INPUT

STRATEGIC MARKET PERSPECTIVE

Outsourcing Vendor Performance Analysis

U.S. Outsourcing Program

MARCH 1996

Outsourcing Vendor Performance Analysis

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Abstract

Outsourcing has grown aggressively over the last several years. It seems the perfect solution to bloated, overstaffed organizations that recognized the information technology expertise of others and sought to take advantage of that by moving some company functions out of house. But, how has that gone? Is it the solution for which companies had hoped? And the vendors, are they performing up to expectations? These and other questions of satisfaction with outsourcing were the focus of this study.

Research for this report included data gathered from over 50 North American companies who are actively engaged in outsourcing one or more information systems functions. Data from fifty-four European outsourcing users was also used on a comparative basis. Interviews were also conducted with vendors and selected industry experts and a review of secondary information sources was conducted to ensure comprehensive coverage of this marketplace.

Users report generally positive results with both the approach of outsourcing and with vendors' outsourcing performance. Both are graded in the "acceptable" to "good" range. These results are, however, below user expectations for either the goals of outsourcing or its practice. Cost effectiveness and ability to control costs were cited as key shortcomings by a majority of users. Users also noted concerns over vendor performance criteria such as understanding requirements, on-time delivery, and responsiveness. Terms and conditions were generally rated as satisfactory.

The report identifies a number of vendor initiatives that could lead to the elimination of discrepancies between user expectations and vendor performance.

This report contains 62 pages, including 49 exhibits.

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Outsourcing Vendor Performance Analysis

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I

Introduction

Outsourcing mega-deals make good headlines and lead to the assumption that users are satisfied both with the benefits of outsourcing and with the chosen outsourcing vendors. But is this the case? Are users really satisfied or do they find themselves forced into outsourcing by seemingly uncontrollable forces including downsizing, lack of in-house expertise, or fiscal issues? Answers would not only provide direction to users anticipating outsourcing, but also offer guidance to vendors in terms of what additional features/benefits might increase customer satisfaction.

A

Scope and Purpose

1. Scope

This report is one of a series of INPUT reports on the outsourcing market—see section D (Related INPUT Reports) below. As with most of the INPUT reports on this marketplace, this analysis of customer satisfaction focuses on commercial companies currently engaged in outsourcing arrangements. Outsourcing is operationally defined (see Appendix A for a formal definition) as the provisioning of one or more of the following services:

- Day-to-day operation of mainframe and/or standalone mid-range computing equipment
- Desktop services, especially day-to-day management of the company's personal computer infrastructure (e.g., servers and LAN)
- Network management, the day-to-day management of the corporate data network
- Applications management, that is, support and maintenance of in-house applications, including responsibility for new systems development

- Business operations management of specific functions such as accounting, human resources, and fulfillment

2. Purpose

The purposes of this research, analysis, and report are to provide benchmarking data on the performance of outsourcing vendors and to analyze customer requirements and corresponding satisfaction levels and the extent of unmet needs. On the former, this research seeks to detail the forces that drive users to outsourcing and, correspondingly, the extent to which the practices of outsourcing seem to satisfy these needs. For the latter purpose, data is presented to identify the user criteria for vendor selection and the extent to which users perceive their outsourcing vendors to be meeting or exceeding these criteria.

Specific questions addressed are:

- What is the level of vendor performance in aggregate in meeting customers' needs?

- What are the major benefits sought by customers, and vendors' performance in meeting these expectations?

- What are the key areas for improvement by outsourcing vendors, particularly in identifying and addressing the unmet needs of customers?

Readers of this report will be assisted in a number of ways:

- Vendors will be able to identify weaknesses perceived by users.

- Vendors who act on these perceptions will likely stem the loss of existing business.

- Vendors will be able to compete more effectively through identification of unmet needs.

- Users will be better able to develop criteria for evaluation of a vendor's strengths and weaknesses.

- Users will be more prepared to negotiate improved services and performance levels from existing or prospective vendors.

B
Methodology

This report is based on telephone interviews conducted with knowledgeable representatives of companies currently outsourcing one or more functions as defined above. In total, 54 interviews were conducted with North American companies representing a cross-section by industry type and revenue size (See Exhibit I-1).

Exhibit I-1

Industry and Revenue Profile of Respondents' Companies

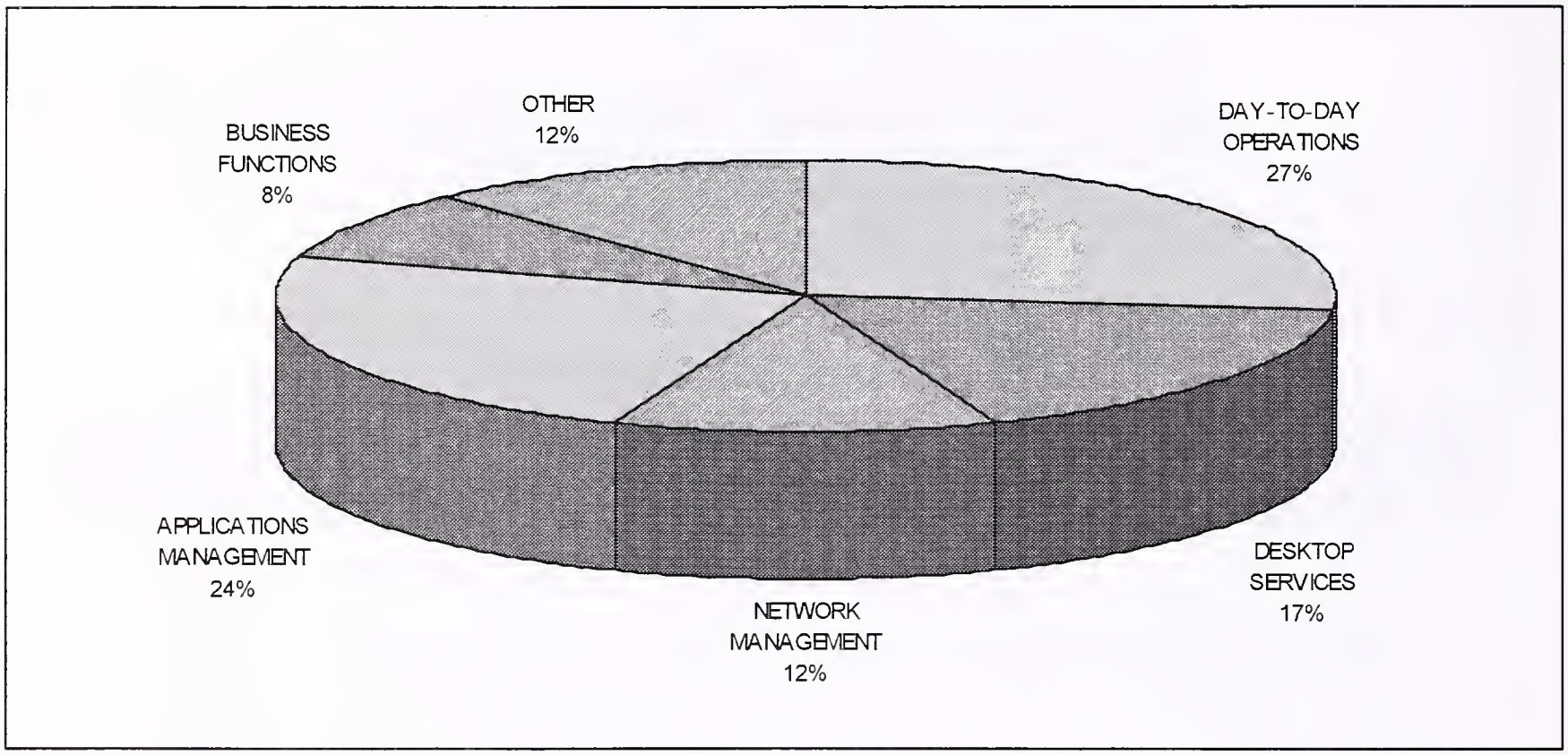
Vertical Market	Percent of Sample (%)	Revenue (Minimum $M)	Revenue (Maximum $M)
Banking/Finance	19	15	6,900
Process Manufacturing	15	300	16,300
Discrete Manufacturing	9	170	5,000
Utilities	9	400	3,900
Federal Government	9	NA	NA
Transportation	7	620	5,700
Services	6	137	955
Other Industry-Specific	5	NA	NA
Communications	4	1,400	11,700
Wholesale	4	2,000	2,300
State & Local Government	4	NA	NA
Insurance	2	DK	DK
Medical	2	150	150
Education	2	300	300
Cross-Industry	2	7,300	7,300

Note: Numbers have been rounded *Source: INPUT*

The survey also included a sampling of outsourcing views by function. A total of 109 outsourced functions were mentioned by the 54 respondents. As indicated in Exhibit I-2, all five of the possible outsourced areas were well represented. The traditional strongholds of outsourcing (i.e., day-to-day mainframe/mid-range operations, applications management) were the leading functions reported. Desktop services, a recent new opportunity, and network management were also frequently mentioned. Specific business functions (e.g., human resources, distribution) were the least frequently mentioned outsourced areas.

Exhibit I-2

Frequency of Mention of Outsourced Functions



Source: INPUT

Finally, the surveyed companies reported a large number of vendors who were providing outsourcing: 31 different vendors were mentioned in the 109 outsourced areas. Exhibit I-3 shows the vendors with multiple mentions along with the frequency of total mentions and the number of outsourced functions for which that vendor was mentioned. These 12 vendors represent 63% of the total mentions in the sample. Clearly, the respondents reflect a wide spectrum of outsourcing activity.

Exhibit I-3

Leading Vendors Mentioned by Respondents

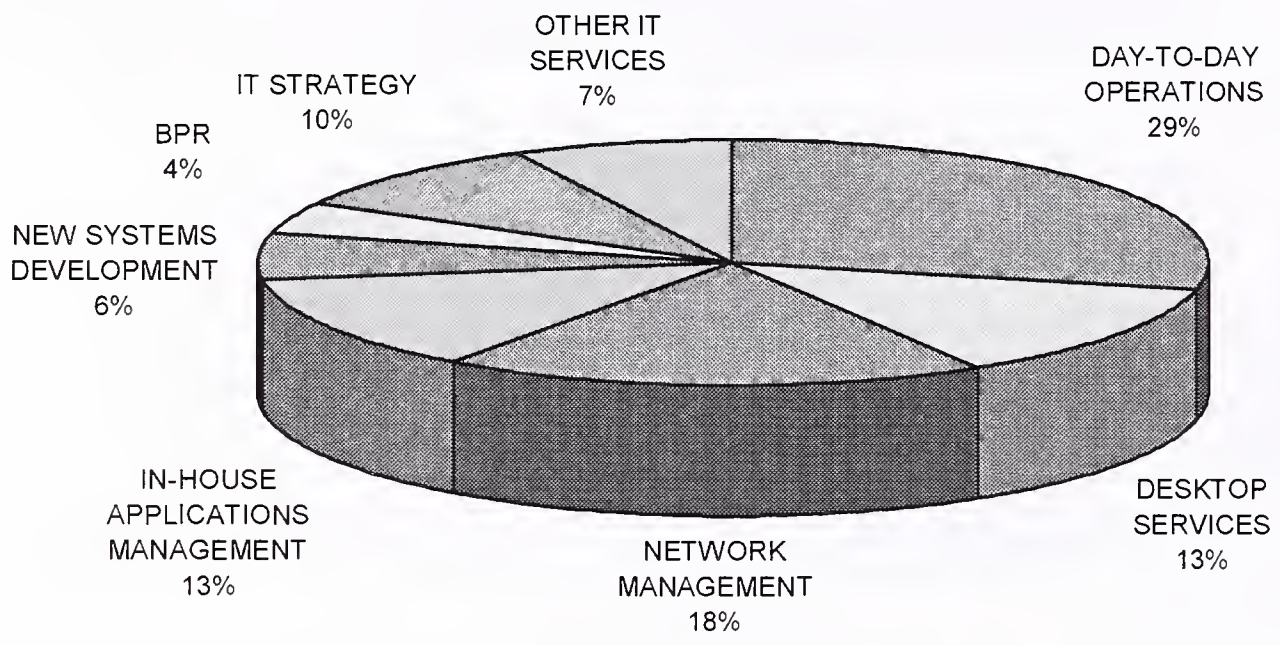
Vendor	Percent of Total Mentions (%)	Number of Outsourced Functions Mentioned
EDS	28	5
SHL	7	4
ISSC	6	4
CSC	4	3
Genix	4	2
Andersen Consulting	3	2
Lockheed Martin	3	3
M&I Data Services	3	2
ACS	2	2
AT&T	2	2
First Integrated Systems	2	2
ALLTEL	2	1

Source: INPUT

INPUT recently completed a similar study of user satisfaction with outsourcing vendors for its European program. Data from that research effort, conducted in a manner similar to that described above for the North American companies, is included in this report for comparison purposes. That data, separately identified throughout this report, included 55 respondents employing outsourcing in a number of functional areas identified in Exhibit I-4.

Exhibit I-4

Frequency of Mention of Outsourced Functions for European Respondents



Source: INPUT

C

Report Organization

Chapter I—Introduction—This chapter describes the purpose, methodology, and organization of the report.

Executive Overview—Chapter II presents an overview of the emerging applications of the Internet and its equivalents.

Aggregate Vendor Performance—Chapter III reviews the satisfaction from the required versus received satisfaction continuum. This analysis aggregates data across all outsourcing service types.

Satisfaction with Outsourcing Analyzed by Type of Service—Chapter IV provides an analysis similar to that of Chapter III for each service type.

Appendix A provides a definition of terms used in this report.

Appendix B includes a copy of the questionnaire used during the telephone interviews.

D
Related INPUT Reports

Other reports from INPUT that could be of interest in relation to this report include:

- *Impact of the Internet on Outsourcing and Processing Services Markets*
- *Pricing and Marketing of Outsourcing Services*
- *Negotiating Outsourcing Contract Terms and Conditions*
- *Analysis of Leading Outsourcing Vendors*
- *U.S. Outsourcing Market Analysis, 1994-1999*
- *The Impact of Business Process Reengineering on Outsourcing Services*
- *Desktop Services User Perspectives*
- *The Role of the CFO in Outsourcing Decisions*

In addition to these reports, profiles are available on many outsourcing vendors. Examples of the companies profiled by INPUT include:

- *ALLTEL Information Services , Inc.*
- *Andersen Consulting*
- *AT&T GIS*
- *Bell Atlantic Network Integration, Inc.*
- *CAP Gemini America*
- *Computer Sciences Corporation*
- *Coopers & Lybrand*
- *Digital*
- *EDS*
- *Ernst & Young*

- *FIserv, Inc.*
- *Genix*
- *Hewlett-Packard*
- *I-Net, Inc.*
- *ISSC*
- *SHL Systemhouse*
- *Unisys*

II

Executive Overview

The outsourcing market has grown considerably over the last several years and shows every sign of continuing to do so. Nevertheless, there appear to be lingering doubts about the real benefits of outsourcing and about vendors' abilities to perform to the levels of expectations of users. This report addresses these concerns by presenting data collected from a sample of current outsourcing users. Respondents were asked to address not only their evaluation of vendor performance by type of business function outsourced, but also were asked to identify any gaps in their expectations versus their experiences with the very concepts of outsourcing.

A
User Satisfaction with Outsourcing

Users' desire to increase the cost effectiveness of their IT function lead the list of goals reported by outsourcing users. Though there appears to be little evidence that outsourcing results in net savings, users nevertheless continue to believe—perhaps with vendor encouragement—that costs will be reduced, effectiveness will be increased, and new value will be claimed for the IT dollar (see Exhibit II-1).

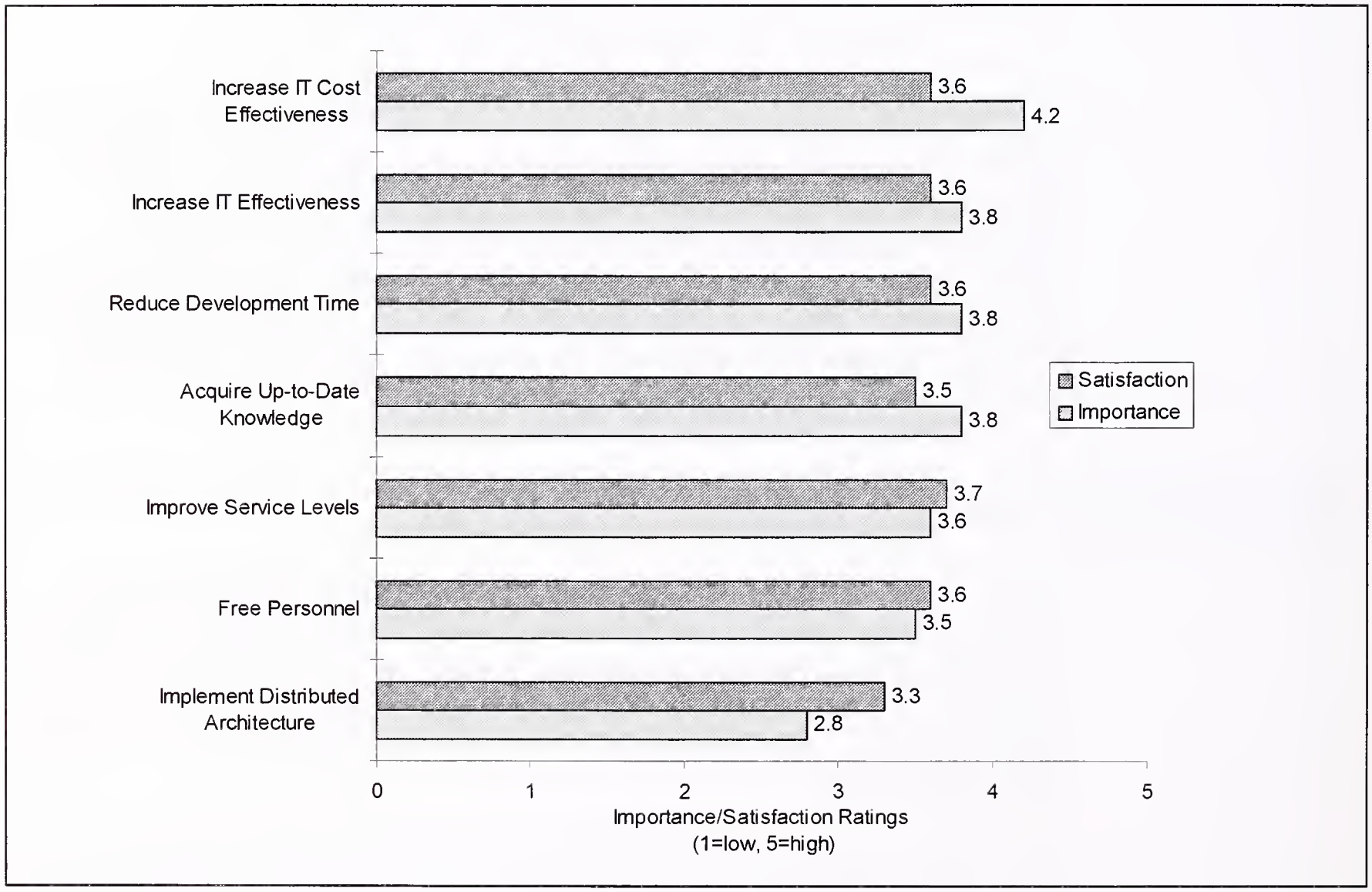
Users rate a number of goals as somewhat secondary to this; they seek reduced development time, the acquisition of up-to-date knowledge, improved service levels, and freeing of personnel for other assignments. Somewhat less important to users is the ability to adopt a distributed rather than a centralized architecture through an outsourcing strategy.

Satisfaction is generally less than the importance of the goal, according to respondents, but the gaps are not severe, except for disappointment in improving cost effectiveness to levels required by users. On three criteria—freeing personnel, improving service levels, and implementing a distributed architecture—satisfaction ratings exceed importance ratings.

These positive impacts and the near-congruence on some of the other criteria offset the lack of improvement in cost effectiveness. But the importance attributed to this criterion for successful outsourcing and the gap with reported satisfaction suggests that this single issue is a potentially dangerous point for vendors. Users need to be refocused on other benefits if vendors cannot deliver cost effectiveness or high expectations of improvement in cost effectiveness must be mitigated by more realistic expectations.

Exhibit II-1

Outsourcing Importance-Satisfaction Gap Analysis



Source: INPUT

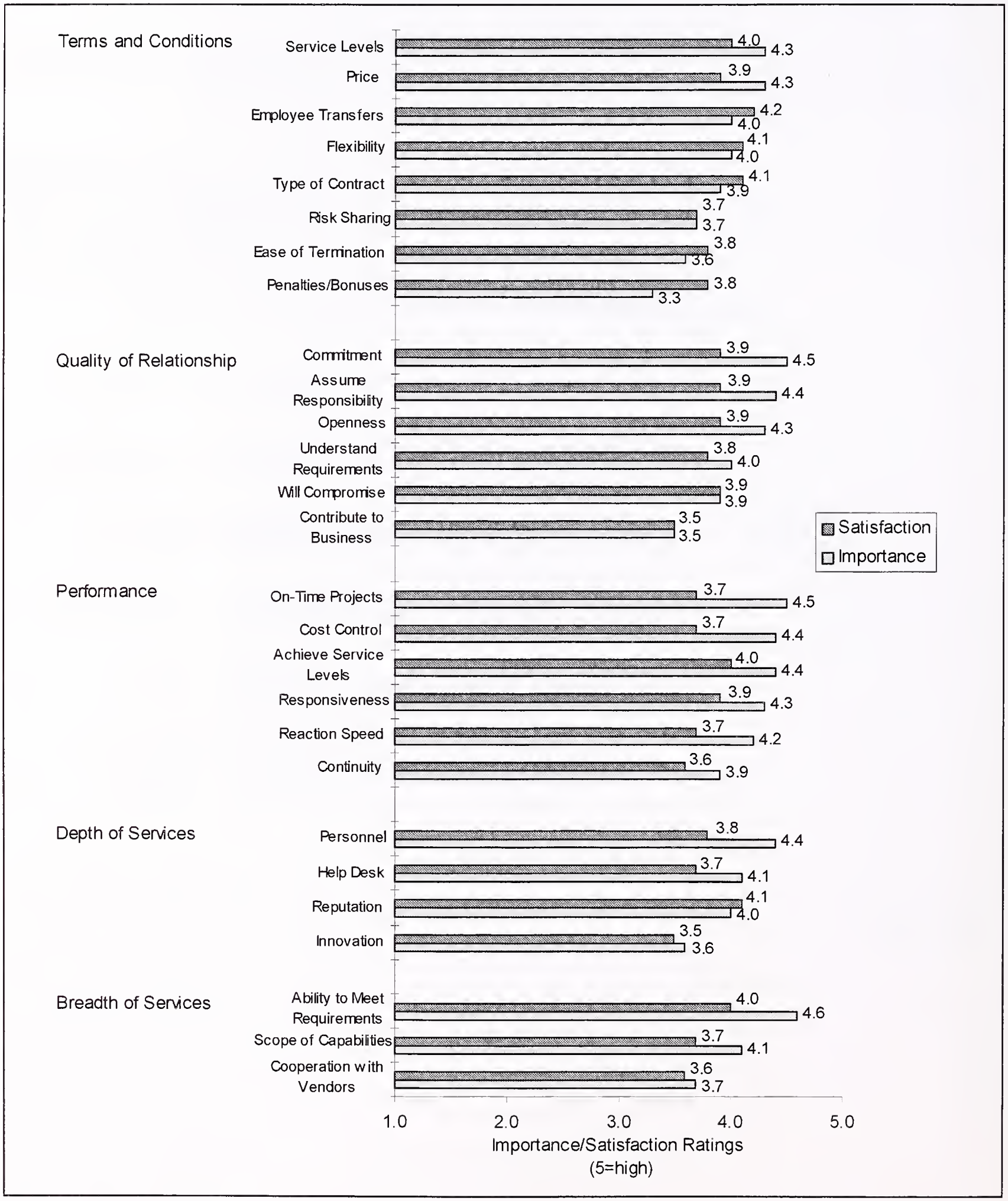
B
User Expectation-Vendor Performance Gap

Actual outsourcing vendor performance is compared to the expectations of users in Exhibit II-2. These ratings are grouped into five issue categories identified to the left of the ratings.

