. What is your role?

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

   Comment______________________________________

   ____

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

   Comment______________________________________

   ____

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

   Comment______________________________

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments ____

____

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments ____

____

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment

____

____

8. What important changes do you see at work in the outsourcing market today?

Comment:

____

____

____

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments

____

____

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

    Comments

    ____

    ____

11. What process do you use for computing the cost of contract bidding?

    ____

    ____

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

    ____

    ____

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

    ____

    ____

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

    ____

    ____

15. What is your policy toward dealing with unions? (How important?)

Comment ____

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment ____

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment ____

____

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ____

____

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment

____

____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

____

____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ______________________________

Phone #: ______________________________

Email Address: ______________________________

Thank you for your time and consideration.

Questionnaire No. #16
Printed: 01/26/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

- ❒ **Vendor** ❒ **Telephone**
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: Unisys
Address: Federal Government Group

City/State: McLean, VA
Zip: 22102
Telephone: (703) 556-5522
Fax #:
WWW

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐|☐☐|☐☐
QC Initials ☐☐☐
QC Date ☐☐|☐☐|☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐|☐☐|☐☐
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

Respondent(s):
Name George Wendt Title: Manger
Phone/Ext. (703) 556-5522 Email george.wendt@unisys.com
Role in Project:

Referrals:

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- ❒ Federal Government
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)
   Yes ________

   Collect related demographics

2. What is your role? Manager Market Development & Planning

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

   Comment Leading provider of outsourcing to both commercial and public sector marketplace________

   ____

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

   Comment Approx 10%________

   ____

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

   Comment Public Sector________

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments Moving upmarket, we are however a full service provider

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments Federal A-76 plans ply an important role in outsourcing. Staffing and Marketing are also significant barriers

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment
Bid activity/capital is based on priority of outsourcing bid

8. What important changes do you see at work in the outsourcing market today?

Comment:
In federal marketplace we feel outsourcing will play a significant role, s government is being downsized and asked to do more with less. A-76 issue and unions need to be addressed

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments
Data Center, Infrastructure and transaction processing

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments
Data Center and
Infrastructure

11. What process do you use for computing the cost of contract bidding?

Based on contract type and requirements

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

Yes

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

Some Federal bid/sales expenses are much lower than commercial

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

No

15. What is your policy toward dealing with unions? (How important?)

Comment N/A

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment We are actively involved in both commercial and federal outsourcing

17. What changes are you seeing in customer motives for outsourcing IT?

Comment Skills drain, and downsizing are two key issues

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment Past performance should be more important than company size

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment
In federal marketplace, control is very important issue

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment
Bundled

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: George Wendt ______________________________

Phone #: (703) 556-5522 ______________________________

Email Address: George.Wendt@Unisys.com ______________________

Thank you for your time and consideration.

CYNDC1

Questionnaire No. #17
Printed: 01/23/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

❒ **Vendor** ❒ **Telephone**
❒ User ❒ On-Site Fed Data
❒ Other ❒ Mail

Company: Tom Arnsmeyer
Address: 10521 Rosehaven St
Fairfax VA

City/State:
Zip:
Telephone: 703-934-7748
Fax #:
WWW

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐|☐☐|☐☐
QC Initials ☐☐☐
QC Date ☐☐|☐☐|☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐|☐☐|☐☐
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

Respondent(s):
Name Tom Arnsmeyer Title: VP - IT Mgmt Serv.
Phone/Ext. Email tarnsmeyer@feddata.com
Role in Project:

Referrals:

Industry (User Interviews Only):

❒ Discrete Mfg.
❒ Process Mfg.
❒ Transportation
❒ Utilities
❒ Telecommunications
❒ Retail
❒ Wholesale
❒ Banking/Finance
❒ Insurance
❒ Medical
❒ Services
❒ Education
❒ Federal Government
❒ State & Local Government
❒ Other Industry
❒ Consumer/Home
❒ Cross-Industry

CYNDC1 Litton/PRC → some to Northrop / some to Logicon / most fed **Questionnaire No.** ________

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey. 90% fed

Fed Data = base of few comm.
Logicon = some comm.