- As a group, vendor performance dominates users' ratings of important vendor criteria. Getting the job done is the number-one goal, but doing it in such a way that engenders a quality relationship between user and vendor is very important as well. Depth and breadth of vendor service offerings are tertiary issues and actual contract terms and conditions are less important.

Exhibit II-2

Aggregate Rating of Vendor Outsourcing Performance



Source: INPUT

- Ability to meet requirements and specifications is the single most important criterion. Other highly rated criteria include the delivery of projects on time, the capabilities of the vendor's personnel, and the level of vendor commitment to the user. Users clearly report that they view outsourcing as an opportunity to improve their IT operations and single out vendor criteria that seek to ensure this improvement. Interestingly, these criteria are generally more important than price; apparently, users are willing to pay to have their expectations surpassed.

- Users don't have to worry about that, according to them, for vendors underperform on nearly all criteria and, when they do meet or exceed expectations, their areas of success are not very important to users: penalties and bonuses of contracts, ease of contract termination, and type of contract.

- Large discrepancies are reported on a number of critical criteria, including ability to meet requirements/specifications, on-time delivery of projects, quality of the vendor's personnel, cost control, and vendor commitment to the outsourcing effort. While individually these may not be deal makers and, as a group, vendor performance ratings are above average, as a group these ratings suggest that users are unhappy with vendor performance. No specific criterion is large enough to warrant deal breaking, but the collective feeling may give users pause as contracts are renegotiated. Indeed, many users did report that changes in vendors or in contracts were planned. Most of the reported plans focus on achieving additional control over the vendor's performance, further defining roles, and refocusing on containing costs and increasing effectiveness.

C

Outsourcing Goal Satisfaction by Business Function Outsourced

The largest outsourcing goal-performance discrepancies, both positive and negative, are presented in Exhibit II-3. The largest discrepancies are reported for users of each particular type of outsourcing: day-to-day operations, desktop services, network management, application development management, and business operations. Criteria above the diagonal line received satisfaction ratings that exceeded users' expectations, while ratings below the diagonal line indicate satisfaction that was less than desired by users.

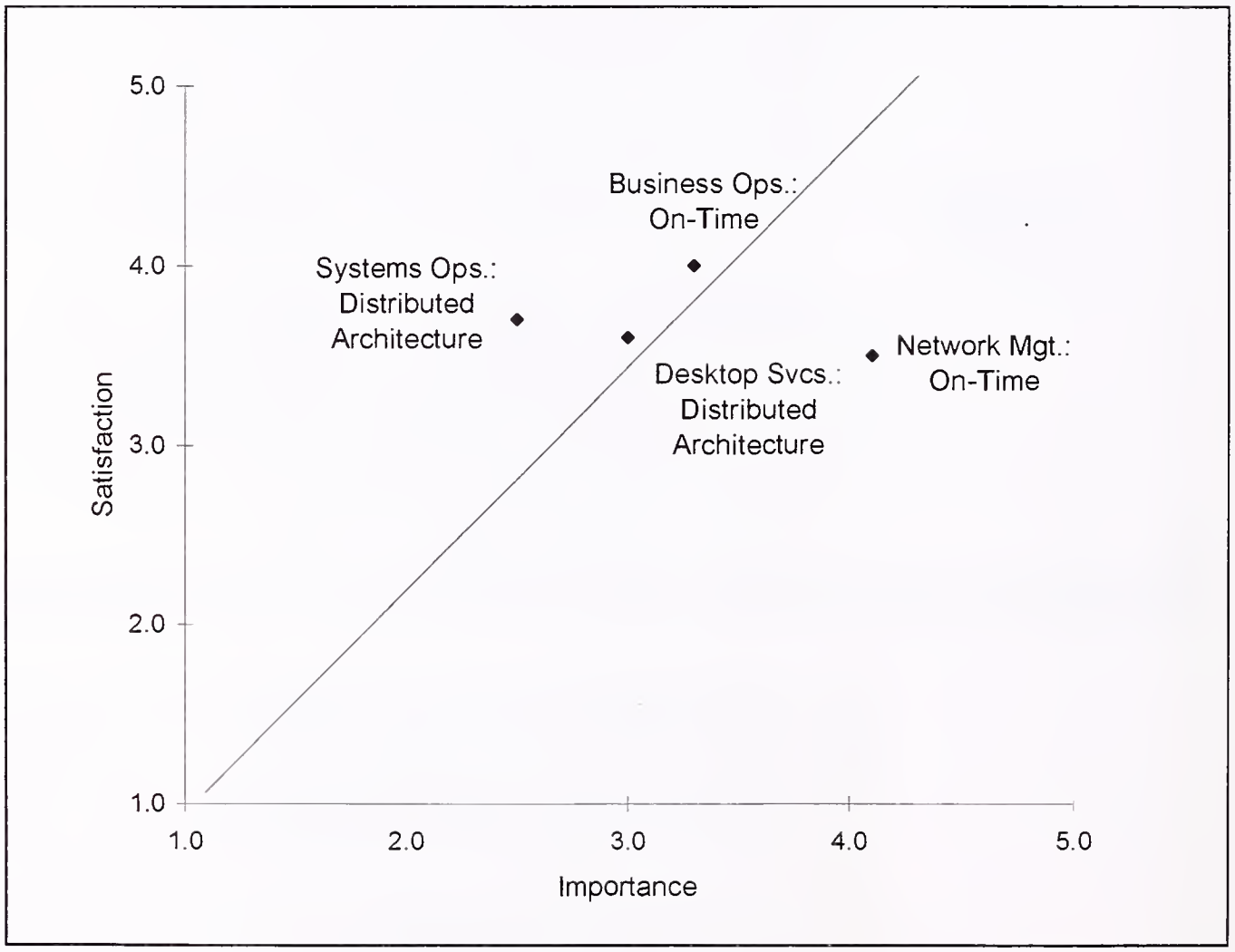
- The most frequently cited satisfying element of outsourcing for these various types of outsourcers was the ability to adopt a distributed rather than a centralized architecture. Though this was not a major goal for outsourcing, users were impressed with this unexpected result. The only other large positive result for an outsourcing segment was on-time

delivery of projects reported by those who outsource entire business functions. This finding is clearly a pleasing one for all parties, as on-time delivery satisfaction was generally not highly rated by users in other segments. Apparently, the closer relationship of user and vendor in these situations compels vendors to adhere more to the commitment to deliver on-time. Also, outsourcing whole business functions may require the kind of specification that leads to few surprises and better ability to meet deadlines. Either way, users are impressed.

- Less impressive is this same on-time delivery by users who outsource application management and network management. Both rated missed schedules as the biggest disappointment of those items queried.

Exhibit II-3

Largest Outsourcing Importance-Satisfaction Rating Discrepancies by Type of Outsourcing Service



Source: INPUT

- The other criterion that was rated with the largest negative discrepancy between expected and actual performance in outsourcing was cost effectiveness. As mentioned above, users in mainframe (day-to-day) outsourcing, desktop services, and business functions are dissatisfied with the inability to improve cost effectiveness through outsourcing. In these

instances the expectations were not overly high (4.0 range out of 5) and outsourcing still did not deliver (ratings in the 3.5 range).

- Overall, these negative ratings are not severe in terms of the amount of discrepancy between expected and actual, but may be so in terms of the issues involved. That is, lack of on-time performance and failure to improve IT cost effectiveness as much as anticipated may lead users to reconsider the value of outsourcing.

D
Vendor Performance by Business Function Outsourced

Discrepancies in vendor performance vis-à-vis expectations for each of these outsourced segments are presented in Exhibit II-4.

- Penalties and bonuses were viewed as a positive by those outsourcing applications management, but expectations were relatively low so any contracting activities in this direction might have exceeded expectations.

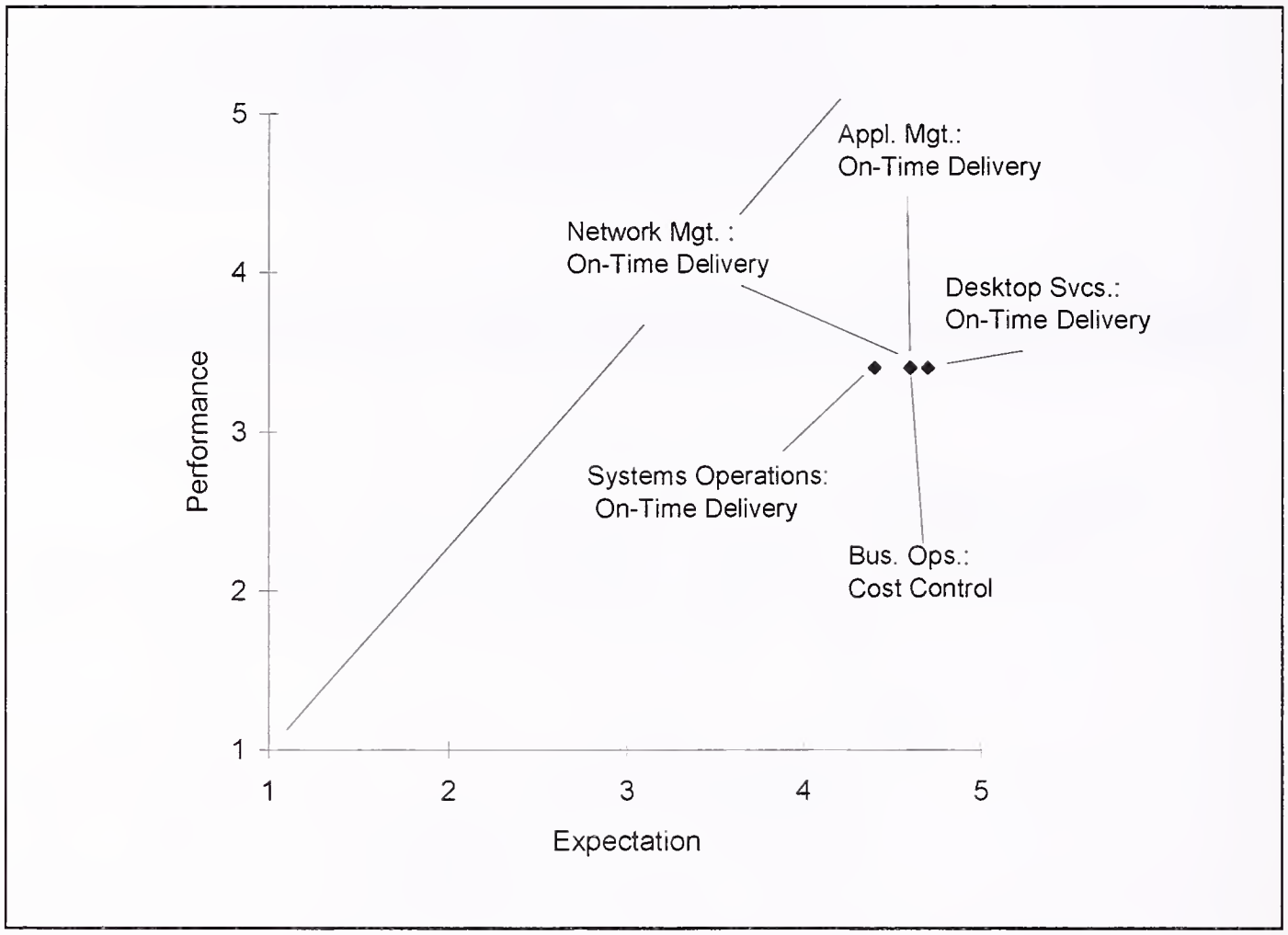
- Network management outsourcing vendors as well as vendors providing day-to-day operations are perceived to have an even stronger reputation after contracting than during vendor selection. Companies may be finding that, while they use this (i.e., vendor reputation) as a selection criterion, end users use it as a benchmark of the vendor's capabilities and these vendors are meeting or beating expectations. For those who do the selecting, the suggestion is that good vendor reputations will help sell outsourcing to the ultimate users.

- Those outsourcing desktop services generally transfer some or all of their help desk employees to the vendor. They hope that this transfer will be smooth and as pleasant as possible for their employees. And for these respondents that seems to be the case; users report that vendors surpass expectations in this regard.

- Vendors also surpass rather high user expectations for vendor flexibility in business function outsourcing. Again, users seem to be finding that vendors can be advisors, partners, or change agents and assume a number of required roles depending on the needs of the company when entire business functions are at stake. Partner roles like these may be the ultimate key to success for all of outsourcing.

Exhibit II-4

Largest Outsourcing Expectation-Performance Rating Discrepancies by Type of Function Outsourced



Source: INPUT

The largest discrepancies for each of the different types of outsourcing involve lack of cost control for outsourcing of business operation functional areas and lack of on-time delivery for the other four types of services. Failure to be on time and within budget are two shortcomings of outsourcing vendors, according to these respondents. Vendors should review their performance on these dimensions and take steps to deliver better results. Otherwise, users will have additional opportunities to reconsider the outsourcing decision or the vendor(s) selected.

III

Aggregate Vendor Performance

This chapter provides a review of respondents' goals in deciding to outsource all or part of their IS functions, the level of satisfaction they have achieved in reaching these goals through outsourcing, the metrics users want to apply to assess vendor performance, and, finally, users' perceptions of actual outsourcing vendor performance against these metrics. Data is presented in the aggregate, across all outsourcing services, to assess overall satisfaction with outsourcing as an approach and with the current outsourcing vendor(s). Chapter IV presents a similar analysis on a service-by-service basis.

A

Service Requirements

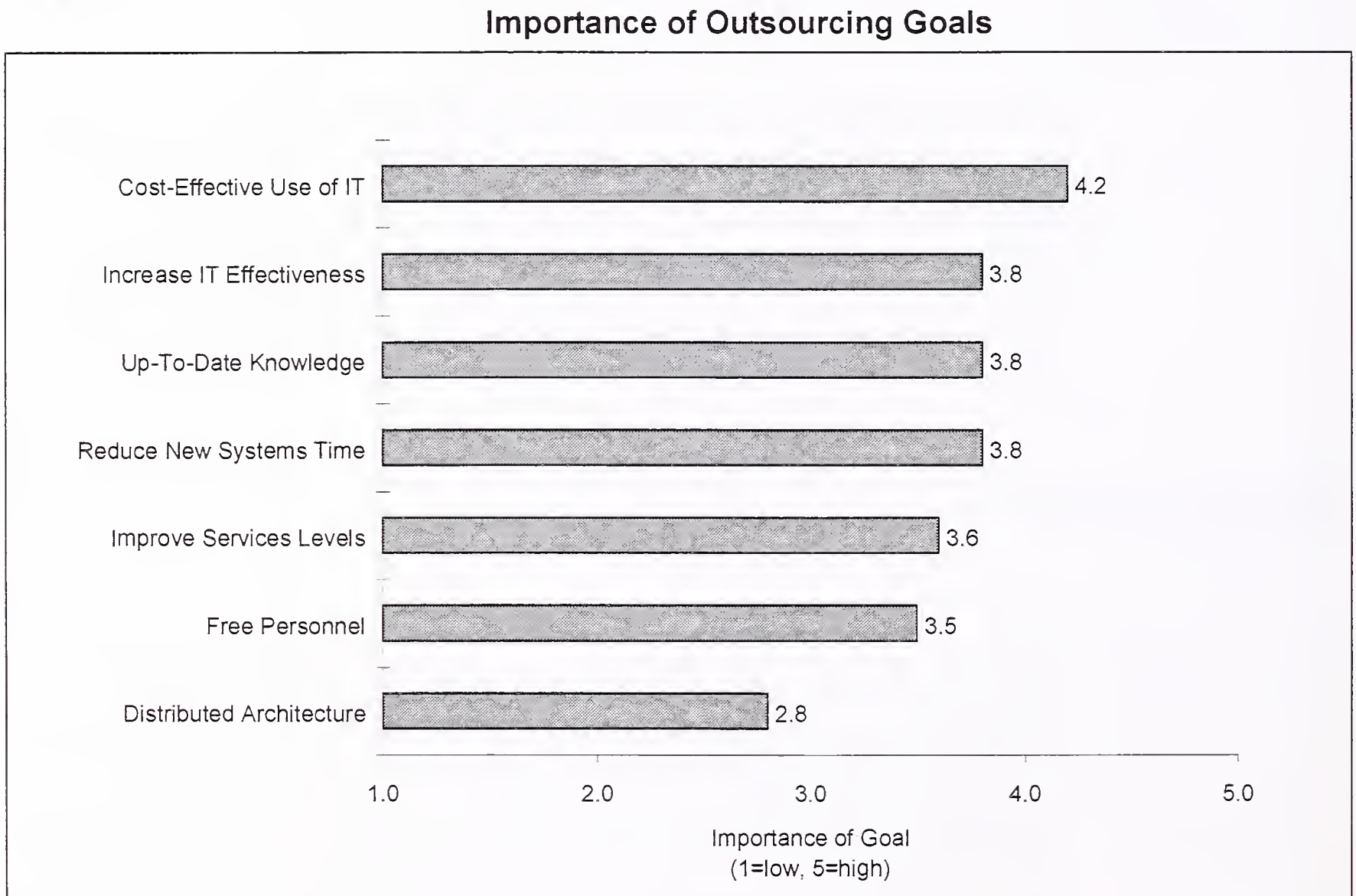
1. Outsourcing Goals

Users are drawn to outsourcing for a number of reasons; a search for cost-effective IT is reported by these users to be the most important goal in choosing to outsource (see Exhibit III-1). The belief is that vendors who manage IS functions as a business should be better at it (more effective) than the in-house group that is "forced" to provide IT services as a means to support the business of the user's company. Further, buying these services from outsiders should be less expensive than providing them in-house both because of a vendor's economies of scale and because of competitive control over price that the market can exert.

To a lesser extent, users seek to improve their operation. Outsourcing implies access to up-to-date knowledge, a reduction in time to develop new systems, and an increase in IT effectiveness by a change of focus on what is relevant (i.e., only the most important activities will be acquired from the outside; secondary information services will be dropped).

Apparently, outsourcing more frequently represents a means to a better IT organization than a way to patch up problems in the current organization.

Exhibit III-1



Note: Number of respondents = 54

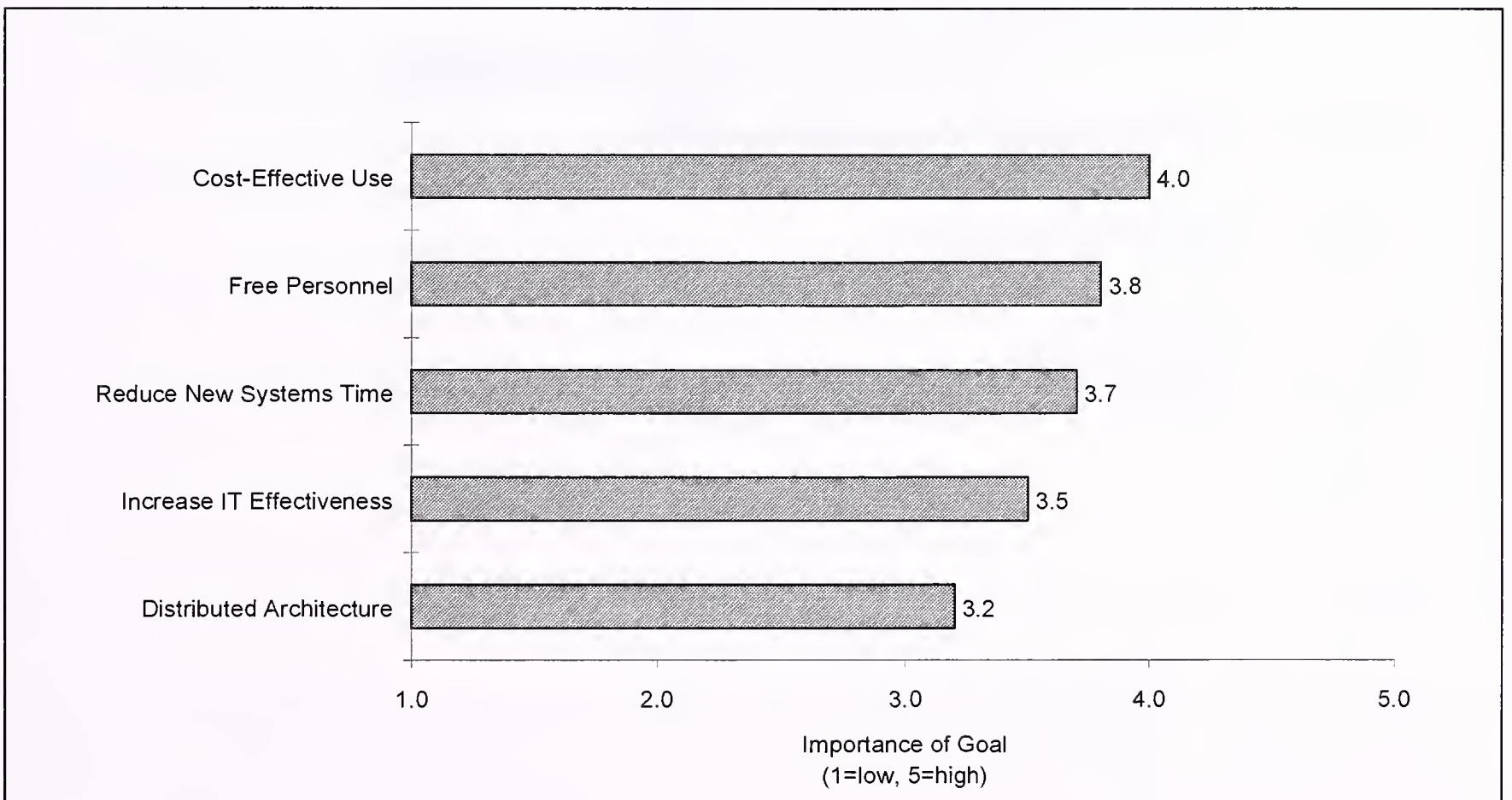
Source: INPUT

Similar ratings from the European study of outsourcing performance (see Exhibit III-2) confirm these user perceptions. Cost effectiveness is the number-one goal. Goals that focus on fixes or improvements are rated as secondary to cost effectiveness, and changes (e.g., adopting a distributed architecture) are least important to the European respondents. This order is essentially the same as for the North American respondents. (The same questions were not asked of each sample, so complete comparisons are not possible.)