10% is OS - 3rd party grant

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

Fed Data
Pantoz Logicon (IT Div);

Collect related demographics

synergy BKG. - 21 yrs IT bus; Kennedy Space Center Lockheed ... Johnson Space - RAN IT supt → OS pre → ODIN -

2. What is your role? Now Fed Data - for ODIN seat mgmt → other similar

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment Before → much ACT at Johnson - turned perf based contr to first seat cont → NASA; Fed Data → set infrast for ODIN ESA seat mgmt

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

Comment comm work diff - no ... done by ... good synergy - ... [illegible] ... no ... [illegible]

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing? best growth pot? LT, DoD, Army, Air Force → compet. with NMCI

Comment exp. some ... budget ..., no ... [illegible]

also asset mgmt, related company partners - ... Wright Pat AFB

(catching) similar to NMCI / EDS ESA, BPA - now small ... initiative ... task order

- groundfull effort - successful - write comments for more enterprise approach

good comments - DoD for NMghut

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments no large-scale handling yet - ex SSA, want to do only 200 seats as a test; uncomfort. with single vendor for all 60,000 seats
- other fear: contract fear to turnover doc work; budget

good to find IT outsourcing for sec. mgmt.

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments common to fed → harder (unprep for long sales cycle, not used to regulatory env.)
- barriers fed to comm? Relationships. lack of marketing, lack of exp & knowledge. Need partner - exper. will carry over

"would need 'mission' organization" - "organizational" - staff up

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment not a problem: spend ex $50K for small ones in most fed US agy. little for larger types contr
- good soluti → cap. lease leasing (EvenNavy = too dt)
- prop tax? if fed facil., no prop tax → no tax if fed agency

would need to be gov't - common to the fed - very diff. ODIN OSD gent

8. What important changes do you see at work in the outsourcing market today?

Comment:
(1) people recog need for change < Budget, Staff
(2) attempt to understand how to transit to OS < new budget (agency doesn't plan for IT) - not enough money
(3) TCO - hard soft cost - agen comfort with hard - diff to take adv of soft cost reduct

Fed = will be many obsolete in less than 5 yrs

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments
(1) enterprise seat mgmt (help desk, netw., apps, break fix)
(2) Netw/LAN/ADMIN support HW/SW acq - cable - some apps with desk
(3) help desk [has been commoditized]
(4) web hosting / web site develp

logi-
State & local - geo est. Data Cent - Texas, CA.
potential? good, but small - slow OS
- agree - in trouble -

$$? pre ... gov't GO?

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments ① seat mgmt / enterprise ② network 2-3 yrs = seat & entrp

11. What process do you use for computing the cost of contract bidding?

models used; KM sys, pricing models; how big deal to be worthwhile - No seat mgmt differ between competitors

- lots of reuse models, proc for new fed bid (would use same in comm market)

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

changes don't all ch. profitability - ex seat, SOW - price is all encompassing - model is broad. (try to keep cost same as changes are made)

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?) [overhead, HR, Admin] + dir costs incl.

fed comm & not real impt

marketing cost as % of total cost of doing business = 20%

- 20% is high now → to sustain fed bus → 10-15% - commercial

6-9% - cheaper - sales cycle much shorter

Def. Government

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

- not an issue at all - feds - agencies make changes

- fed & comm seem need TRAINING, tech & processes

15. What is your policy toward dealing with unions? (How important?)

CSC - diff to get comm. model to work in fed market

Comment ______________________________

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment ______________________________

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment ______________________________

____

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ______________________________

____

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment agencies very aware of security - data mgmt. - locking
sent mgmt - loss of control is perception ex. remote netw
mgmt → can be solved, misconceptions [illegible]

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment ______________________________

____

- likelihood of more comm bus? yes
ideal diversity?

50% fed
25 state & local
25 comm.

State & local & commercial

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ____________________

Phone #: ____________________

Email Address: ____________________

Thank you for your time and consideration.

Sorry
for info?

Fed Data = big backlog of bills
$20 mil.
Logic most large

2 yr ago around
now 20 mil
Logic '98 → 2001 = $400 mil
$2.1 bill

North Am = 18 bill
↑
2.5 of this

(incl Fed Govt) Logic

Total PRC = 8.5 bill

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

X❒ Vendor ❒ Telephone

❒ User ❒ On-Site

❒ Other X❒ Mail

Company: Compaq Computer Corp

Address: Compaq Global Services

40 Old Bolton Road

City/State: Stow, Mass

Zip: 01775

Telephone: contact: Debbie Botos (978) 496-8521

Fax #: Debbie Botos 978 496-9436

WWW Debbie.Botos@compaq.com

Project Code/Catalog No. ❒❒|❒❒❒|❒❒❒❒

Interviewer Initials ❒❒❒

Interview Date. ❒❒|❒❒|❒❒

QC Initials ❒❒❒

QC Date ❒❒|❒❒|❒❒

Data Entry Initials ❒❒

Data Entry Date ❒❒|❒❒|❒❒

Company Type: *computer products & services*

Annual Revenue: *$42 B*

Employees:

Total IS Budget:

Total # IS Staff:

Respondent(s):

Name Joe Hogan Title: Director of Solutions Development, FutureSourcing

Phone/Ext. *978 496-8269*

Email *Joe.Hogan@compaq.com*

Role in Project:

Referrals:

Industry (User Interviews Only):

X❒ Discrete Mfg.

❒ Process Mfg.

❒ Transportation

❒ Utilities

❒ Telecommunications

❒ Retail

❒ Wholesale

❒ Banking/Finance

❒ Insurance

❒ Medical

X❒ Services

❒ Education

❒ Federal Government

❒ State & Local Government

❒ Other Industry

❒ Consumer/Home

❒ Cross-Industry

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

Yes

Collect related demographics

2. What is your role? **Development of the outsourcing offerings for Compaq Global Services**

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment: 20 years in the business selling, delivering and building different approaches
Compaq Global Services has been providing outsourcing services since the late 1980's.

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

Comment__________**From an outsourcing perspective, very little of our business is in the US Federal Market**__________

____

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

Comment: **Telecom, Financial, Mfg, and Retail/Distribution**

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments: **We are moving up-market to become a virtual support function to the CIO.**

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments: **Developing and delivering a creditable value proposition that the clients in the new market will buy.**

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment: **These factors are minimal constraints if the outsourcer has both the delivery infrastructure and resources to leverage.**

8. What important changes do you see at work in the outsourcing market today?

Comment: **The role of the CIO and technology as it relates to business success or failure has increased in importance. As a result the need to buy sourcing solutions based on results is becoming the norm.**

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments: **(1) Full IT and Process Outsourcing – ability and expertise to manage to the clients desired business results. (2) "Next Generation Mgmt" Infrastructure – ability to manage the risk of transition to the clients desired state. (3) eWorkplace (asset mgmt) – the management of all change, moves, adds around network access devices such as: desktop, PDA, messaging and enterprise help desk support.**
REASON: expertise, process and methodologies that can provide the desired consistent office environment required by the client to perform their business offerings is situated in a highly competitive market. (4) Customer Care (Enterprise Help Desk)
REASON: specific helpdesk support (level 1) is focused usually on cost reduction for the client. The market is a highly competitive market when the offering is transitioned to an enterprise approach integrating requirements for multi-language, application and international support the value to both the

client and the sourcer increase. (5) Private Storage Utility and Business Continuity
REASON: This offering provides the integrated support of both product and services to secure the valuable information of our clients.

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments : **Information technology sourcing**

11. What process do you use for computing the cost of contract bidding?

Compaq has disciplined approaches to pricing. ________________________

____

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

Yes

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

Minimal

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

No it has not

15. What is your policy toward dealing with unions? (How important?)

Comment: **We are open depending on the opportunity, the legal constraints of the client/labor relationship and the geography.**

16. How ready is your organization to bid on contracts in the federal (or commercial) market?

What would you need to do to become ready?

Comment: **We already do this and have many reference-able clients.**

17. What changes are you seeing in customer motives for outsourcing IT?

Comment: **They are considering the strategic nature of its ability to impact business results quickly.**

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment: **Company size cannot be limited universally to revenue, this criterion is sensitive to other key factors such as industry, business model and services or goods provided.**

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment: **Control of proprietary data is a trust some of our clients place with us. It must be treated as such.**

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment: **It depends on the nature of the business arrangement. Unbundled services are typically provided in the Govt. Market or for services which are highly competitive and basic i.e., help desk out-tasking, etc.**

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: **Joe Hogan, Director of Global Solutions Development**

Phone #: 978-496-8269

Email Address: **Joe.Hogan@compaq.com**

Thank you for your time and consideration.

Questionnaire No. #18
Printed: 02/02/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

X☐ Vendor ☐ Telephone
☐ User ☐ On-Site
☐ Other X☐ Mail

Company: Compaq Computer Corp
Address: Compaq Global Services
40 Old Bolton Road

City/State: Stow, Mass
Zip: 01775
Telephone: contact: Debbie Botos (978) 496-8521
Fax #: Debbie Botos 978 496-9436
WW Debbie.Botos@compaq.com

Project Code/Catalog No. ☐☐|☐☐☐|☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐|☐☐|☐☐
QC Initials ☐☐☐
QC Date ☐☐|☐☐|☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐|☐☐|☐☐
Company Type: *computer products & services*
Annual Revenue: *$42 B*
Employees:
Total IS Budget:
Total # IS Staff:

Respondent(s):

Name **Joe Hogan** Title: Director of Solutions Development, FutureSourcing

Phone/Ext. *978 496-8269*
Email *Joe.Hogan@compaq.com*
Role in Project:

Referrals:

Industry (User Interviews Only):

X☐ Discrete Mfg.
☐ Process Mfg.
☐ Transportation
☐ Utilities
☐ Telecommunications
☐ Retail
☐ Wholesale
☐ Banking/Finance
☐ Insurance
☐ Medical
X☐ Services
☐ Education
☐ Federal Government
☐ State & Local Government
☐ Other Industry
☐ Consumer/Home
☐ Cross-Industry

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

Yes

Collect related demographics

2. What is your role? **Development of the outsourcing offerings for Compaq Global Services**

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment: 20 years in the business selling, delivering and building different approaches
Compaq Global Services has been providing outsourcing services since the late 1980's.