When users were asked through an open-ended question what issues might prevent them from outsourcing, the most frequent reply related to its cost and, second, its effectiveness. This is another indication of the importance of cost effectiveness to users. Interestingly, ability to maintain control over the vendor (sometimes referred to as vendor "flexibility") was also a key issue. The discussion of expected roles below confirms this strong need to control the outsourcing vendor.

Exhibit III-2

Importance of Outsourcing Goals in Europe



Note: Number of respondents = 55

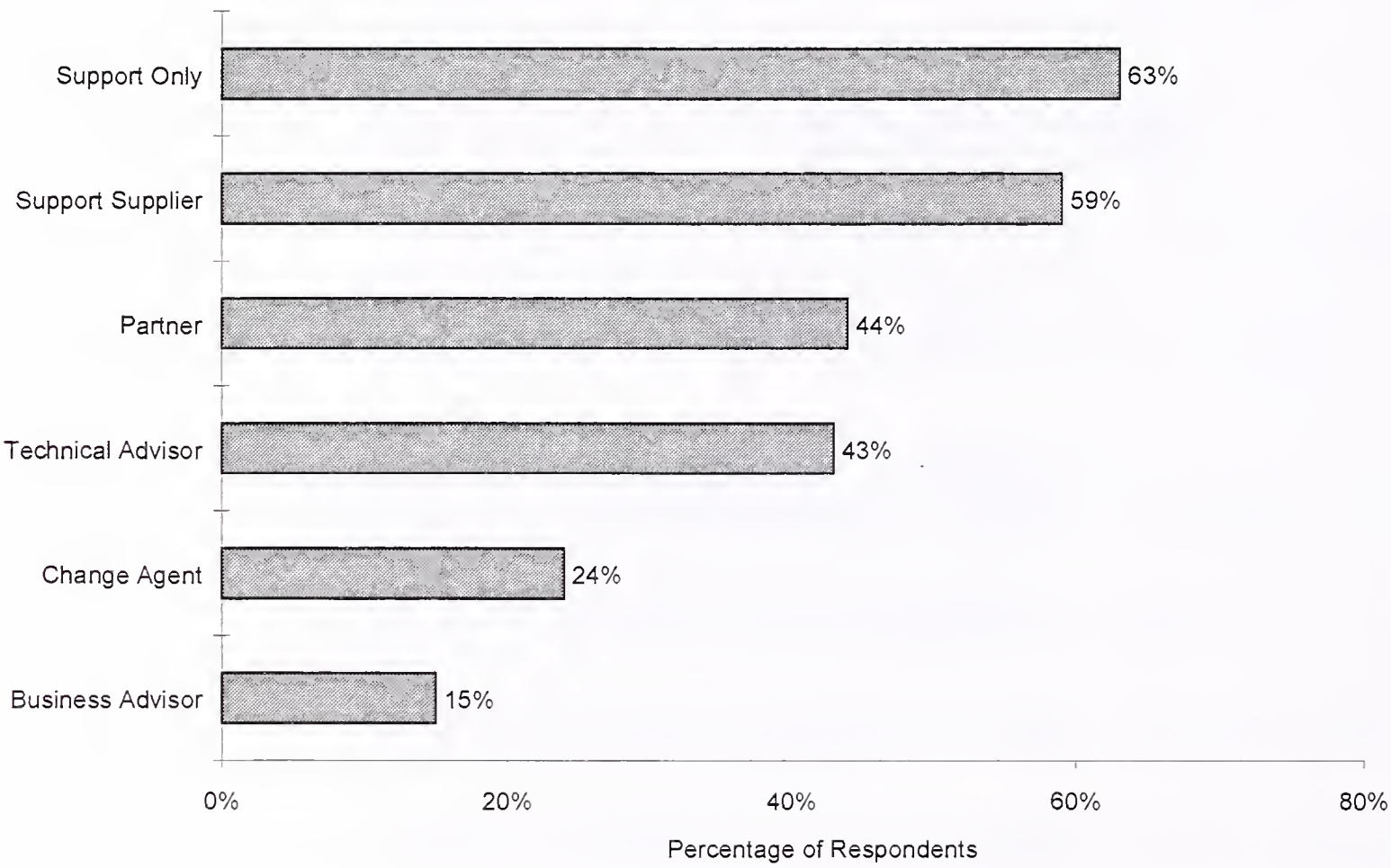
Source: INPUT

2. Vendor Roles

In line with this view of outsourcing, users expect that vendors will most often be suppliers of IT services (see Exhibit III-3). Less than half of the respondents also wanted their outsourcing vendor to be a partner or advisor on technical issues. The broadest roles, those of change agent or business advisor, were reported to be tertiary roles less frequently required of vendors.

Exhibit III-3

Vendor Roles Desired by Customers



Source: INPUT

Taken together, these results indicate an inverse relationship between the users' expectation of vendor roles and the breadth of these roles. The broader the role is in extent beyond technology and into the business of the company, the less interest users have in vendors filling that role. Although it is possible for vendors to change users' perceptions in the course of a working relationship, these results suggest that the strategies of expanding from advisor to vendor or vice versa are not particularly in step with users' perceptions of the roles of outsourcing vendors.

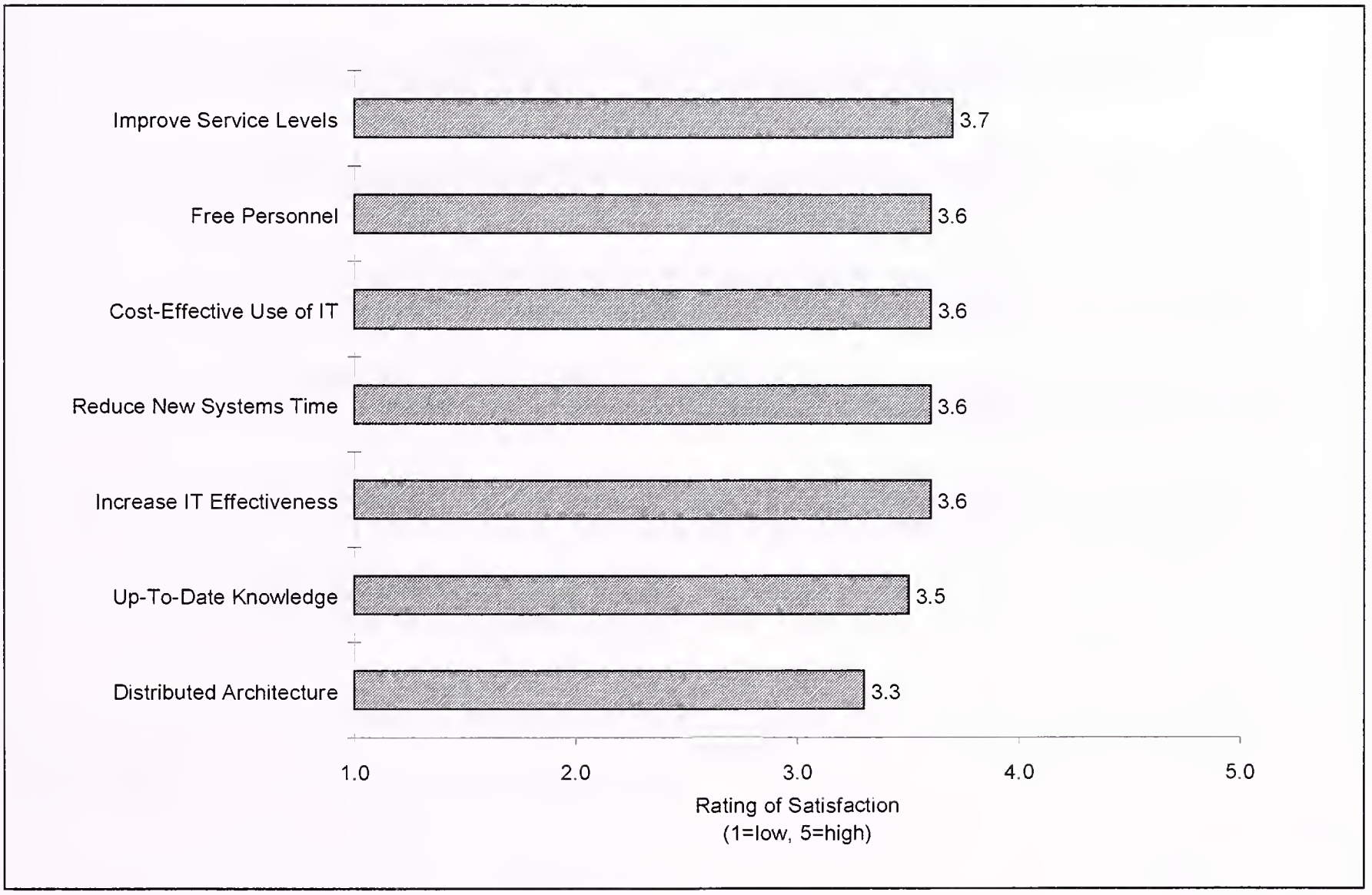
B
Service Performance

1. Outsourcing Goals

Respondent satisfaction with outsourcing is presented in Exhibit III-4 for the North American respondents and Exhibit III-5 for the European respondents. In general, outsourcing receives an "average" grade from both sets of respondents.

Exhibit III-4

Customer Satisfaction with Outsourcing Approach



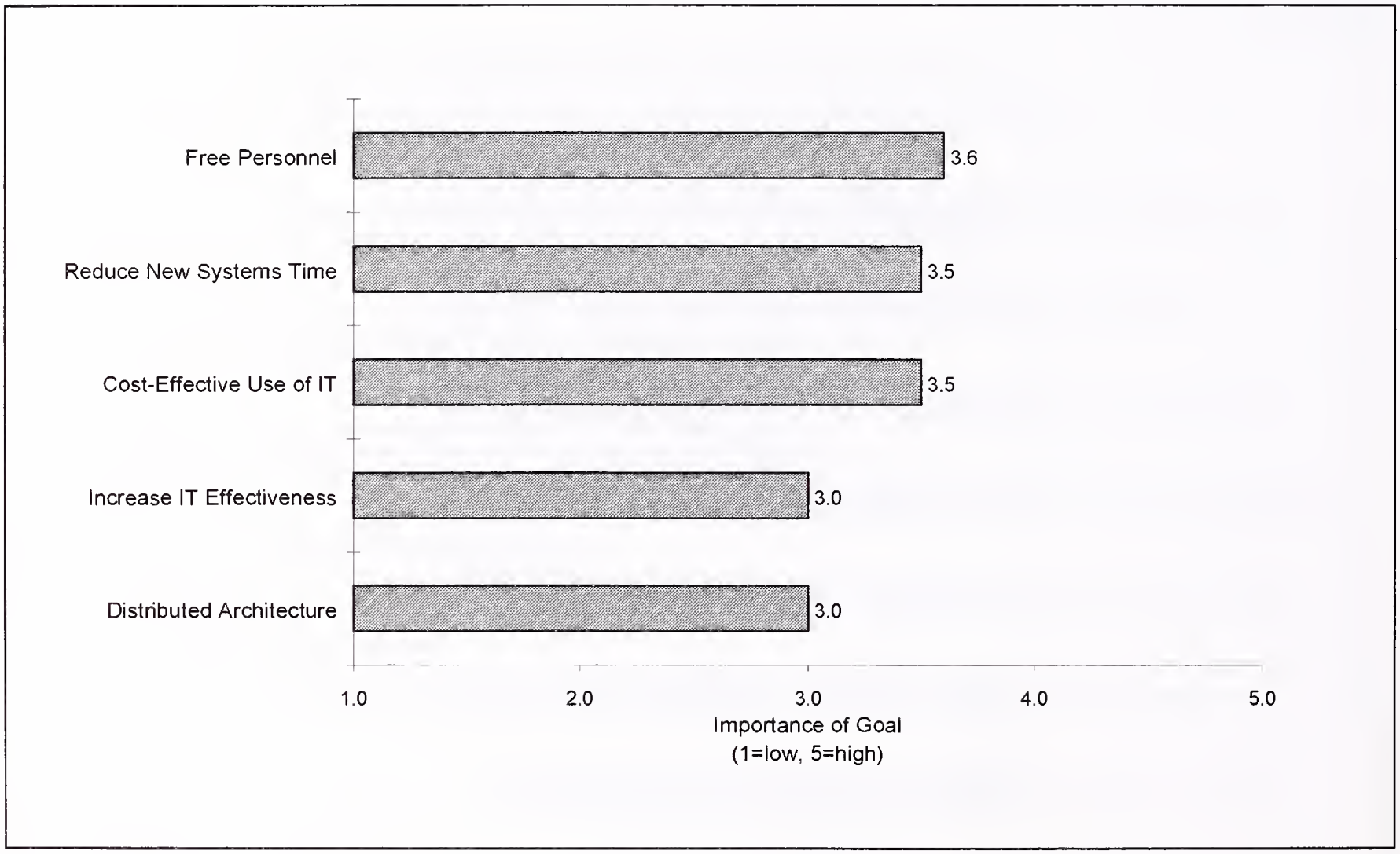
Source: INPUT

- North American users give a slight, but not statistically meaningful, edge to improved service levels, while European respondents give the edge to the freeing of personnel through outsourcing.
- Items that were less important (e.g., achieving a distributed architecture) were rated less satisfying.

The important lesson from this information is that vendors cannot be complacent. Although users are not expressing signs of discontent, neither are they indicating any particular reason for committing to a long-term relationship with the current vendor. This long-term commitment would be far more likely if the satisfaction ratings were in the range 4.0-5.0. A rating in the range of 4.5-5.0 should be the target for a vendor who is determined to keep a customer.

Exhibit III-5

Customer Satisfaction with Outsourcing Approach—Europe



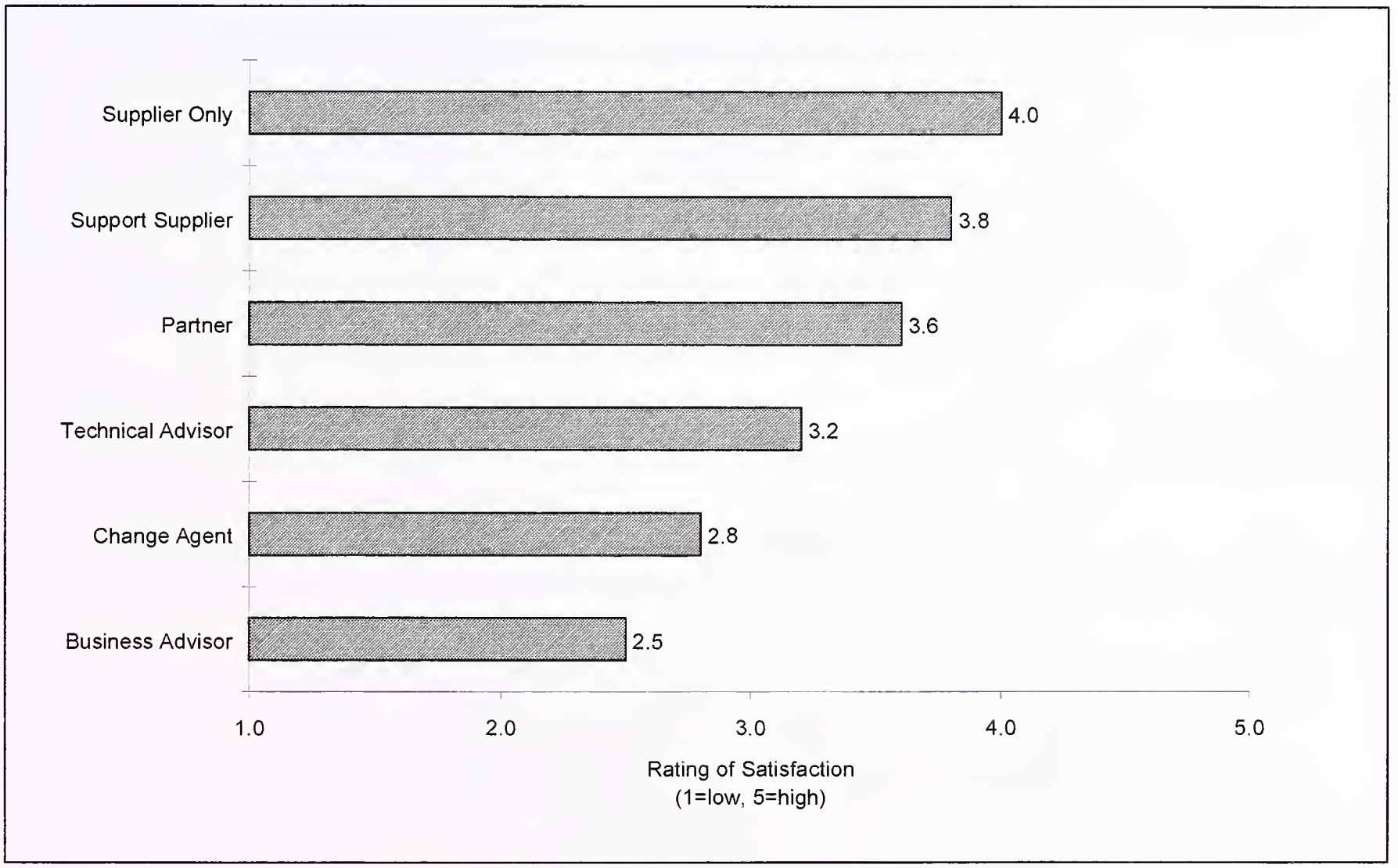
Source: INPUT

2. Vendor Roles

User satisfaction with vendor roles for the European respondents (this question was not asked in the North American survey) is presented in Exhibit III-6. Vendors rate an "excellent" for their supplier only role and a "good" for their technical advisor or support partner roles. Less satisfactory were the roles of change agent, support supplier, or business advisor. It appears that these users are basically pleased with their vendors' performance in those roles that users require.

Exhibit III-6

Satisfaction with Vendor Roles in Europe



Source: INPUT

3. Outsourcing Requirements and Performance

Exhibit III-7 summarizes top-rated user goals to be achieved by outsourcing, and results. In general, users appear to look for very specific results from outsourcing, namely advancement of IT performance to the next level in a cost-effective manner. Respondents report the most satisfaction with performance on items that "fix" inherent in-house problems, but less satisfaction on items that lead to the primary goal of cost effectiveness. The next section explores this requirements-performance gap in greater detail.

Exhibit III-7

Respondents' Top-Rated Goals and Results of Outsourcing

Service Requirements	Service Performance
Achieve Cost-Effective IT	Improved Service Levels
Improve IT over Existing Operations	"Fixes" to Operations
Hire Vendor Focused on Supply of Service and, Secondarily, Offering Technical Assistance	Vendor is Supplier and Advisor

Source: INPUT

C
Gap Analysis

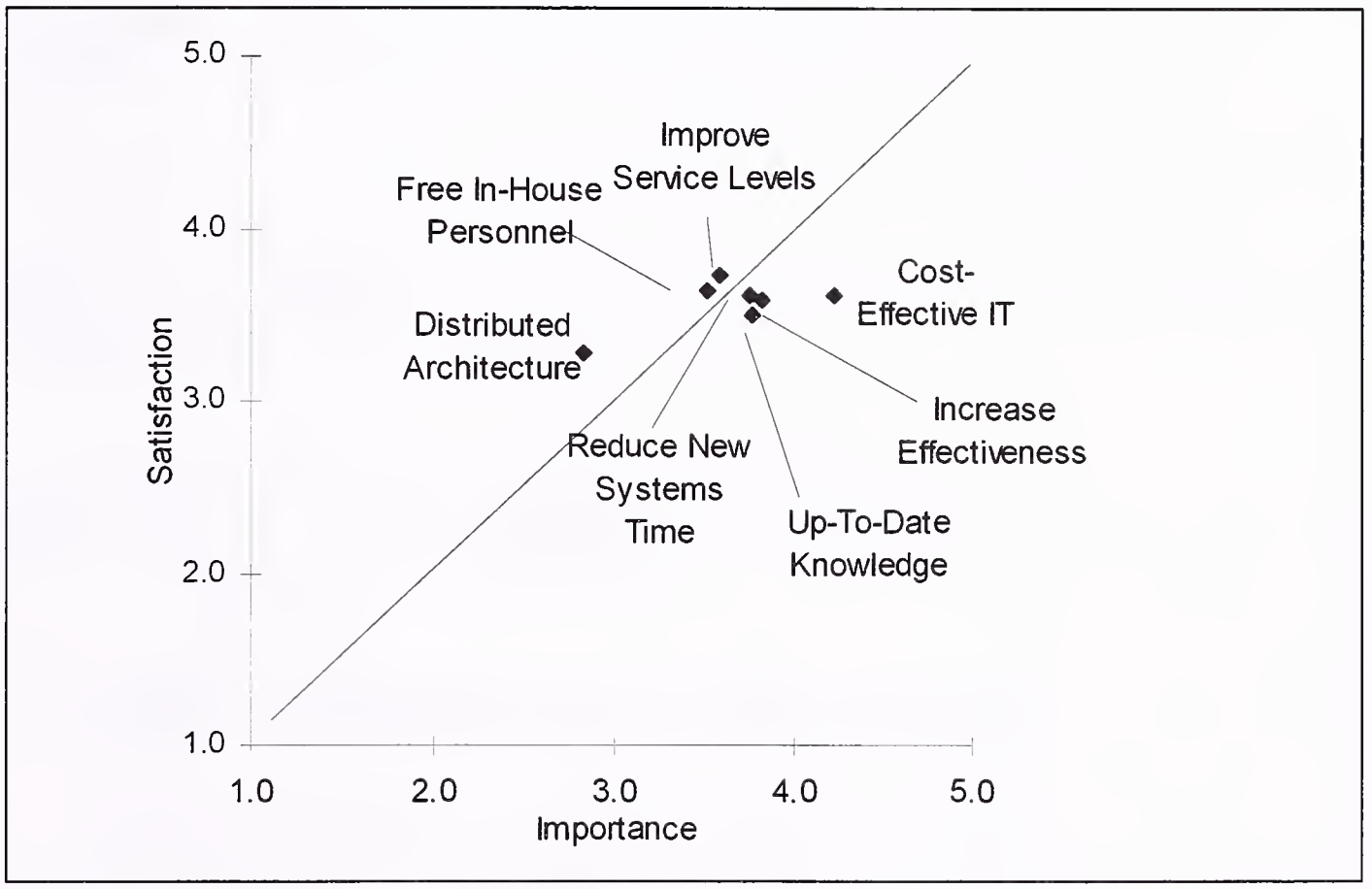
Users' reports of discrepancies between the level of importance of each criterion and the level of satisfaction received through outsourcing are presented in Exhibits III-8 and III-9, respectively, for North American and European respondents.