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

Comment__________**From an outsourcing perspective, very little of our business is in the US Federal Market**____

____

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

Comment: **Telecom, Financial, Mfg, and Retail/Distribution**

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments: **We are moving up-market to become a virtual support function to the CIO.**

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments: **Developing and delivering a creditable value proposition that the clients in the new market will buy.**

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment: **These factors are minimal constraints if the outsourcer has both the delivery infrastructure and resources to leverage.**

8. What important changes do you see at work in the outsourcing market today?

Comment: **The role of the CIO and technology as it relates to business success or failure has increased in importance. As a result the need to buy sourcing solutions based on results is becoming the norm.**

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments: **(1) Full IT and Process Outsourcing – ability and expertise to manage to the clients desired business results. (2) "Next Generation Mgmt" Infrastructure – ability to manage the risk of transition to the clients desired state. (3) eWorkplace (asset mgmt) – the management of all change, moves, adds around network access devices such as: desktop, PDA, messaging and enterprise help desk support.**
REASON: expertise, process and methodologies that can provide the desired consistent office environment required by the client to perform their business offerings is situated in a highly competitive market. (4) Customer Care (Enterprise Help Desk)
REASON: specific helpdesk support (level 1) is focused usually on cost reduction for the client. The market is a highly competitive market when the offering is transitioned to an enterprise approach integrating requirements for multi-language, application and international support the value to both the

client and the sourcer increase. (5) Private Storage Utility and Business Continuity
REASON: This offering provides the integrated support of both product and services to secure the valuable information of our clients.

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments : **Information technology sourcing**

11. What process do you use for computing the cost of contract bidding?

Compaq has disciplined approaches to pricing. ___________________________

____

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

Yes

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

Minimal

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

No it has not

15. What is your policy toward dealing with unions? (How important?)

Comment: **We are open depending on the opportunity, the legal constraints of the client/labor relationship and the geography.**

16. How ready is your organization to bid on contracts in the federal (or commercial) market?

What would you need to do to become ready?

Comment: **We already do this and have many reference-able clients.**

17. What changes are you seeing in customer motives for outsourcing IT?

Comment: **They are considering the strategic nature of its ability to impact business results quickly.**

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment: **Company size cannot be limited universally to revenue, this criterion is sensitive to other key factors such as industry, business model and services or goods provided.**

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment: **Control of proprietary data is a trust some of our clients place with us. It must be treated as such.**

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment: **It depends on the nature of the business arrangement. Unbundled services are typically provided in the Govt. Market or for services which are highly competitive and basic i.e., help desk out-tasking, etc.**

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: **Joe Hogan, Director of Global Solutions Development**

Phone #: 978-496-8269

Email Address: **Joe.Hogan@compaq.com**

Thank you for your time and consideration.

CYNDC1 Doc (x) ✓ Questionnaire No. #19
Printed: 01/30/01

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

❒ Vendor ❒ Telephone
❒ User ❒ On-Site
❒ Other ❒ Mail

Company: Convergys
Address: ______
______
HQ ______
______
City/State: Cincinnati, OH
Zip: ______
Telephone: ______
Fax #: ______
WWW

Project Code/Catalog No. ☐☐|☐☐☐☐|☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐|☐☐|☐☐
QC Initials ☐☐☐
QC Date ☐☐|☐☐|☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐|☐☐|☐☐
Company Type: ______
Annual Revenue: ______
Employees: ______
Total IS Budget: ______
Total # IS Staff: ______

30 Jan 01

Respondent(s):
Name David Stein Title: VP - Marketing Strategy
Phone/Ext. Tel 513-723-7768 Email david.stein@convergys.com
Role in Project: ______

Referrals:
______
______

Industry (User Interviews Only):

❒ Discrete Mfg.
❒ Process Mfg.
❒ Transportation
❒ Utilities
❒ Telecommunications
❒ Retail
❒ Wholesale
❒ Banking/Finance
❒ Insurance
❒ Medical
❒ Services
❒ Education
❒ Federal Government
❒ State & Local Government
❒ Other Industry
❒ Consumer/Home
❒ Cross-Industry
______

Questionnaire No. #19

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)

Collect related demographics

2. What is your role?

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment

3a. Also, what proportion of your company's business, if any, is the U.S. federal market.