The diagonal line through the chart represents the points of congruence between users' report of level of importance and users' report of level of satisfaction with performance. Items on that line indicate perfect agreement. Items below the line indicate criteria for which users are not receiving the performance they desire while items above the line indicate items in which the performance exceeds what is required by users.

Vendors should consider the need to improve on criteria below the diagonal. However, a variety of approaches may be applicable for items that are above the line. In some cases, vendors may choose to continue without change as the rating may be interpreted as overdelivery on the part of the vendor and may be something the vendor is willing to do. In some circumstances, the vendor may view the high rating for satisfaction compared with importance as something that wants a premium price charged. Yet another option is to curtail delivery for that criterion so that satisfaction equates to importance or expectation on the part of the user.

Exhibit III-8 indicates a slight overperformance on "fixes" (i.e., freeing personnel and improving service levels) and a slight underperformance on "improvements" (i.e., reduce time, add knowledge, increase effectiveness). Given the closeness to the diagonal line, the discrepancies in either direction are not substantial.

Exhibit III-8



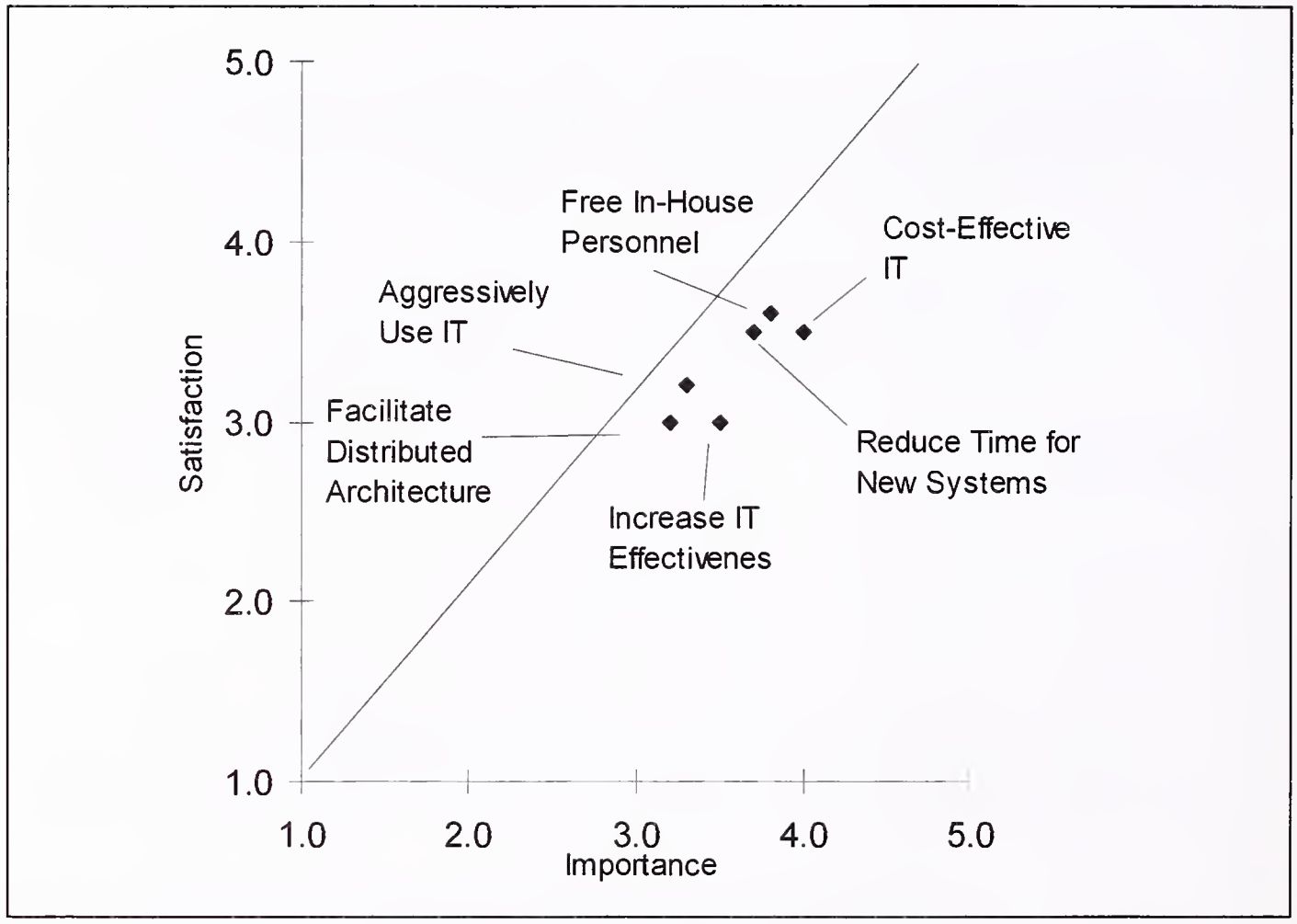
Source: INPUT

However, distributed architecture and cost-effective IT are some distance from the required-received congruence line and deserve attention. For the former, the indication is that outsourcing aids the development of a distributed approach that is not a key goal of users. There is no negative attached to this result of outsourcing. The failure of outsourcing to achieve the desired level of cost effectiveness in IT is an important issue. The one goal that users most desire in deciding to outsource is the one goal that they report they cannot achieve.

Exhibit III-9, the European data, shows an even worse situation, in which users report no instances of outsourcing performance exceeding the importance of the outsourcing goal. The effectiveness of outsourcing criterion has the largest discrepancy (most dissatisfaction), again suggesting that these users, as well, feel they are missing the key goal of their outsourcing strategy.

Exhibit III-9

Outsourcing Importance versus Satisfaction—Europe



Source: INPUT

In both sets of data, the discrepancies are large enough to cause users to question the basic tenet of outsourcing as cost effective, but not large enough for users to reject the concept of outsourcing completely. The warning is clear, however, that users have not met their most important goal for outsourcing. Whether their expectations exceed reality or not, vendors must be sensitive to the potential for increased pressure to meet cost effectiveness expectations of users or face canceled contracts.

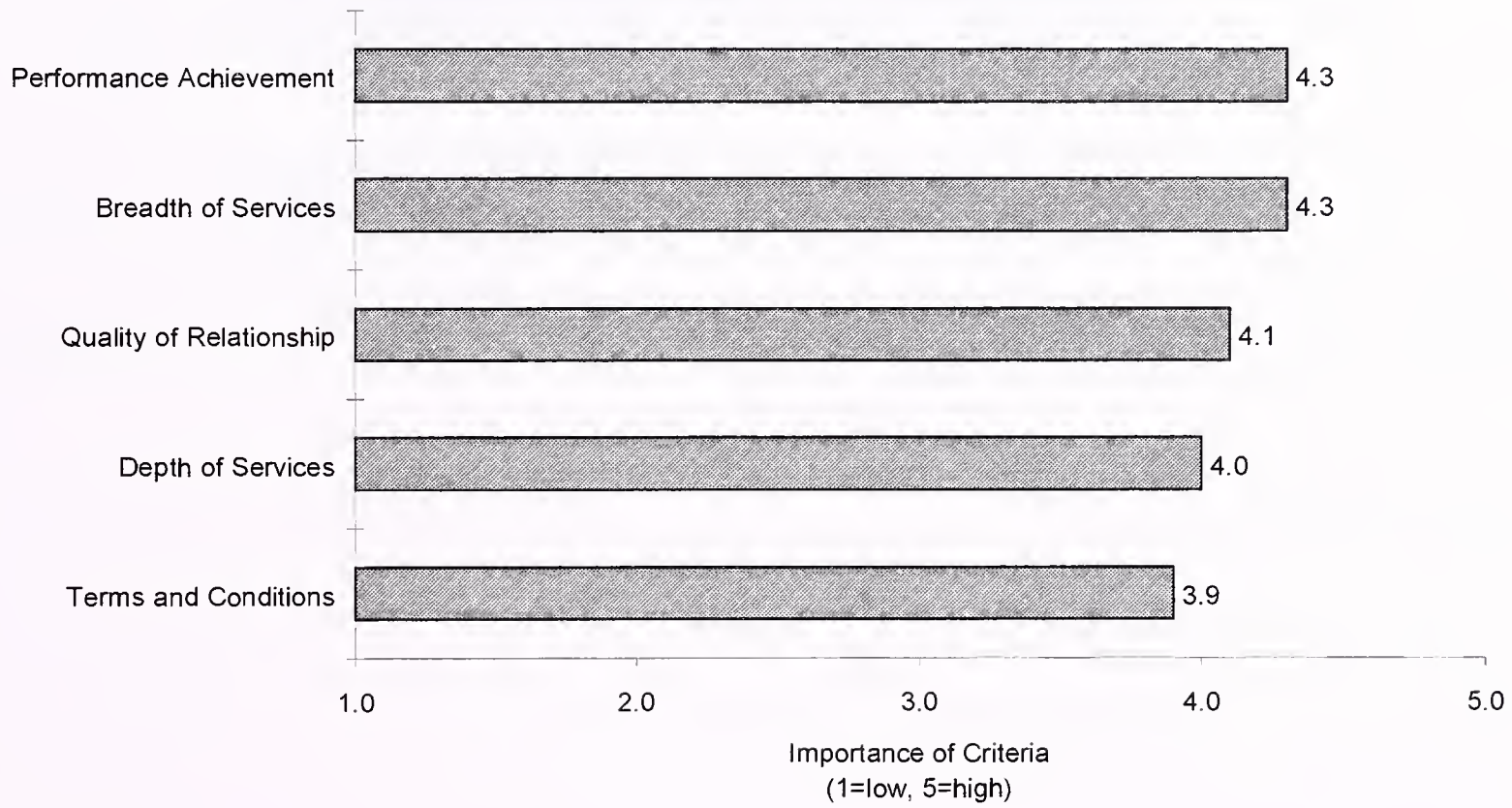
D
Vendor Requirements

To determine how users hoped to achieve their outsourcing goals by the careful selection of an outsourcing vendor, they were asked to rate importance and performance on twenty-seven vendor selection criteria. These criteria represent five broad categories of concerns.

Composite ratings of the categories are presented in Exhibit III-10. All categories are highly rated in importance, with breadth of services and the user's perception of the vendor's performance given the edge. Contract issues were rated, on average, as least important, although the difference between the highest and lowest category was small. Overall, these "details" are secondary to what the vendor can do, how well it does it, and the quality of the vendor-customer relationship. The importance of the criteria within each broad selection category is explored below.

Exhibit III-10

Outsourcing Vendor Selection Criteria Categories



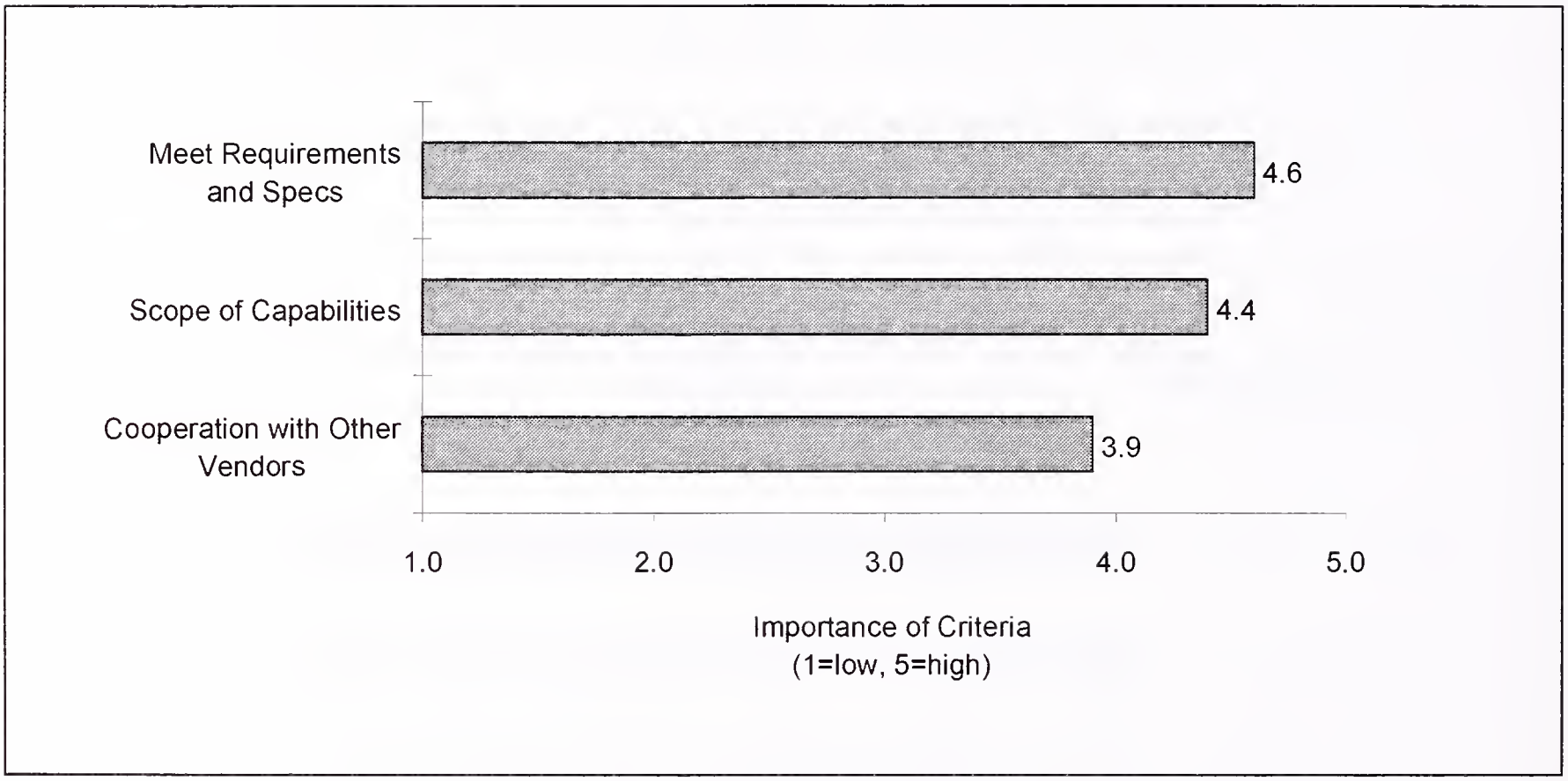
Source: INPUT

1. Breadth of Services Offered

The key question is, "Can the vendor do the job?" Users also worry if the vendor's capabilities are as broad as the job and, to a lesser extent, if the vendor can work with other vendors in multiple-vendor sites. The latter criterion is likely rated less important than the others for it may not apply to all outsourcing situations, especially in single-vendor sites or where the outsourced function is of limited scope.

Exhibit III-11

Importance of Breadth of Service Criteria

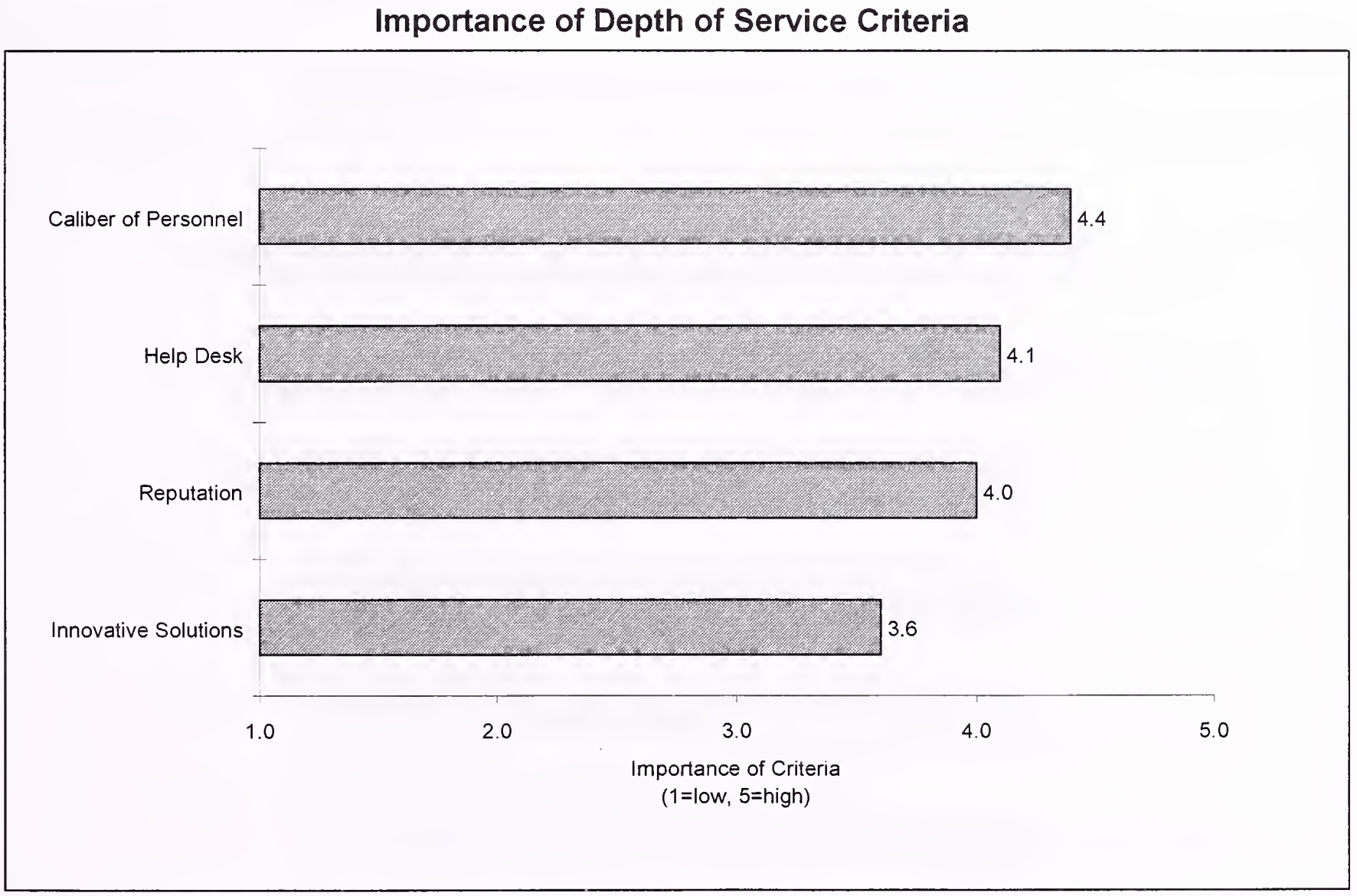


Source: INPUT

2. Depth of Services Offered

The depth of services offered by the vendor include, in order of importance, the caliber of the personnel, the existence and quality of their help desk offering, the vendor's reputation, and their ability to provide innovative solutions. Good people are a key to success, according to users, far more important than being innovative. In fact, given that users are looking for suppliers and not advisors, innovative solutions may be a detriment.

Exhibit III-12



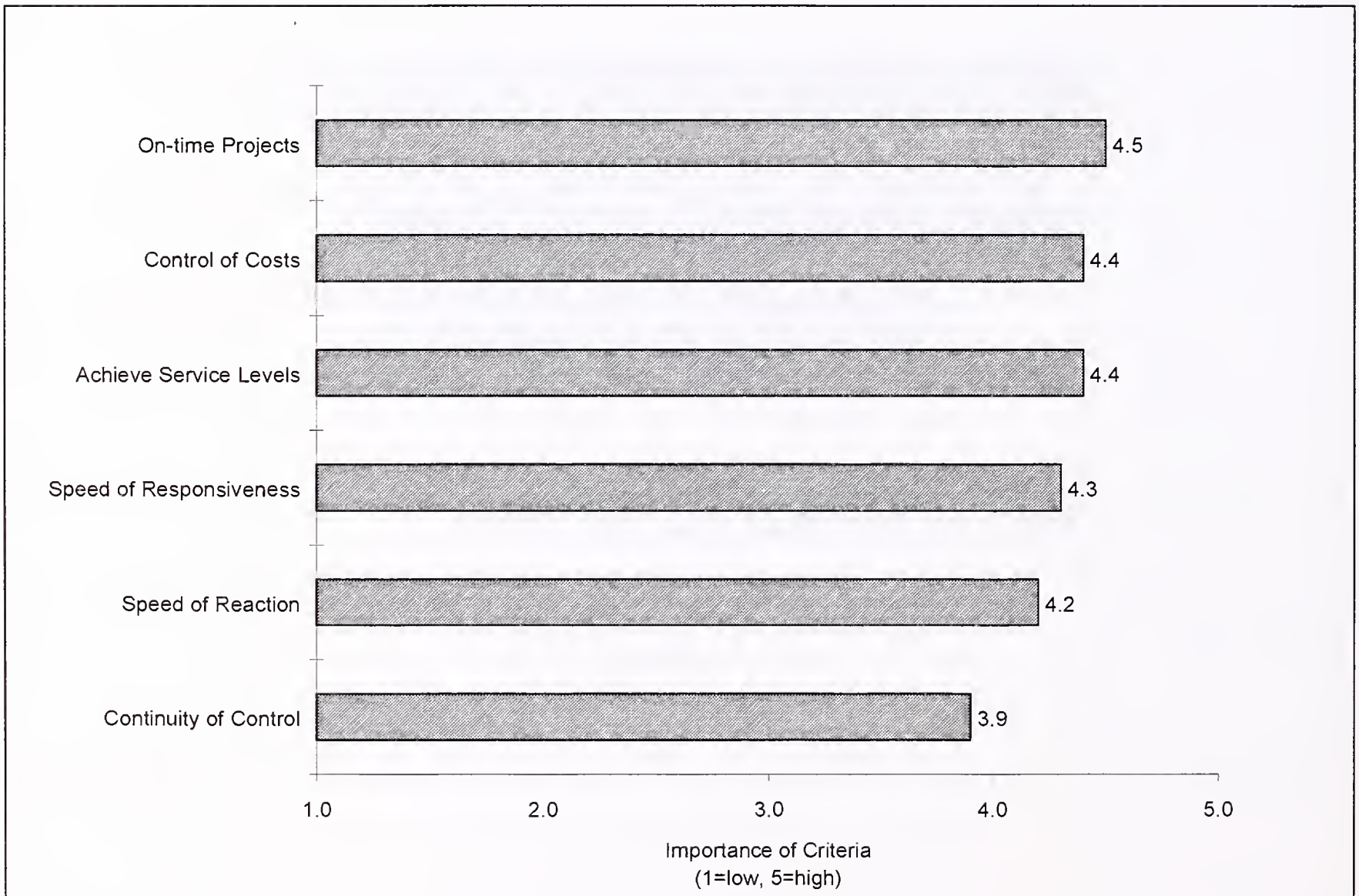
Source: INPUT

3. Performance Achievement

The key criterion is performance (see Exhibit III-13). Users want vendors to deliver what is planned (i.e., on time, within budget, and at or below cost). Secondarily, they want vendors who can adapt to changes in the outsourcing requirements (i.e., responsiveness, speed of reaction). Lastly, users require vendors to have some control over continuity of personnel, whether those personnel are company employees being "acquired" by the vendor or whether they are the vendor's employees. Frequent and unexpected personnel changes in this service arena are not looked on with favor by users.