Comment zero

B. Priority Questions

4. In which vertical industries do you see the best growth potential for IT outsourcing?

Comment

- nature of "transaction" becoming more complex, voice, data, other
- g/market - to provide better cust. exp?

(6) comm clients want seamless tech serv —
not likely to be influenced by fed work -
comm cust.
- want knowledge of vertical
- high value, 5000. relat. in private-sector → pole of wid. exp. required
- for basic procurement, basic appl - fed work would be useful
- prods: can't use same sales people - Fed to Comm (long sales cycle in Fed) → speed diff in comm.
- retraining - proc would be slow
- separate unit needed for Fed/comm → challenge in integr technical people (complicated by acquisitions)

— Slt more demanding in

movement of solution is frugality? our architecture wants — porting of assets to ... call ctr. period

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments sell end to end 'sol — cust serv & billing — CRM — analytics — we "pre-integrate" elements of solution → time to market urgent

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments comm to Fed? — we do "mission-crit-app" clients want experienced provider; could use own comm. ref. → more diff to go Fed. to Comm → work more diff — ex: tech & skill set of Fed integ is diff ("wired into its own")

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business? — leasing do not take over cust. assets

Comment buying cap't existing data center is an asset, ex. no ... facility → is barrier, use partnership — larger you are, easier it is — can use BOT model approach (shared invest.)

8. What important changes do you see at work in the outsourcing market today? 05 → ASP model "outs. light" — consolidation in telecom

Comment: offshore? Gov. is moving in that direction. Azure ftc. Canada etc — investments? we have relat with several — can be critical step in moving into new market

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments Billing Sol, call cent | high volume → ability to scale up

— longer term contract — (5 yr +)

more much work done remotely (80%+); 20% on-site for customer

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments

11. What process do you use for computing the cost of contract bidding?

use price book — TOC model used — will vary dep on kind - platf used; we try to create a strat. partnership → we help client understand TOC → we show how we can be

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

20-30% of rev is prof serv. for FMG - not OS & SI work
- often turned into proj. which into contr relat.
- continue to do contr. extension → done regularly (we re-eval contr)
- in part, have decided not to cont. with clients

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

- relat. low — less than 5% of TCV, or less. Fed would be lower. contr capture costs "transfer" in fed.
- ~~Expect sales + marketing costs to rise~~ —
[SW vendor = 10-15%]

Fed diff in how costs are computed

14. Has inability to absorb staff transfers ~~from~~ customers impeded your ability to close new outsourcing deals? (Strategy?)

- doesn't apply (small degree) — can do "co-sourcing" - take over cont mns. Some cases - absorb staff
- our str. → along to make success acquisition.

15. What is your policy toward dealing with unions? (How important?)

Comment ______________________________

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market?
What would you need to do to become ready?

Comment ______________________________

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment ______________________________

____

18. To what extent does, or should, company size (based on annual revenues) influence a cust. perspect. decision regarding whether to outsource?

Comment Emerging — we eval. fin stats of cust. (award contract, incumbents — no upper limit — depends on cust. strategy)
— growth pot. of customer

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment

____

____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

____

____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ______________________

Phone #: ______________________

Email Address: ______________________

Thank you for your time and consideration.

resp for corp. research

Jim Taylor - Dir of Corp Res.

CYNDC1

SAIC - works w/ gov 1997 - bought Telcordia

Questionnaire No. ~~#19~~ 20
Printed: 01/30/01

CONFIDENTIAL

INPUT Questionnaire

Jose (7)

Type of Interview:

- ❒ Vendor ❒ Telephone
- ❒ User ❒ On-Site
- ❒ Other ❒ Mail

Company: SAIC
Address: 1241 Cave St.
La Jolla CA
92037

City/State:
Zip:
Telephone:
Fax #:
WWW

Project Code/Catalog No. ☐☐|☐☐☐☐|☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐|☐☐|☐☐
QC Initials ☐☐☐
QC Date ☐☐|☐☐|☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐|☐☐|☐☐
Company Type:
Annual Revenue:
Employees:
Total IS Budget:
Total # IS Staff:

30 / Jan / 01

Respondent(s):
Name ART Slotkin Title: Exec VP
Phone/Ext. 858-826-6206 Email arthur. ~~L~~. Slotkin@saic.com
Role in Project:

Referrals:
new position is more senior than that of his predecessor — now has four large bus. units

Industry (User Interviews Only):

- ❒ Discrete Mfg.
- ❒ Process Mfg.
- ❒ Transportation
- ❒ Utilities
- ❒ Telecommunications 38%
- ❒ Retail
- ❒ Wholesale
- ❒ Banking/Finance
- ❒ Insurance
- ❒ Medical
- ❒ Services
- ❒ Education
- 50% ❒ ~~Federal~~ Energy Government Public Sec
- ❒ State & Local Government
- ❒ Other Industry
- ❒ Consumer/Home
- ❒ Cross-Industry

CYNDC1 Questionnaire No. 20

Introduction Part of Fed business grants to Cont & as appl. to Comm.