Exhibit III-13

Importance of Performance Achievement Criteria



Note: Number of respondents = 54

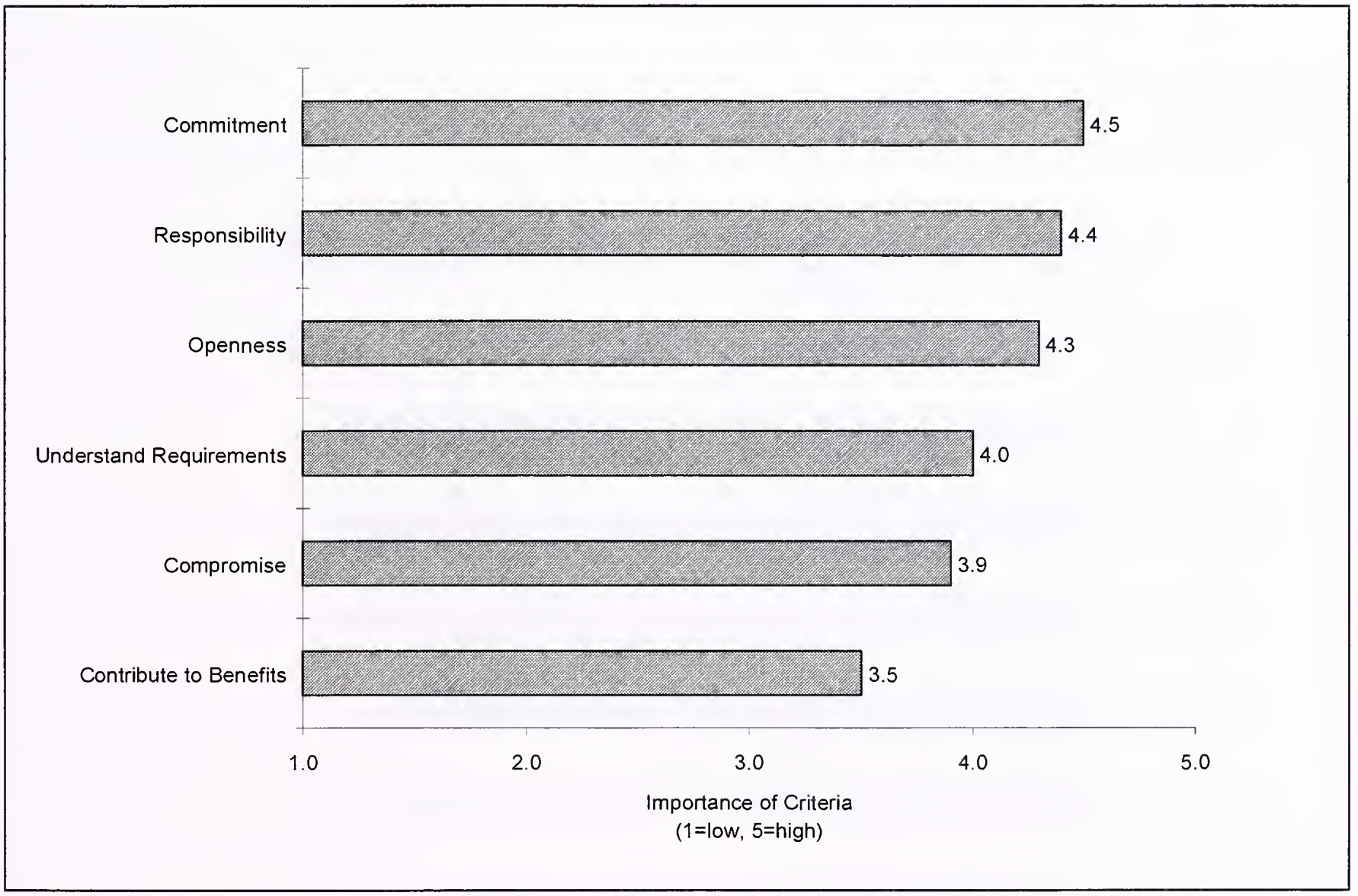
Source: INPUT

4. Quality of Relationship

Users stress vendor ownership (i.e., commitment and taking responsibility) as key components they value in the vendor-customer relationship (see Exhibit III-14). Being a part of the team through open communications is also important, as is a vendor focus on contributing to the company's success (i.e., understanding requirements, compromising). Actual contribution to the business was rated as less important, perhaps reflecting the underlying perception that users look to vendors to be suppliers and not necessarily partners.

Exhibit III-14

Importance of Quality of Relationship Criteria



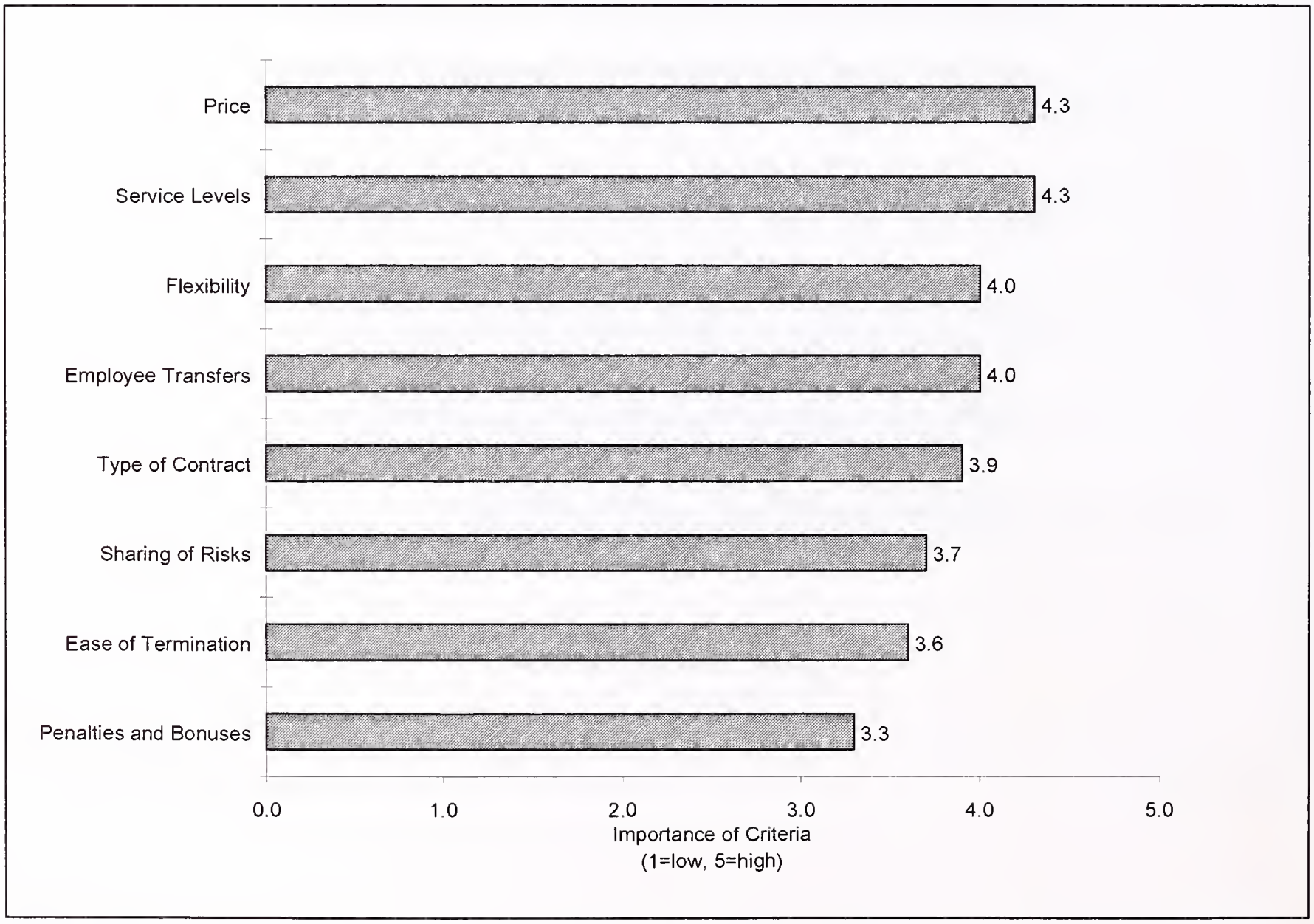
Source: INPUT

5. Contract Terms and Conditions

The details of terms and conditions are reported as less important to users, on average, although some specific vendor criteria are as important as those cited above (see Exhibit III-15). Specifically, price and service levels are key. These are followed by a set of criteria that reflect how easy the vendor is to deal with (i.e., flexibility, employee transfers, and type of contract). Sharing risks and contract language that eases termination are less important; the former is another indication that users want vendors to be suppliers and not partners. Ease of termination and bonuses and penalties are less important selection criteria, perhaps because neither of these are frequent concerns in the terms and conditions of contracts. Termination clauses are most likely standard and pricing is mostly straightforward fixed price or cost plus without incentives or penalties.

Exhibit III-15

Importance of Terms and Conditions Criteria



Note: Number of respondents = 48

Source: INPUT

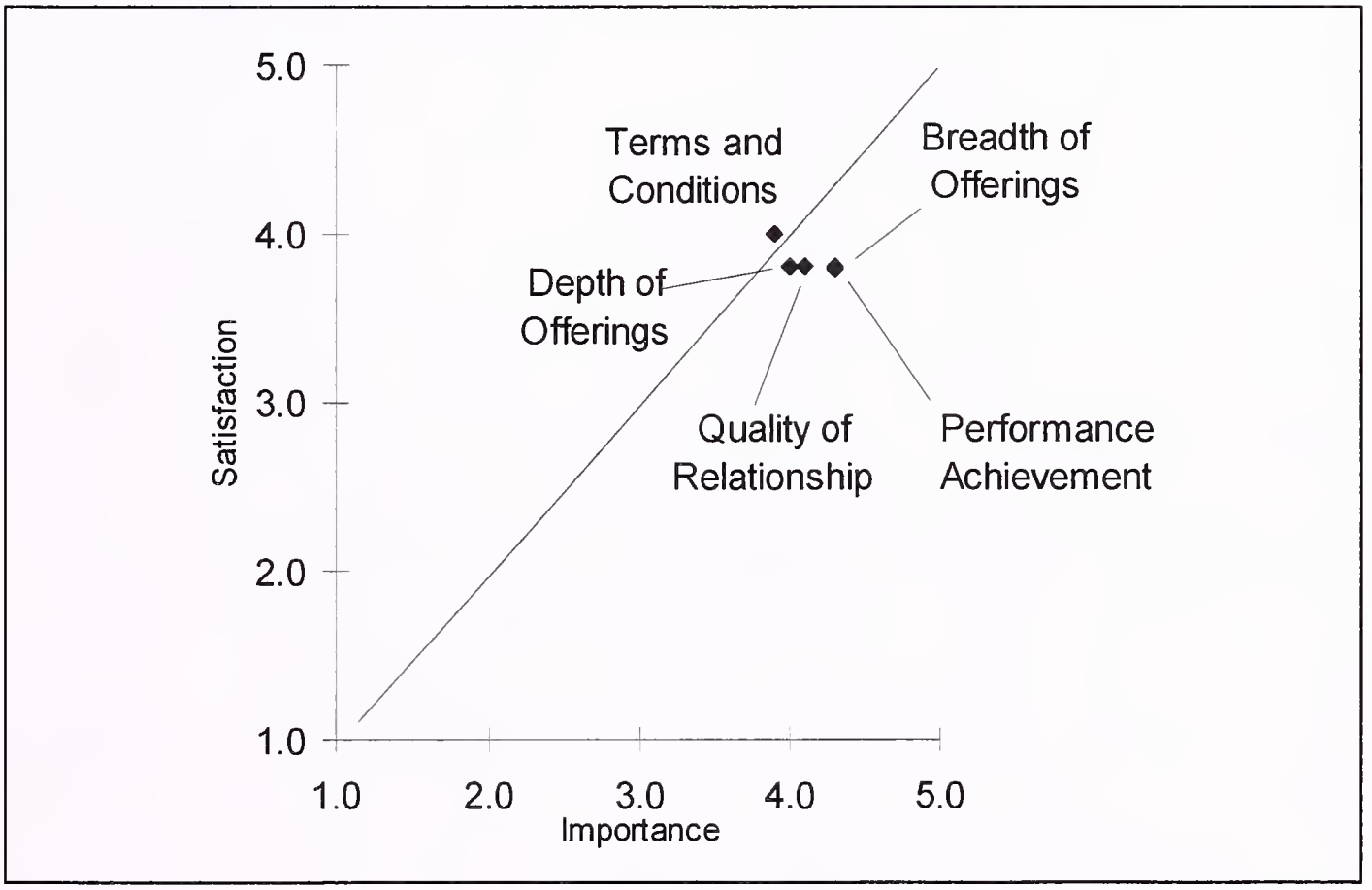
E
Vendor Requirements-Performance Gap

On an aggregate basis for the vendor selection categories discussed in the previous section, users report (see Exhibit III-16) that their satisfaction with vendors is not up to the level of importance users attach to each category. Large discrepancies are noted for breadth of offerings and performance achievement, the two most important vendor selection categories to users. Vendors also underperform in the quality of relationship maintained with the customer and the depth of their service offerings versus expectations. Only terms and conditions criteria exceed user importance ratings.

The following sections examine the criteria in each of these categories.

Exhibit III-16

Importance versus Satisfaction with Vendor Selection Categories



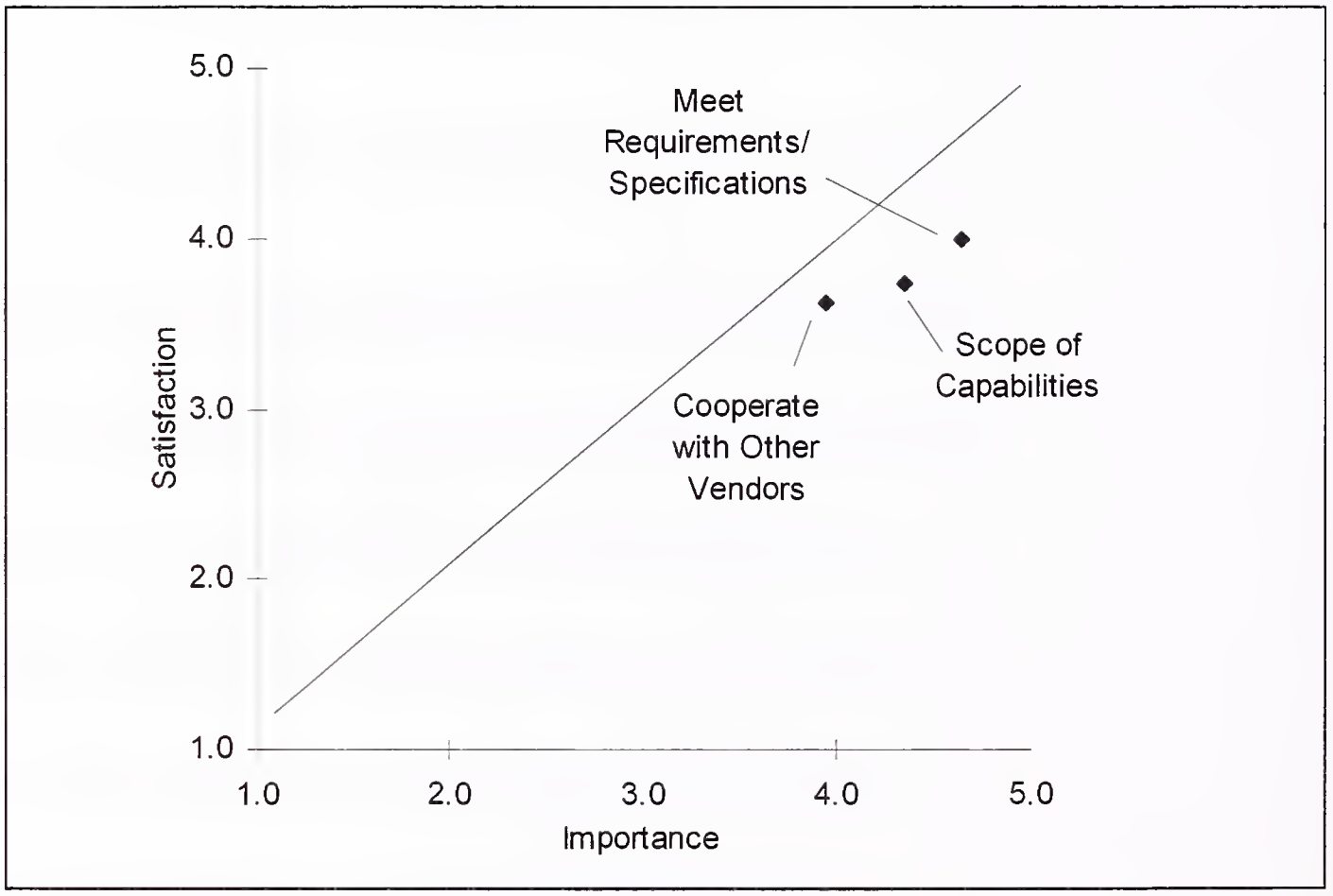
Source: INPUT

1. Breadth of Service Offerings

Vendors are rated by users as underperforming compared to the importance of each of the criteria in this category (see Exhibit III-17). While vendors are graded in the "acceptable" category, users are looking for "excellent" performance on handling the outsourcing assignment as specified. According to users, vendors underperform most on the scope of their capabilities and somewhat less on their ability to meet requirements and specifications. Ratings of vendor cooperation with other vendors are close to congruence with importance.

Exhibit III-17

Importance versus Satisfaction with Breadth of Services

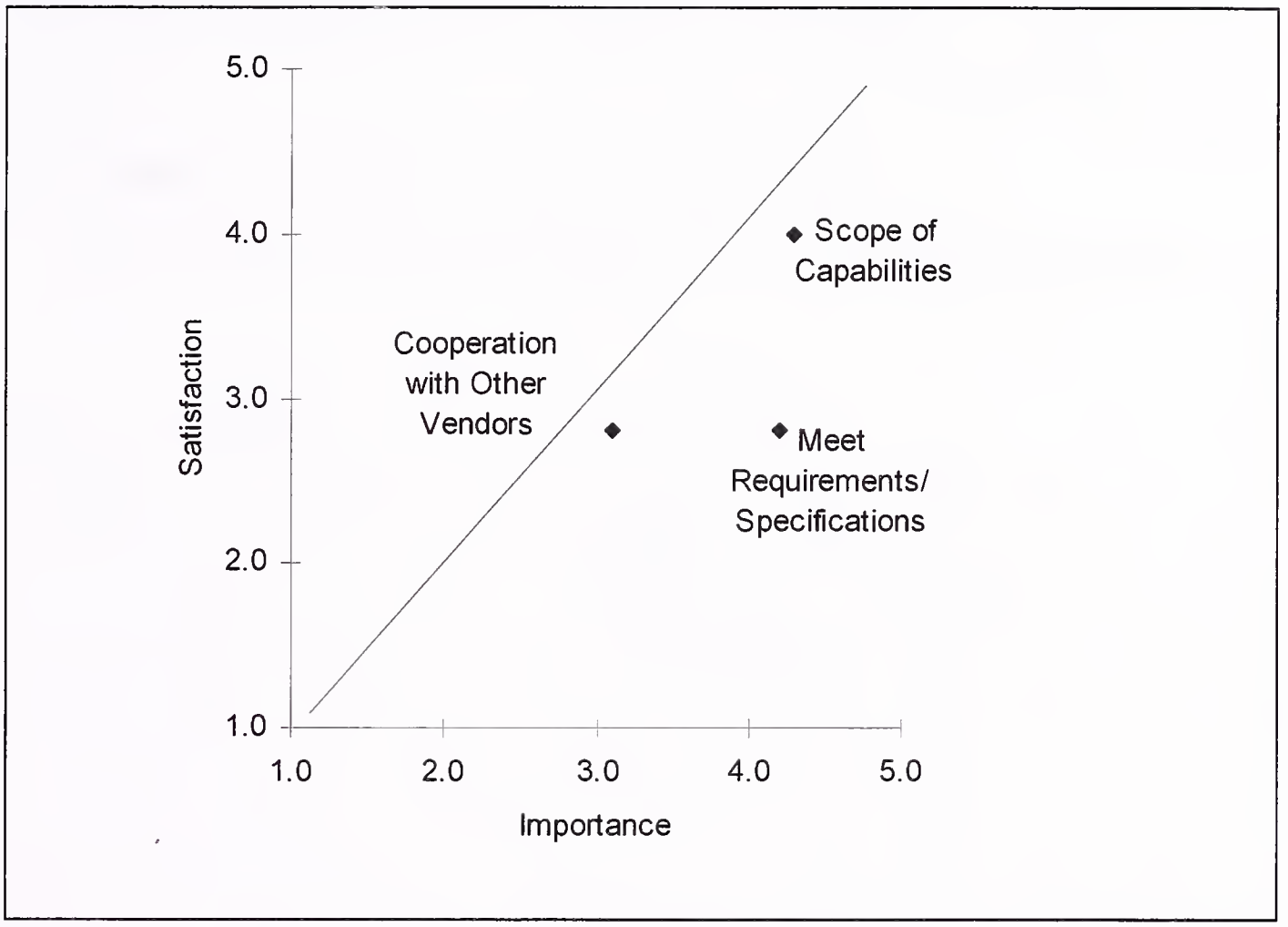


Source: INPUT

Users in the European market (see Exhibit III-18) indicate similar levels of underperformance on all three criteria. A very large discrepancy is reported by these users on vendors' abilities to meet requirements and specifications. Vendors have their work cut out in closing this sizable gap.