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

- Fed mant – 10 Fed – 20 Comm | almost all OS – started Fed at Unisys

A. Recipient Qualification 30 yrs exp

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.) Can use same technical people

Fed/Comm – can't have same sales force; diff. cost accounting struct.

New role – org. of (1) O & G bus BP, etc contr jt vent. Petevesa "Enterprise" Venezuela (2) Utilities – Entergy Scottish Power (on boyonh contr) (3) State & local – San Diego City (4) Fed – Data Sec – FBI (5) SW engineering

Collect related demographics

cont on job for few weeks

2. What is your role?

Rev: $800 – $1 billion

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment - sep team for fed contr capture

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

Comment 50% (incl. State & Local, 4%)

- how much is outsourcing? Comm / Fed.

B. Priority Questions

4. In which vertical industries do you see the best growth potential for IT outsourcing? in US

Comment O+G, Utilities -> Telecom / IT; emerging market = w/ telecom contr. chang.

Total Rev – $5.5 bill, 1999 FY Jan 31

Financial & manuf, exp but static bus little expanded in comm fin sector

CYNDC1 Questionnaire No. ____________

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments OS has changed → 89-90 was commodity/DP outs – last 10 yrs = soc. accept form of bus, comm or gov. Gov has always used contractors → Comm bus later. OS only recently gone →

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments Sales, learn is lack of understand. new market. Fed to Comm – need people who understand that; Comm unit will not be impressed by exp in Fed market

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business? Fed clients are impressed by Comm exp – But would differ in moving into Fed market (regulat)

Comment

large infrast – need cap; other – don't need; leasing will cost client more BOT? can be done

– clients rarely bring work back in house

8. What important changes do you see at work in the outsourcing market today?

Comment:

cust – more sophisticated; OS – more acceptable; CIO's – used to oppose OS → now accept; size of deals getting smaller – control issue

consultants? yes, but consultants can harm cust. (bad by hour)

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments – integr + develop apps – consult
– network & infra mgmt

least – Data center / desktop mgmt

"losers view" depending on consultants; cap Gemini used TPI → can be good

Beyond commodity DP cent

- Large vendors don't want to be in this
- "web hosting"? < co-locate - pure commodity play / Sell RE & elect.
  managed svc.

- excess supply driving prices down

Exodus will fail

PSINet
[illegible]

lack svc expertise

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

Comments

11. What process do you use for computing the cost of contract bidding?

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

cost of sales high → guess not higher

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

Comm - spend same as % of deal - fed deals can be larger. absol. $ equal - % lower & lower margin

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

Not at SAIC - if model → commodity Data Center - Staff Outs not a problem - Value added work → no problem; if client wants to transf; if one - HR proc. Believe important

15. What is your policy toward dealing with unions? (How important?)

unions? will remain marginal

SAIC - low turnover - employee-owned - positive discrimination

Comment ______________________________

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment ______________________________

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment ______________________________

____

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ______________________________

____

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment

____

____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

____

____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ____________________

Phone #: ____________________

Email Address: ____________________

Thank you for your time and consideration.

Growth – 1997 –
Fed. – growing – no long of total revenues

ongoing comm healthcare

Purchase of Bellcore – Bell Labs.
Bought by SAIC

1994 → Fed Comm HC – not successful
1996 → success
1997 – BellC – Telcordia → div of SAIC –
Prof Serv.
devel of prods
lic agreements

Questionnaire No. #21

Printed: 01/30/01

CONFIDENTIAL

7 Feb 01

INPUT Questionnaire

Type of Interview:

- ☑ Vendor ☐ Telephone
- ☐ User ☐ On-Site
- ☐ Other ☐ Mail

Company: EDS

Address:

HQ

City/State: Plano, TX

Zip:

Telephone:

Fax #:

WWW

Project Code/Catalog No. ☐☐|☐☐☐☐|☐☐☐☐

Interviewer Initials ☐☐☐

Interview Date. ☐☐|☐☐|☐☐

QC Initials ☐☐☐

QC Date ☐☐|☐☐|☐☐

Data Entry Initials ☐☐

Data Entry Date ☐☐|☐☐|☐☐

Company Type:

Annual Revenue:

Employees:

Total IS Budget:

Total # IS Staff:

Respondent(s):

Name Robert Grisham Title: VP - Sales

Phone/Ext. 972-605-1054 5250 Direct Email Bobby.grisham@eds.com

Role in Project: —

Referrals:

Industry (User Interviews Only):

- ☐ Discrete Mfg.
- ☐ Process Mfg.
- ☐ Transportation
- ☐ Utilities
- ☐ Telecommunications
- ☐ Retail
- ☐ Wholesale
- ☐ Banking/Finance
- ☐ Insurance
- ☐ Medical
- ☐ Services
- ☐ Education
- ☐ Federal Government
- ☐ State & Local Government
- ☐ Other Industry
- ☐ Consumer/Home
- ☐ Cross-Industry

CYNDC1 Questionnaire No. #21

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A [illegible] nt Qualification

indiv. ref.

[illegible] person who is best able to describe your company's **approach to IT** [illegible] If not, to whom should I speak? (Close the interview and contact the specified [illegible]

____

[illegible] related demographics

2. What is your role? Four divisions – (1) Inf. Solutions 80% (FRAD 05) of comp (4) AT Kerns (3) e-Sol (Web devel, integ) (4) BPO ex DP, Proc

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

Comment 24 yrs with EDS – was Pres of Banking & Sec div (8 yrs) – now MANSF. cont. group → 4 yrs on GM relat. → prime solns for Non Govt US bus

CPA MBA Amer.

3a. Also, what proportion of your company's business, if any, is the U.S. federal market.

Comment ____________________________________

____

B. Priority Questions

4. In which vertical industries do you see the best growth potential for IT outsourcing?

Comment Financial, telecom, manuf. Energy. HC Some fed/public, transp (emerging)

[Air argu current freight.]

Attach new industry?

- we understand dynamics of new market → issue
  then understand segment of market → their IT
  spending priority → then we put EDS capabs.
  to the industry model.

+ STRAT → market → product

- hard to comm.? clients will pay attention
- only as good as last client "
- transition based on image & perf.
- alliances & partnerships.

 Questionnaire No. #21

capit on value to business

role more strategic

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments more toward comprehensive pkg. -> fewer are selecting many vendors + EDS doesn't have 100% partner. usually some IT work remains in-house. cands spend

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

no 1

Comments ability to address business issues -> sol. should be industry specific - also to have gpl. penetr. as well

critical issue is critical mass

7 To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment capital is important factor - no deal ever turned down on capit. avail. basis

leasing? Don't do it typically - feel we can manage better

8. What important changes do you see at work in the outsourcing market today?

Comment: more oct. is strat. - less commodity. In many disc. about bus partner role

9. Top down, which types of outsourcing can you do most profitably? (Reasons?)

Comments

* risk-sharing? have some high-profile relat. on (?) but no STRONG trend toward it. Diff. to measure (cond. p3 for) successful contracts. -> changes all the structure -> benefits disap.

C. Additional Questions

10. In which type of outsourcing do you have the most expertise and success? (Future?)

    Comments

11. What process do you use for computing the cost of contract bidding?

12. Do you have a dynamic model for estimating total contract profitability as changes are made over time?

13. How burdensome are the overall sales & marketing costs associated with winning new outsourcing contracts? (Federal vs commercial?)

14. Has inability to absorb staff transfers from customers impeded your ability to close new outsourcing deals? (Strategy?)

15. What is your policy toward dealing with unions? (How important?)

Comment ____

____

16. How ready is your organization to bid on contracts in the federal (or commercial) market? *What would you need to do to become ready?*

Comment ____

____

17. What changes are you seeing in customer motives for outsourcing IT?

Comment ____

____

18. To what extent does, or should, company size (based on annual revenues) influence a decision regarding whether to outsource?

Comment ____

____

19. In relation to outsourcing, how sensitive are your customers to the issue of control, in general, and control of proprietary data in particular?

Comment

____

____

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)

Comment

____

____

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information:

Name/Title: ______________________________

Phone #: ______________________________

Email Address: ______________________________

Thank you for your time and consideration.

Questionnaire No. #22
Printed: 02/08/01~~02/07/01~~

CONFIDENTIAL

INPUT Questionnaire

Type of Interview:

X☐ Vendor ☐ Telephone
☐ User ☐ On-Site
☐ Other ☐ Mail

Company: Perot Systems Corporation
Address: 12404 Park Central
City/State: Dallas, TX
Zip: 75251
Telephone: 1-877-737-6973
Fax #: 972-340-6100
WWW.perotsystems.com

Project Code/Catalog No. ☐☐-☐☐☐-☐☐☐☐
Interviewer Initials ☐☐☐
Interview Date. ☐☐-☐☐-☐☐
QC Initials ☐☐☐
QC Date ☐☐-☐☐-☐☐
Data Entry Initials ☐☐
Data Entry Date ☐☐-☐☐-☐☐
Company Type: Consulting & Computer Services
Annual Revenue: $1.1 billion
Employees: 7000
Total IS Budget:
Total # IS Staff: ____________

Respondent(s):
Name Andy Tramel Title: Relationship Manager
Phone/Ext. 972-577-7296 Email: andrew.tramel@ps.net
Role in Project: ____________

Referrals:

____

____

Industry (User Interviews Only):

X Discrete Mfg.
X Process Mfg.
X Transportation
X Utilities
X Telecommunications
X Retail
X Wholesale
X Banking/Finance
X Insurance
X Medical
X Services
☐ Education
☐ Federal Government
☐ State & Local Government
☐ Other Industry
☐ Consumer/Home
☐ Cross-Industry
____

Introduction

The purpose of this survey is to determine how vendor attitudes toward IT outsourcing are changing. The survey also aims to track the evolution of vendor attitudes and practices in regard to specific aspects of outsourcing.

You will be provided with an executive summary of the results of this survey.

A. Recipient Qualification

1. Are you the person who is best able to describe your company's **approach to IT outsourcing?** If not, to whom should I speak? (Close the interview and contact the specified person.)
   Yes

   Collect related demographics

2. What is your role?

   Comment: Individually, I manage relationships with Clients

   As a company, we assist customers with aligning, managing and applying technology toward client business objectives.

3. Please indicate the nature of your experience with outsourcing (IT or otherwise).

   Comment: I have been in the IT outsourcing field for 5 years. I began my career at EDS where I achieved Inner Circle Status as one of the top sales people globally. I now represent Perot System's Integrated Solutions Group and am one of the top sales people representing this group.

3a. **Also, what proportion of your company's business, if any, is the U.S. federal market.**

   Comment: None

B. Priority Questions

4. In which vertical industries to you see the best growth potential for IT outsourcing?

   Comment: Financial Services, Manufacturing and Healthcare

5 Is your business moving "upmarket" toward entire business processes or "downmarket" toward more commodity transaction processing?

Comments: Perot Systems is focused on the "upmarket".

6. How would you categorize the most important barrier to entering a new market, financial? Technical? Marketing? Organization? Staffing? Management? Other?

Comments:
It is my opinion that financial and organizational are equally difficult barriers. Successful existing business units are competing for the same capital resources and have a proven track record and history. One of the key areas affecting your ability to obtain capital is the proposed organizational structure. Financial and organizational alignment should be considered part of your strategy while marketing, technical, and staffing is more tactical in nature and is something you can leverage from existing business units.

7. To what extent is cost or availability of capital a constraint in bidding for new outsourcing business?

Comment
As we all know pursuit cost can be very expensive. With that being said, capital to pursue an opportunity that we believe has a high probability of Perot Systems being successful is not a factor in our opportunity pursuits. Capital allocation requests for pursuits are denied only when we perceive there is a less than average chance of being successful.

8. What important changes do you see at work in the outsourcing market today?

Comment:
The ability to do something better, faster and cheaper is the price of entry today. Clients today are looking for strategic partners that offer breadth and depth. Clients are seeking ways that they can drive business to fewer partners and hold them accountable for the results. Basically treating their service providers as an extension of their IT department and business units.

One other area that we, the incumbents, seem to be ignoring is the possibility of new competitors in our space. We have done a very good job of placing concern into our clients that in the new economy paradigm competitors are in every vertical. We point to Enron and others as examples. The creation of shared services groups that are independent of their parents possess industry knowledge, relationships, and an understanding of industry applications and technologies that can be tapped as solutions. They have been authorized to capture revenue from other firms but because of their organizational structure have not been successful. I see these as potential back office competitors. One the front end what if Amazon, Yahoo or Ebay decided to get into the CRM space? The virtual companies we are building today possess the skillsets and knowledge to be our potential competitors tomorrow.

20. Is the bulk of your OS business in bundled, or unbundled services? (Preference? trend?)
   Comment
   Today the bulk of our business is bundled but we are moving towards unbundled. Our preference is to manage in a bundle, but it doesn't matter what we want, it's what the client wants and feels comfortable with in the scope of a relationship.

As I mentioned, we will send you an executive summary of the data derived from this survey. Please confirm the following contact information: Name/Title: Andy Tramel, Relationship Manager Phone #: 972-577-7296 Email Address: andrew.tramel@ps.net

Thank you for your time and consideration.