Exhibit III-18

Importance versus Satisfaction with Breadth of Services—Europe



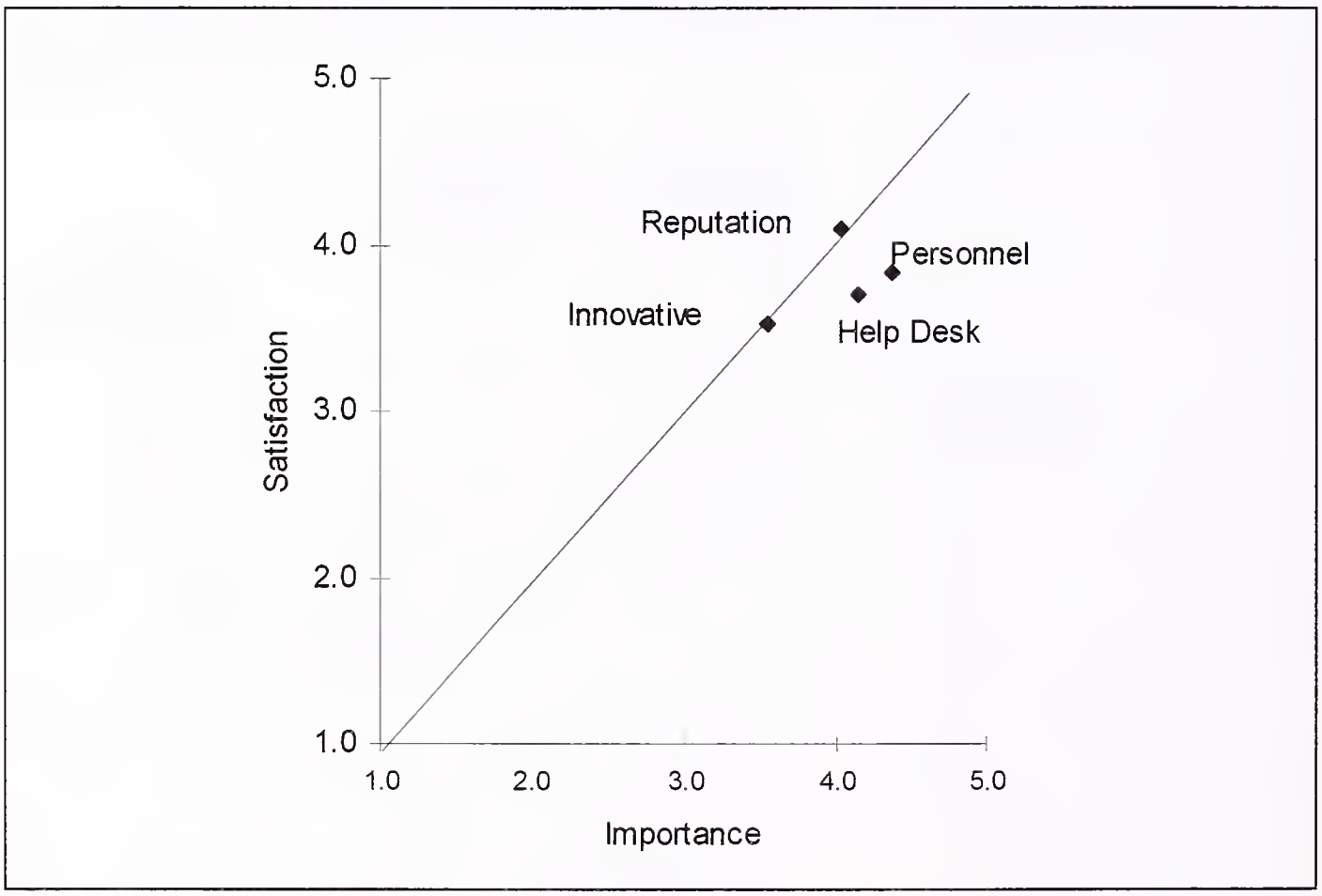
Source: INPUT

2. Depth of Services Offered

The strength of vendors shows more congruence with users' ratings of importance (see Exhibit III-19). The caliber of personnel and, to a lesser extent, help desk functions are found to be less than desired, but the gaps are not large, even though the ratings of importance are relatively high. Apparently, selected outsourcing vendors are delivering most of the depth required. No important differences are noted in the comparable European data.

Exhibit III-19

Importance versus Satisfaction with Depth of Services Offered



Source: INPUT

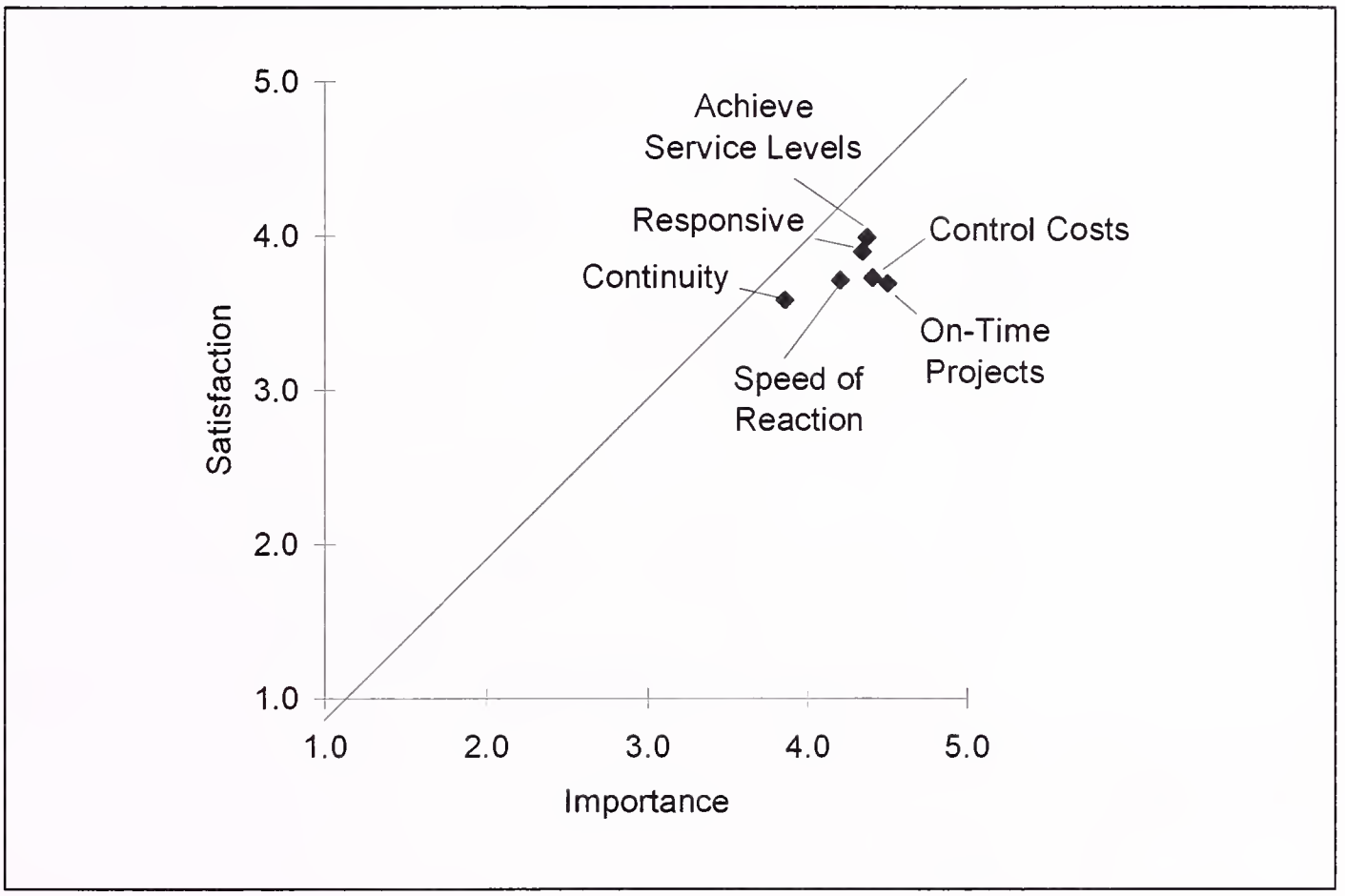
3. Performance Achievement

The critical performance measures—on time, within budget, and at the agreed-upon service level—are not being met by vendors. Speed of reaction, responsiveness, and continuity of personnel could be improved, as well.

While user expectations are high for these basic components of performance, vendors need to move to close these gaps. As noted above, performance achievement is critical to vendor selection and re-selection. Underperformers are likely to be closely monitored and replaced if this performance gap widens.

Exhibit III-20

Importance versus Satisfaction with Performance Achievement

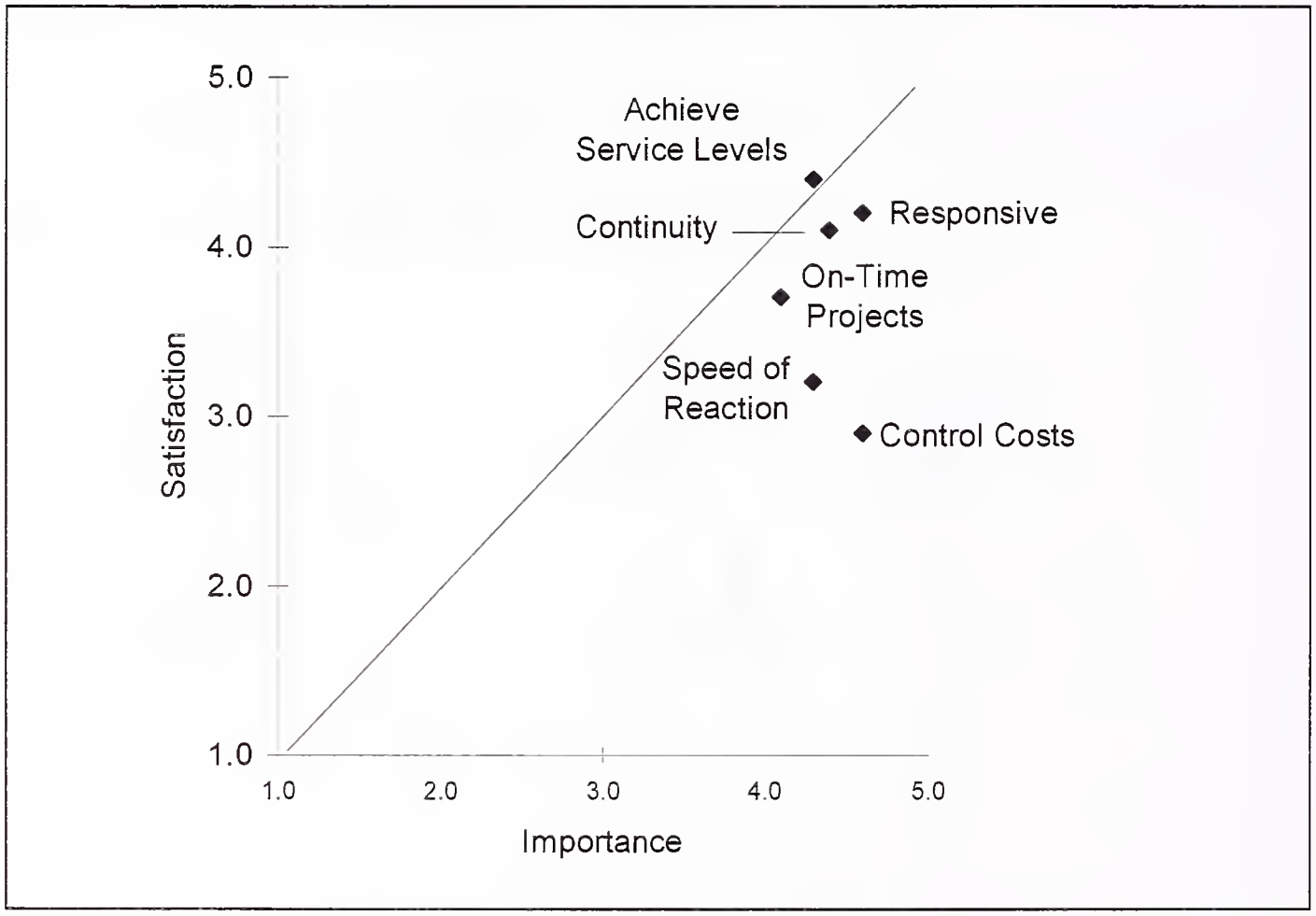


Source: INPUT

The urgency may be greater in Europe, where the gaps (see Exhibit III-21) are wider already. Costs and speed of reaction appear to be in the danger area. Service level achievement, which is above the user requirement level, may be offsetting some of the dissatisfaction being felt at these discrepancies.

Exhibit III-21

Importance versus Satisfaction with Performance Achievement—Europe



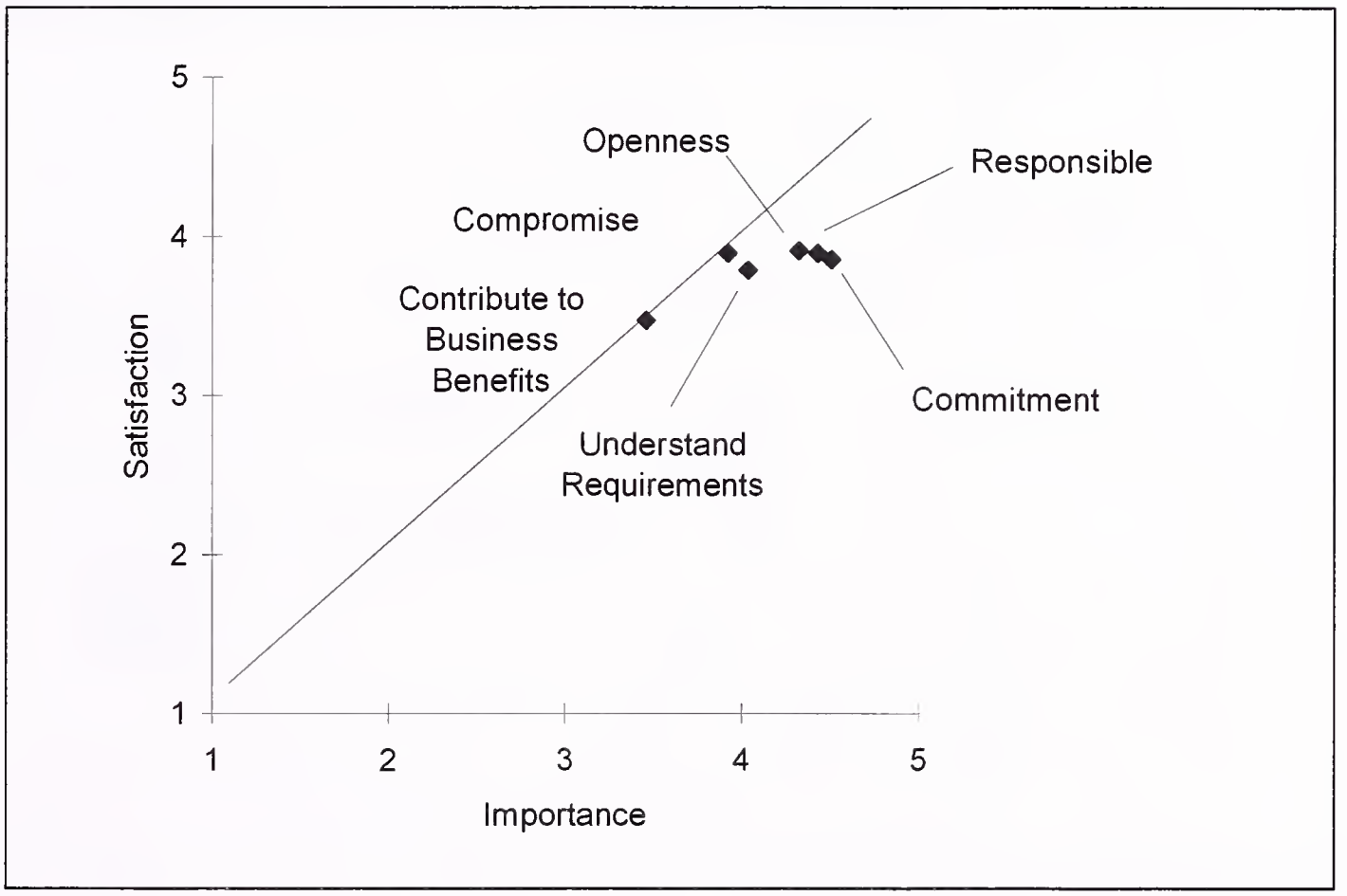
Source: INPUT

4. Quality of Relationship

The quality of relationship category (see Exhibit III-22) finds users' ratings of importance versus satisfaction generally congruent with vendors' understanding of requirements, contribution to the company's business, and willingness to compromise. Less congruent is the rating of vendor openness. Vendor responsiveness and commitment show unacceptable gaps with expected performance levels.

Exhibit III-22

Importance versus Satisfaction with Quality of Relationship

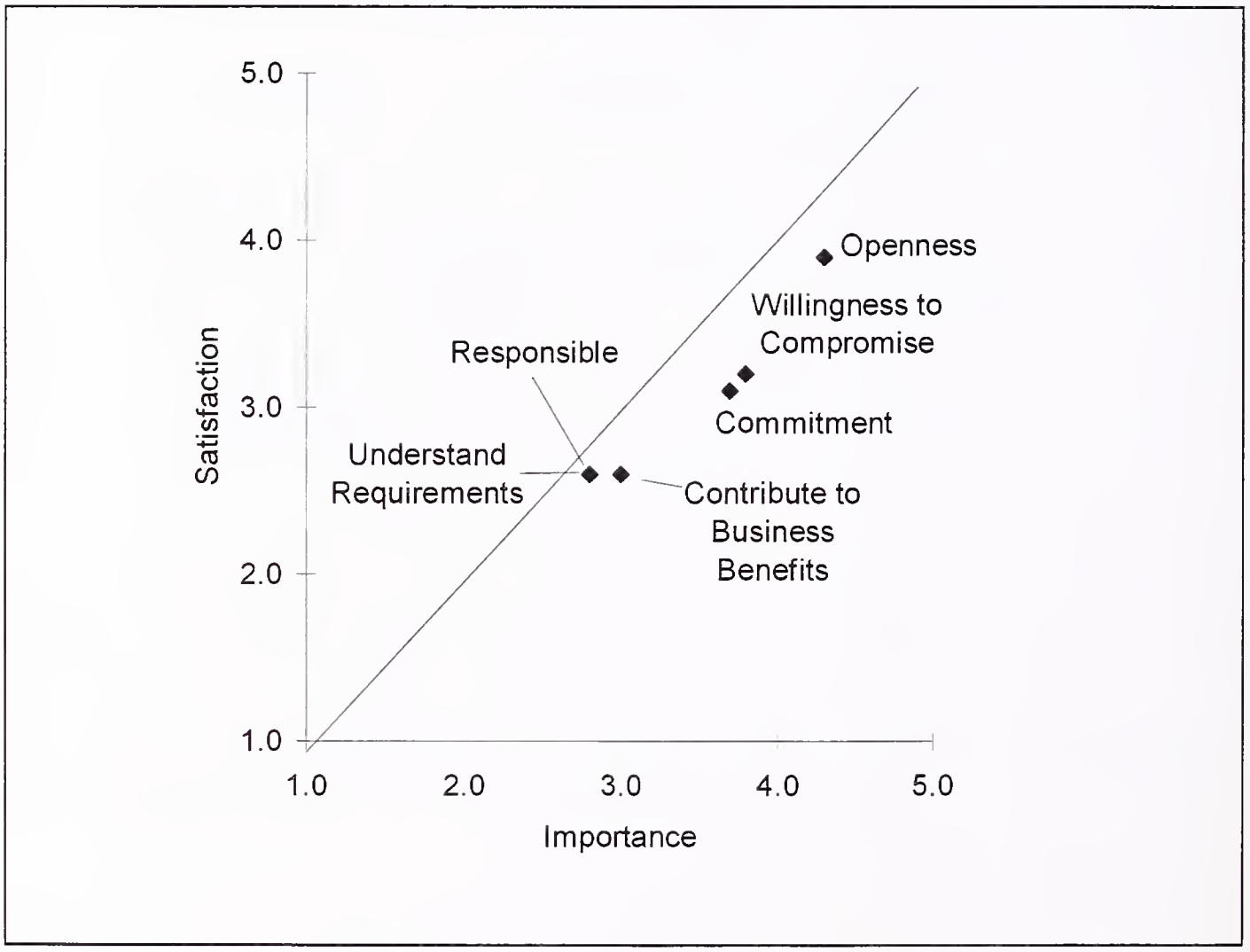


Source: INPUT

In Europe, both the importance and the satisfaction levels are less than among North American users. Gaps are noticeable (see Exhibit III-23) in openness, vendors' willingness to compromise, vendor commitment, and vendors' contribution to the business. It is likely that only those with gaps that are highly rated in importance, namely openness and willingness to compromise, are potential problems. Gaps in importance-satisfaction for criteria that are lower in importance may not receive the concern that very important criteria get.

Exhibit III-23

Importance versus Satisfaction with Quality of Relationship—Europe



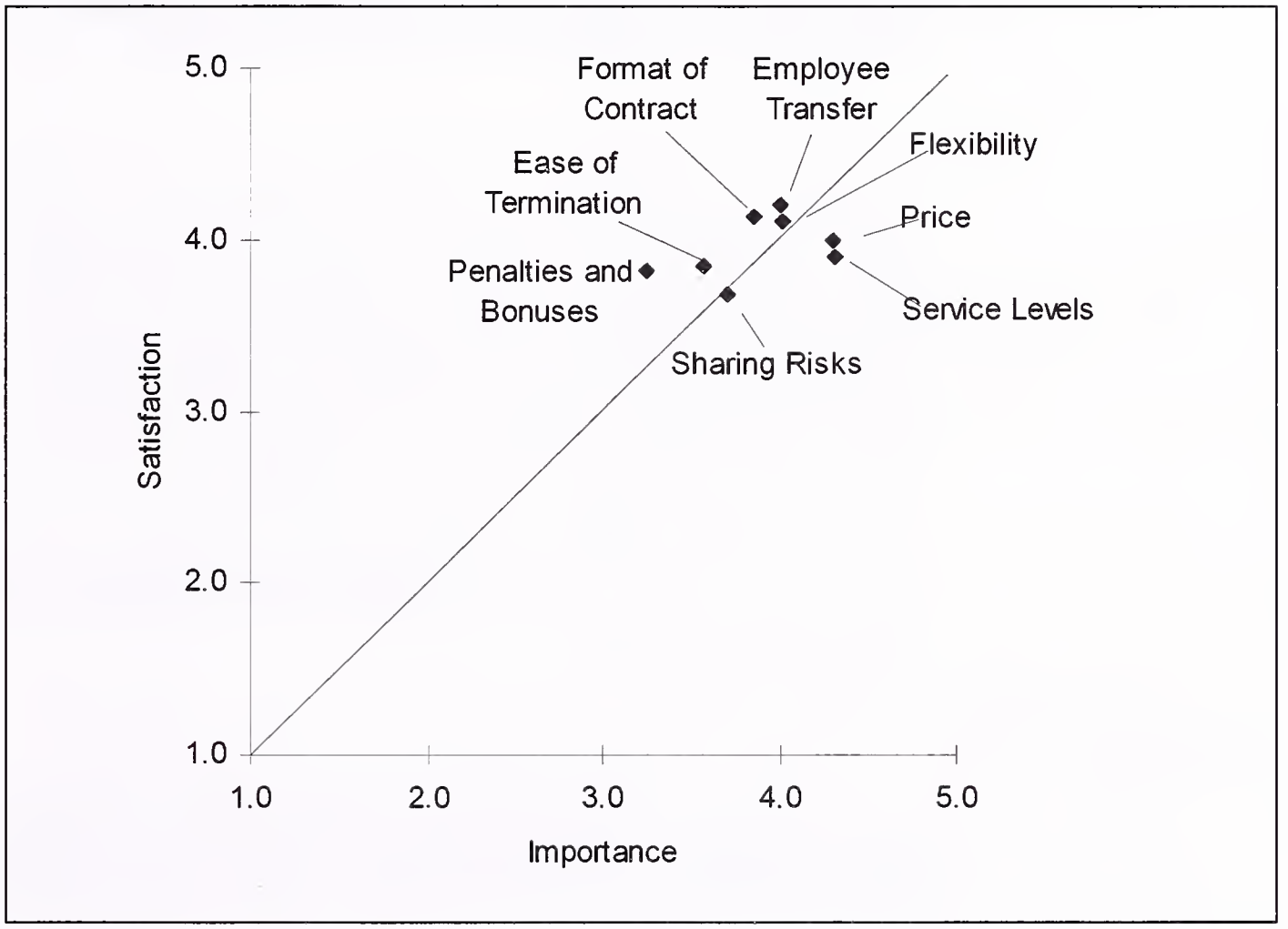
Source: INPUT

5. Contract Terms and Conditions

Contract terms and conditions, the one area that is potentially openly contentious, shows the greatest amount of satisfaction. Most of the criteria in this category (see Exhibit III-24) are within limits; only price and service levels seem to fall into the potential problem area.

Exhibit III-24

Importance versus Satisfaction on Terms and Conditions



Source: INPUT

F
Anticipated Actions

The ultimate result of user-perceived discrepancies between what is required and what is received is for the user to terminate the outsourcing contract. When respondents were asked their likely action vis-à-vis their level of satisfaction, most indicated that contracts with the current vendor(s) would be renewed—a clear indication that reported discrepancies were irritants, but not deal breakers. But, as indicated in Exhibit III-25, 12% of the respondents reported that vendor changes were possible. Two-thirds of this group (8% overall) had already decided to change and the others indicated they would give the issue serious consideration as a matter of business prudence.

Exhibit III-25

Likelihood of Changing Vendors

Action	Frequency of Mention (%)
Continue with Current Vendor	82
Yes, Will Definitely Switch Vendors	8
Too Early to Tell	6
Will Consider Changing Vendors When Contract Ends	4

Source: INPUT

Although vendors may be locked in, users report that changes will be made as contracts are renegotiated. Exhibit III-26 indicates the types of changes that users anticipate. Twenty-four percent of the respondents imagine the contracts expanding to include additional services or even entire functional areas. But 14% report that the changes will be detrimental to the vendors involved. Current services will be more closely specified in such areas as help desk expectations, service level requirements, and quality expectations. Vendor roles could be reduced, according to 4% of the respondents, due to company downsizings and the elimination of legacy systems that were the reason for the need for outsourcing in the first place. Finally, in 2% of the cases, prices will be the target of negotiations as users seek to reduce the expense of outsourcing.

Exhibit III-26

Changes to Arrangements Anticipated

Action	Frequency of Mention (%)
None	62
Additional Services To Be Included	24
Current Services To Be Better Specified	8
Reduce Outsourcing Vendor's Role	4
Renegotiate Price	2

Source: INPUT

IV

Satisfaction with Outsourcing Analyzed by Type of Service

This chapter presents an analysis of outsourcing users' responses to INPUT's customer satisfaction survey with the data segmented by the outsourcing service. Similar to Chapter III, this chapter looks for gaps between anticipated versus actual benefits of outsourcing and required versus actual vendor performance.

A Performance in Systems Operations

Some twenty-nine of the fifty-four total respondents indicated that their respective companies outsourced day-to-day operation of mainframe and/or standalone mid-range computer equipment. These respondents represent some 27% of the total outsourcing services mentioned by the respondents (many respondents mentioned more than one outsourced function). Most industries were represented in this segment and the average company size was $2.2 billion in revenue.

1. Satisfaction with Outsourcing in Meeting Goals

Exhibit IV-1 presents the gap analysis between respondents' outsourcing goals and how well they perceive these goals to have been met. (Similar to charts in Chapter III, data points above the diagonal line of congruence between importance and satisfaction represent satisfaction beyond what was required, while points below the line represent shortcomings in meeting goals.) Service levels improved through outsourcing beyond the rated goal of users. Similarly, in-house personnel were freed for other tasks and a distributed architecture was advanced, even though these were not the main goals of users.

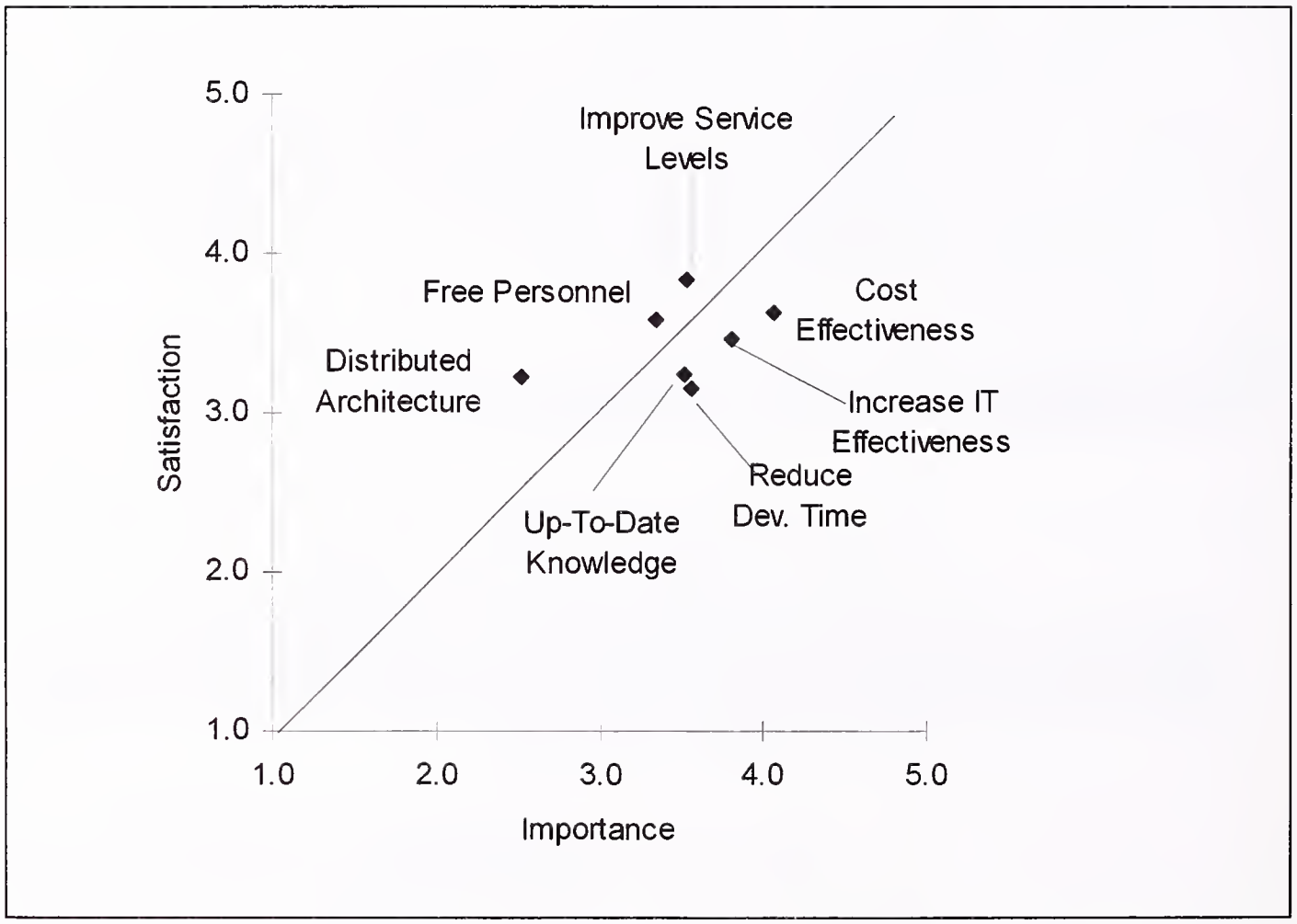
Less satisfying to users was the inability of an outsourcing approach to improve overall IT effectiveness, reduce development time, or capture the up-

to-date knowledge required of IT organizations. Worse, cost effectiveness goals were not attained. With no satisfaction rating above a 3.5 out of 5.0 (the highest rating) it is fair to summarize these results with a grade of "B" for outsourcing.

Although it is unlikely that users will simply cancel contracts, especially when overall results are above average, vendors should note these discrepancies and work to narrow gaps, either by fostering more positive perceptions of the outsourcing approach to systems operations or by helping users to lower what may be unrealistic expectations.

Exhibit IV-1

Users' Satisfaction with Systems Operations Outsourcing



Source: INPUT

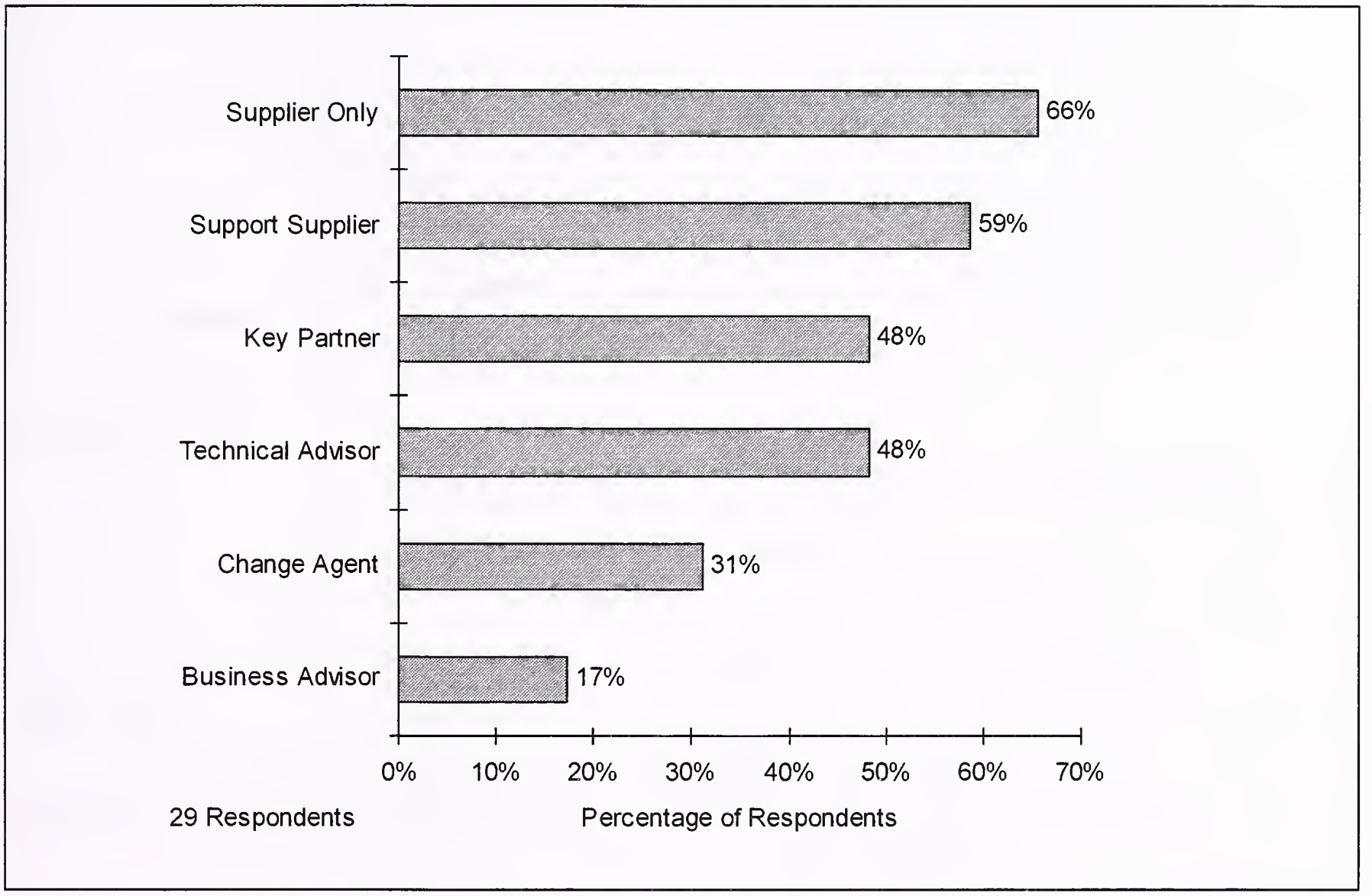
2. Vendor Roles Expected by Outsourcing Users

Part of the perceived discrepancies between goals users have for outsourcing systems operations and their level of satisfaction with attaining these goals may be differences of opinion between users and vendors regarding the roles to be fulfilled by vendors. As indicated in Exhibit IV-2, for this segment of users, very focused suppliers of agreed-upon services were most frequently expected by users. Second, their expectations extended to narrowly focused roles as advisors or partners in IT and, thirdly, broader roles in the business

of the company. Users seem to believe that effectiveness of outsourcing would be increased if vendors would stick to these expected roles.

Exhibit IV-2

Roles Expected of Systems Operations Outsourcing Vendors



Note: Number of respondents = 29

Source: INPUT

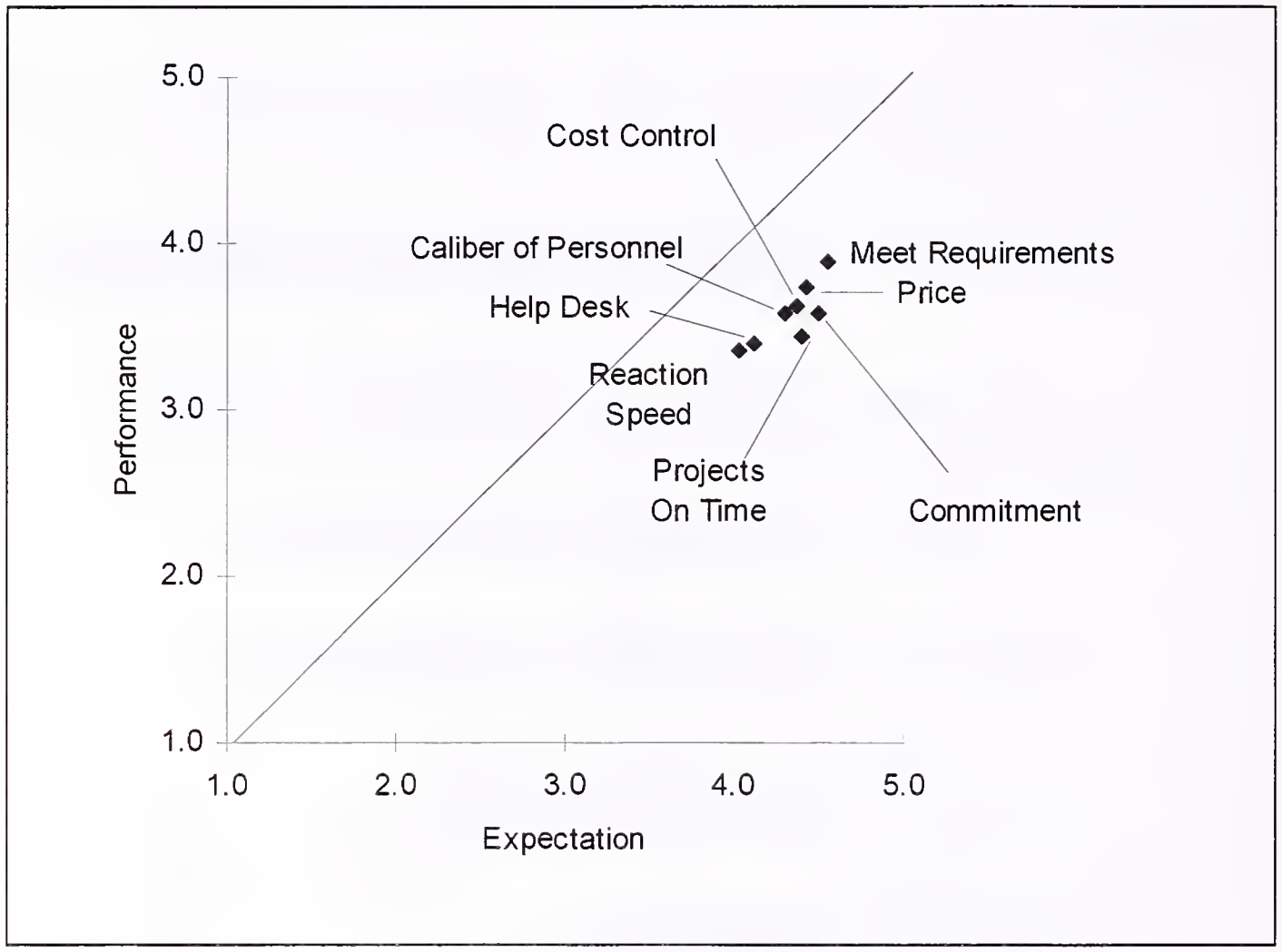
3. Users' Satisfaction with Outsourcing Vendors

In terms of actual vendor performance for these systems operations outsourcers (see Exhibit IV-3), a number of large discrepancies were noted between users' ratings of vendor selection criteria and actual vendor performance. (For this analysis in this chapter only the largest discrepancies, positive or negative, were included in the graphic. INPUT selected a discrepancy of plus/minus 0.5 rating points on a scale of one-to-five and included all absolute ratings with discrepancies larger than this.)

- The largest discrepancy was indicated for on-time delivery of projects. Users feel this is an important requirement—perhaps because they have a hard time meeting it in-house—and are unhappy with vendors' inability to deliver on time. Not only are schedules missed, but budgets as well.

Exhibit IV-3

User Expectations versus Systems Operations Vendor Performance



Source: INPUT

- Meeting requirements/specifications, the caliber of personnel, the presence and quality of the help desk, and the vendor's speed of response to issues that arise are all noted as significant discrepancies.

- Interestingly, the least of the larger discrepancies is the price of outsourcing. Though it's higher than users want, pricing is more in line with their expectations than the other issues cited above.

B

Performance in Desktop Services

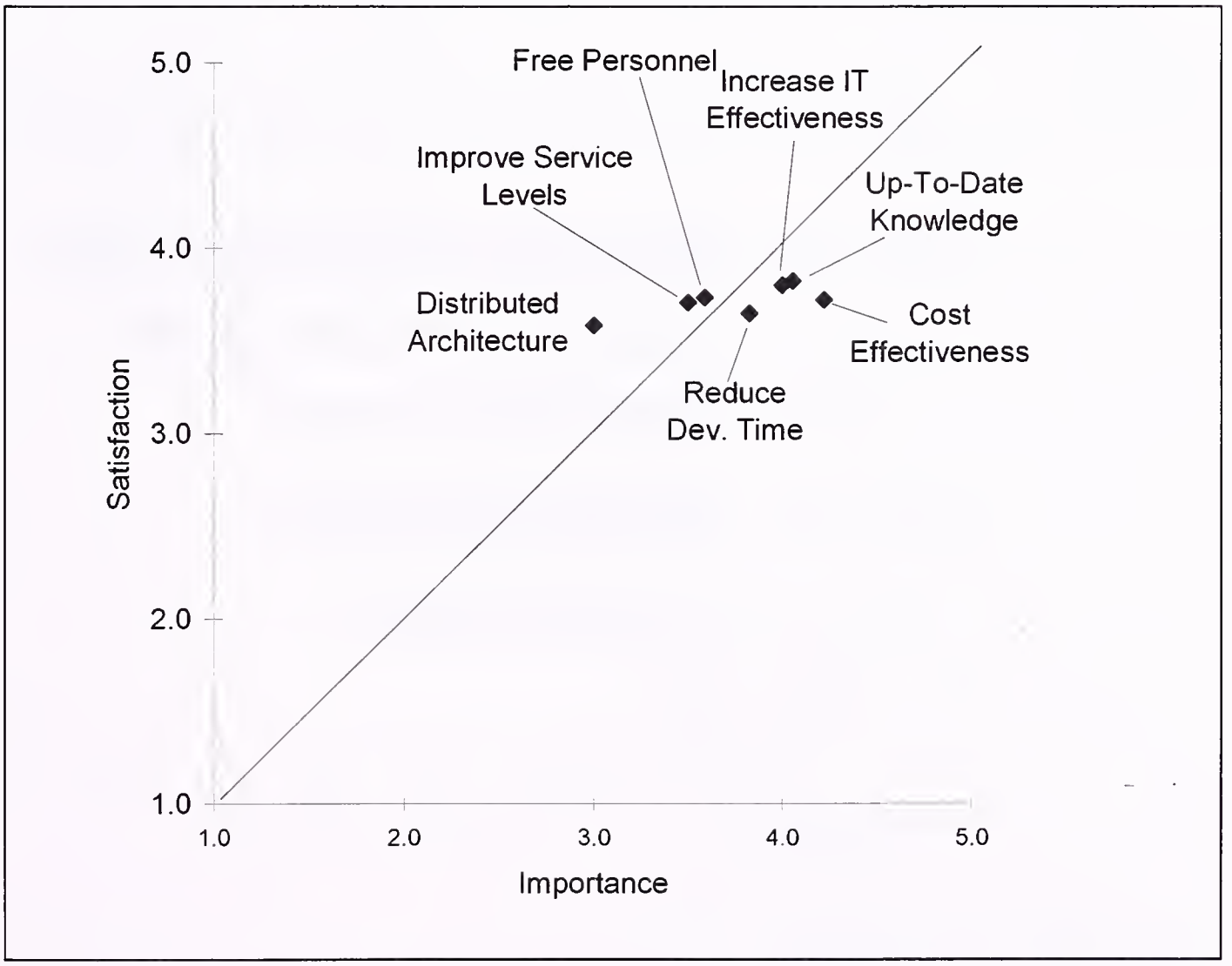
Desktop services include the day-to-day management of the personal computer infrastructure, including servers and local-area networks. Seventeen percent of the respondents indicated use of outsourcing for this function. Again, a number of industries were represented in this data segment, but the average company revenue, at $4.9 billion, was larger than for some other segments.

1. Satisfaction with Outsourcing in Meeting Goals

Users in this relatively new outsourcing arena are finding that their outsourcing goals are being met (see Exhibit IV-4). All discrepancies, positive and negative, were relatively small except for the delivery of a distributed architecture, where satisfaction exceeded importance, and a less-than-satisfactory cost effectiveness performance. The former, mentioned throughout this report, seems to be a positive, unanticipated result of outsourcing. The latter, also mentioned throughout this report, seems to be a nagging desire, even an unrealistic expectation, to lower costs through outsourcing. While entering the competitive arena for services has an intuitive notion of lower costs, vendors may be reinforcing this expectation through their selling propositions. To ensure that this discrepancy doesn't expand to a size where contracts are not renewed or are canceled, vendors need to help users develop realistic views of the cost effectiveness obtainable through outsourcing.

Exhibit IV-4

Users' Satisfaction with Desktop Services Outsourcing



Source: INPUT

2. Vendor Roles Expected by Outsourcing Users

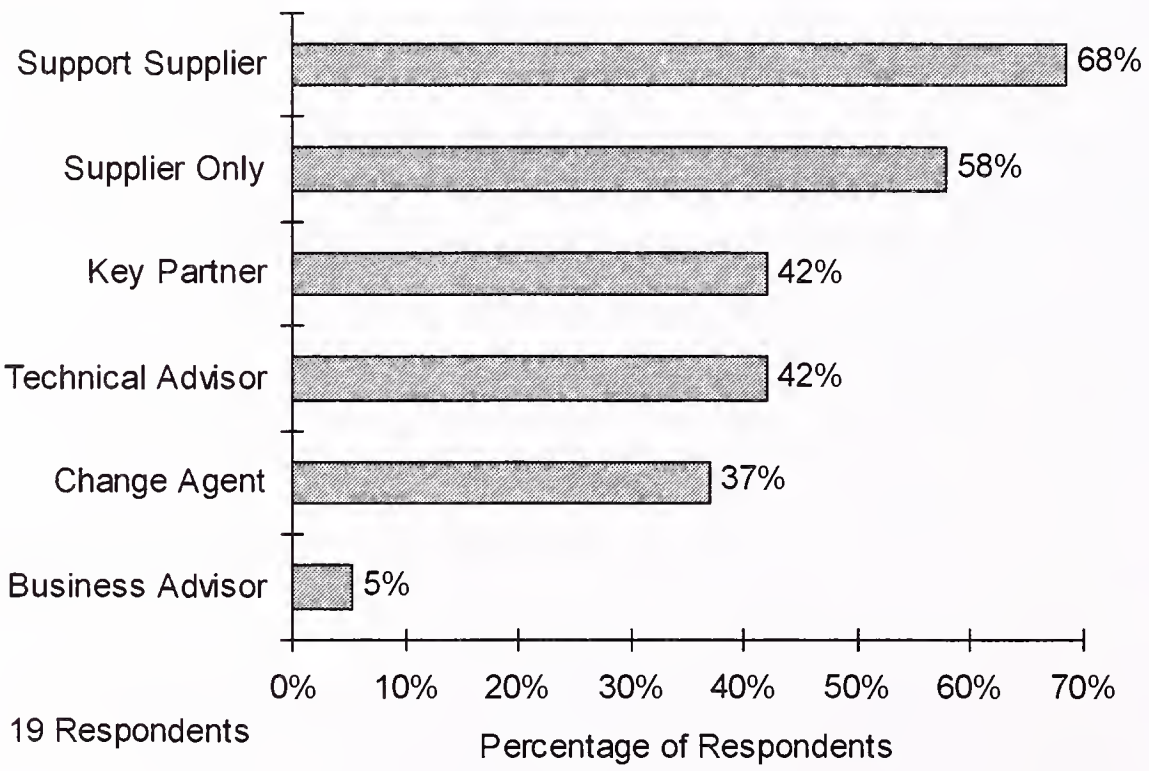
Users expect the primary role of desktop services outsourcing vendors to be one of supplying support (see Exhibit IV-5) or other specific services. Partner/advisor roles for this segment are similar to the sample as a whole, but this group also favors the vendor as a change agent, a role not frequently expected by users of other outsourcing functions. To be sure, this role was secondary to both the supplier roles and the partner/advisor roles.

It may be that the constant change in services requirements and the extent of the functional user base in each company requires companies to look to the vendor for help in such areas as training, hardware or software selection, enhanced performance support systems, documentation, and the like.

A business advisor role was not desired by this segment. While some other functions are more at the core of the organization and could be facilitated by the vendor as advisor, desktop services is not. Vendors would do well to focus on the supply of required services, which might be broad but not mission critical.

Exhibit IV-5

Roles Expected of Desktop Services Outsourcing Vendors



Note: Number of respondents = 19

Source: INPUT

3. Users' Satisfaction with Outsourcing Vendors

User importance-vendor performance discrepancies were mostly negative for desktop services users. As indicated in Exhibit IV-6, the most severe discrepancy was in on-time delivery. Users' expectations were very high and that may have contributed to the low performance ratings, the lowest of the discrepant criteria. There may be a link between this perceived poor performance and the finding noted earlier that desktop services outsourcing users expect vendors to assume the roles of supplier, advisor/partner, and change agent. Perhaps these several hats, some of which get placed after project dates are committed, are one reason schedules are frequently missed. Vendors should make roles and expectations clear at the outset.

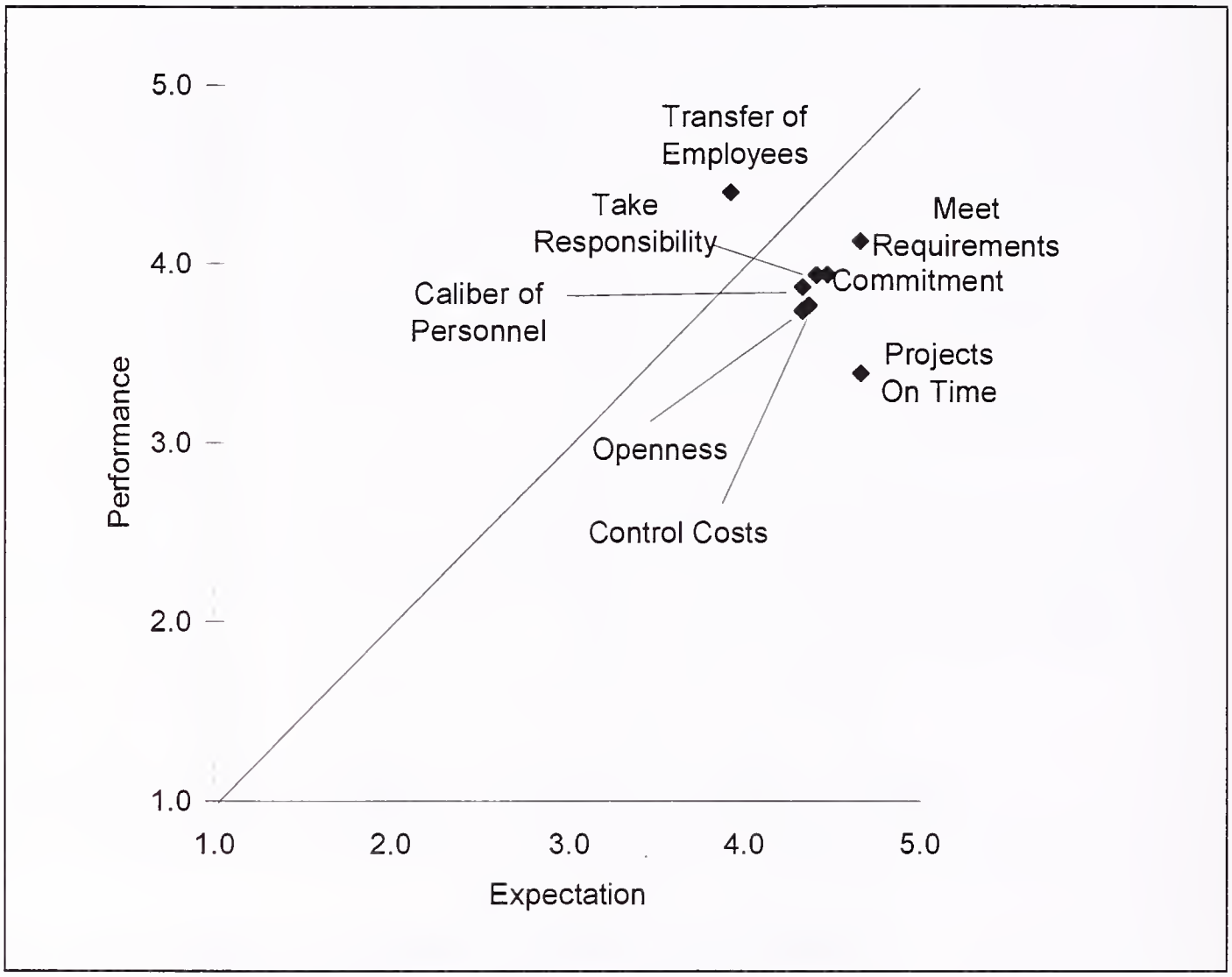
In this context, users' dissatisfaction with vendors' ability to meet requirements/specifications may be accounted for by the fact that the specifics are not pinned down before projects are started. Or, specifications are made, only to be changed in the fast-paced whirl of the desktop.

Related to these two major issues are a number of others: lack of openness, lack of commitment, failure to take responsibility, and inability to control costs. When one issue gets as severe as project delivery seems to have done, other criteria may begin to look worse than they actually are. Even so, these discrepancies are not large, particularly in light of the fact that the expectations are fairly high.

Vendors are applauded for the smooth transfer of help desk personnel from the user's company to the vendor's payroll.

Exhibit IV-6

User Expectations versus Desktop Services Vendor Performance



Source: INPUT

C

Performance in Network Management

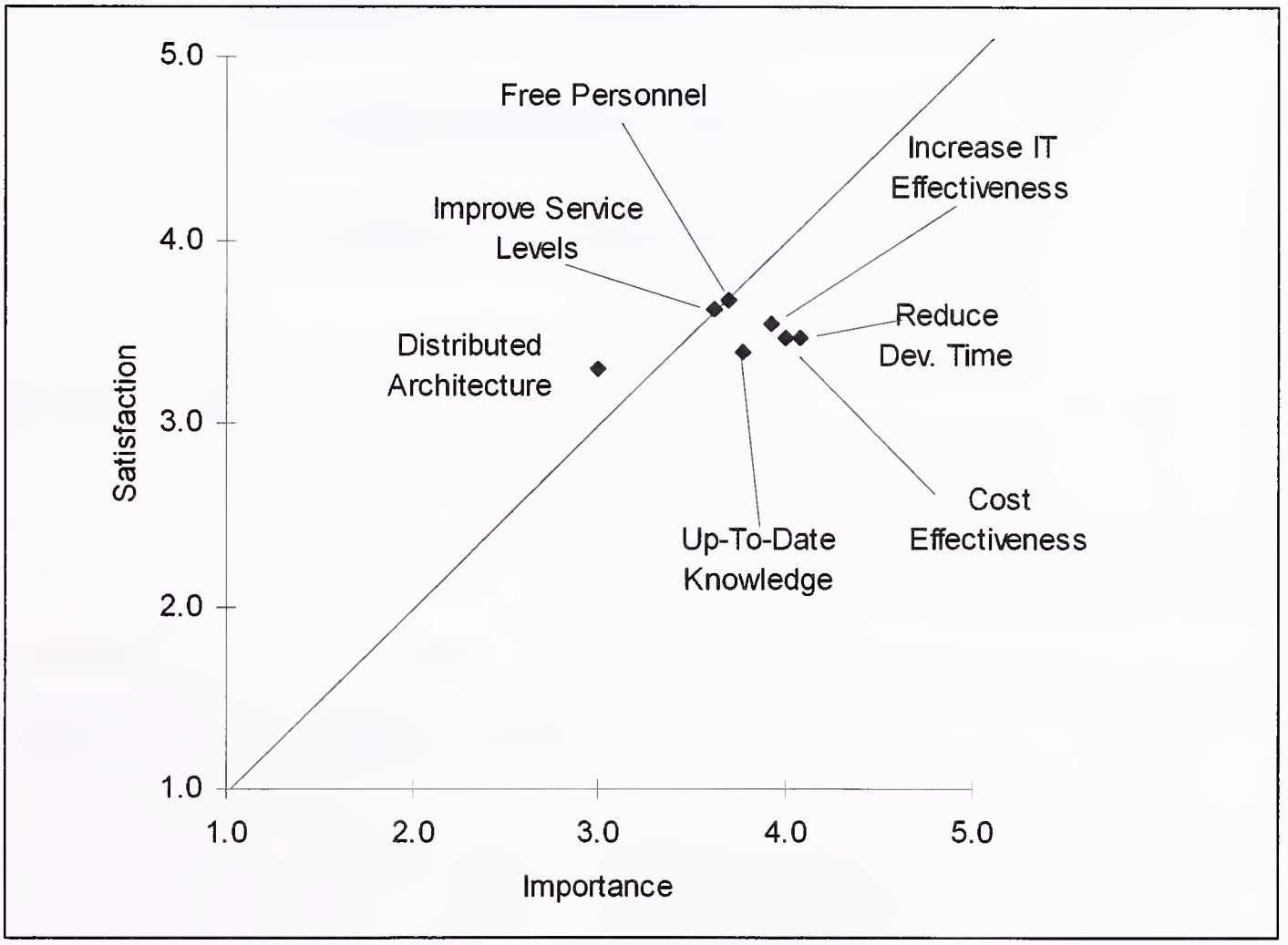
Outsourcing the day-to-day management of the corporate data network has increased in frequency of late. In this survey some 12% of the outsourced functions were network management. Several of these users were from government, federal as well as state and local, but there were some large companies represented as well; the average revenue for commercial companies in this data segment was $5.2 billion. As with most of the other segments analyzed, these users also outsourced other functions, including, with equal frequency, day-to-day operations, desktop services, and applications management.

1. Satisfaction with Outsourcing in Meeting Goals

Exhibit IV-7 shows a basic congruence between the importance of outsourcing goals and the actual ability to meet these goals through outsourcing. Reducing development time and achieving cost-effective IT still are not up to expectations; gaining access to up-to-date knowledge and increasing overall IT effectiveness also fall short. But outsourcing has, according to these users, improved service levels as much as they had expected while freeing personnel for other roles.

Exhibit IV-7

Users' Satisfaction with Network Management Outsourcing



Source: INPUT

2. Vendor Roles Expected by Outsourcing Users

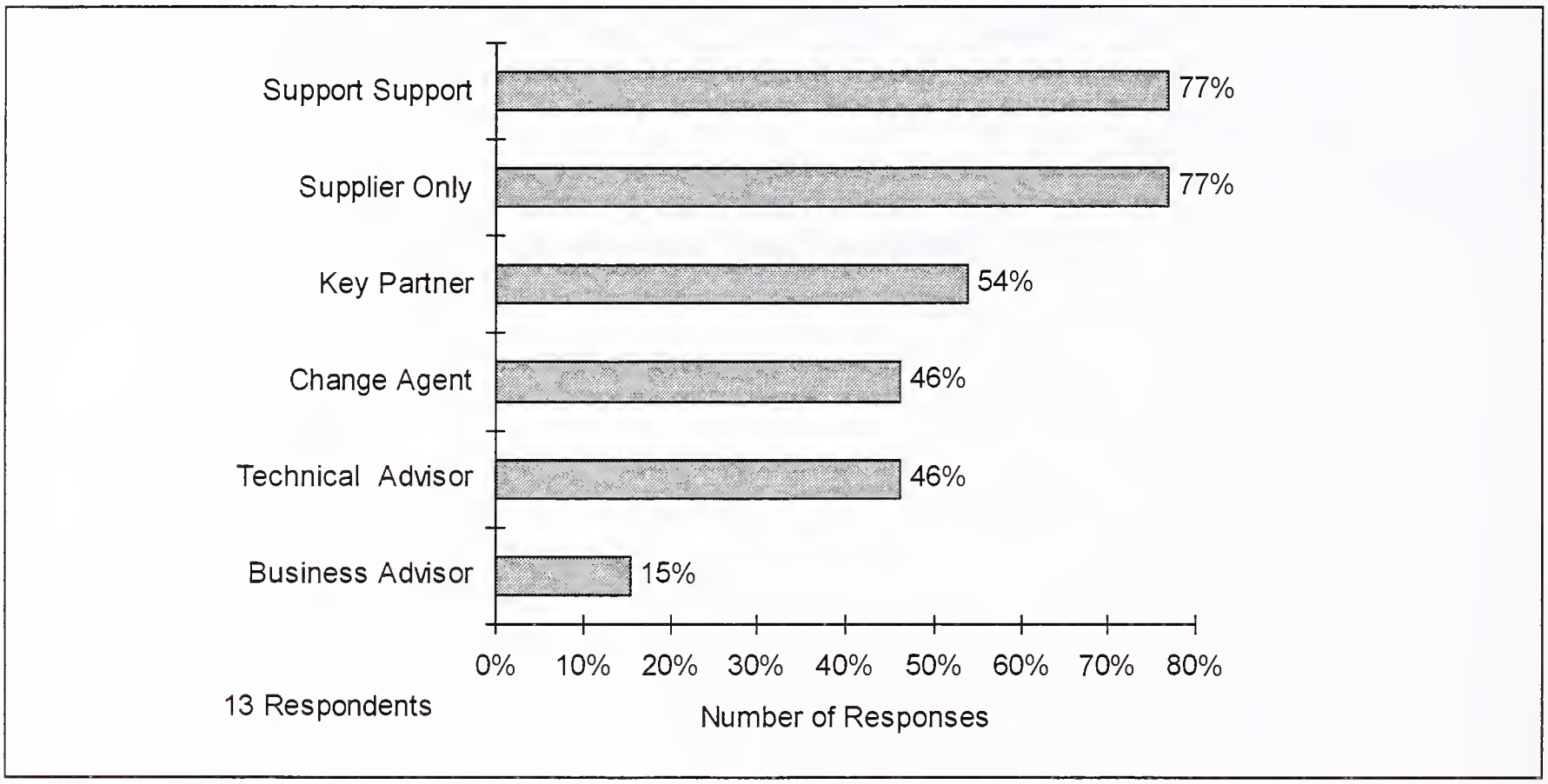
Role expectations for network management outsourcers are similar to other segments analyzed, but there is also a noticeable increase in the frequency of additional roles for these vendors. The supplier role is stronger here, as are the change agent and partner roles. Perhaps the frequencies are elevated because these roles are more likely to be part of government requirements.

A business advisor role is less frequently expected by these users; the role is not particularly relevant to government users and the remainder (primarily

banks and insurance companies) generally felt that such roles are best assumed in-house.

Exhibit IV-8

Roles Expected of Network Management Outsourcing Vendors



Note: Number of respondents = 13 *Source: INPUT*

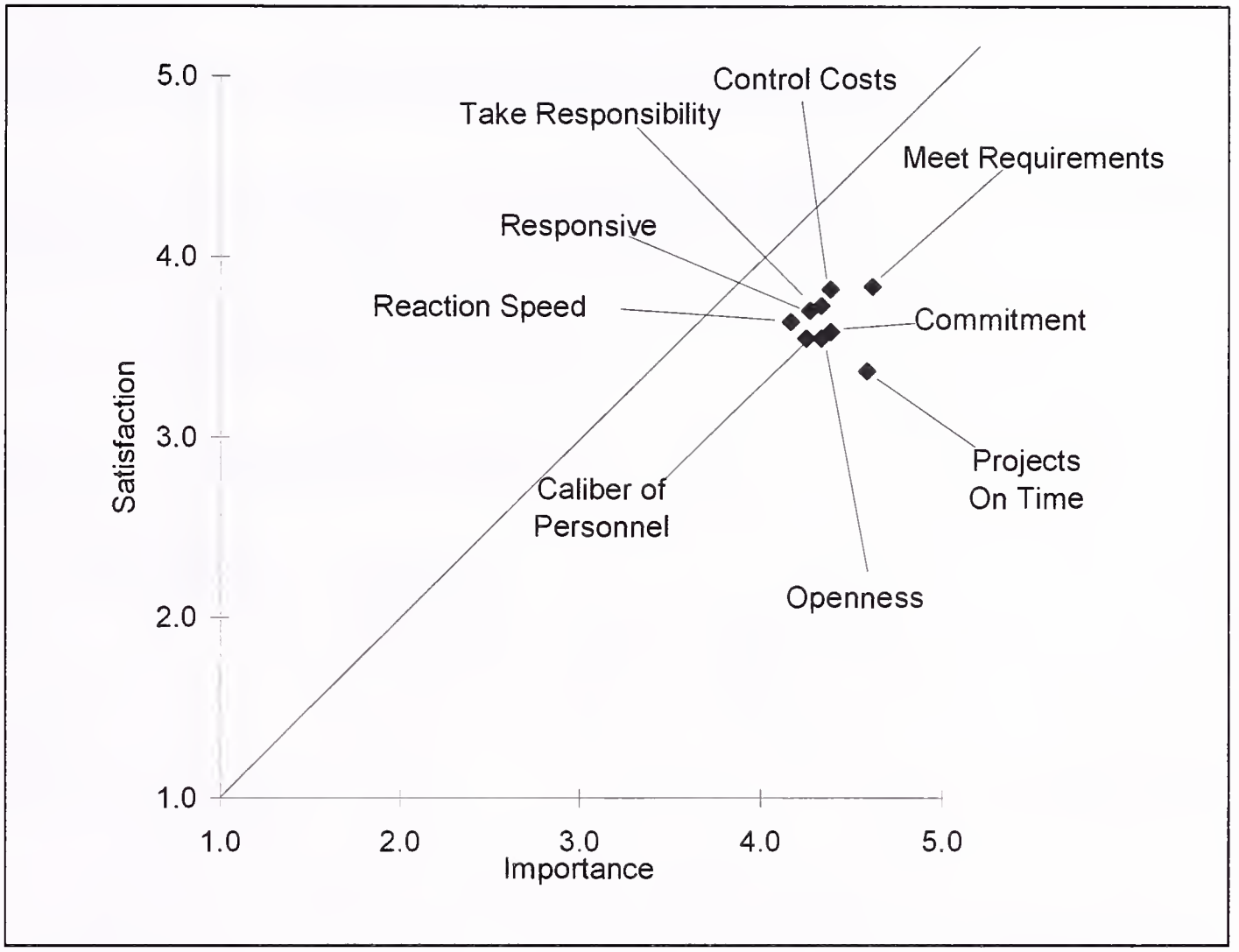
3. Users' Satisfaction with Outsourcing Vendors

A number of discrepancies—all negative—appeared for these users (see Exhibit IV-9). With two exceptions, expectations all cluster in the 4.0-4.5 range (out of 5) and perception of performance clusters in the 3.5-4.0 range. In general, these discrepancies deal with the quality of the user-vendor relationship: failure to be open, to take responsibility, to respond quickly, etc. Network management vendors seem to provide the breadth and depth of services, even to satisfy on terms and conditions, but cannot seem to meet user expectations for the quality of the relationship.

The two exceptions are meeting requirements and on-time delivery. Similar to users' reports from other segments, vendors scored poorly on both criteria. User do seem to have very high expectations in both of these areas and in at least one, meeting requirements, vendors performed adequately—yet still fell short of expectations.

Exhibit IV-9

User Expectations versus Network Management Vendor Performance



Source: INPUT

D

Performance in Applications Management

Applications management outsourcing was the second-most frequently cited service, at 24% of the total outsourced services for this sample. Support and maintenance for in-house development applications, including responsibility for new systems development as a preferred supplier, has grown in popularity and now extends to relatively small companies (the average revenue size of companies in this segment was $2.3 billion).

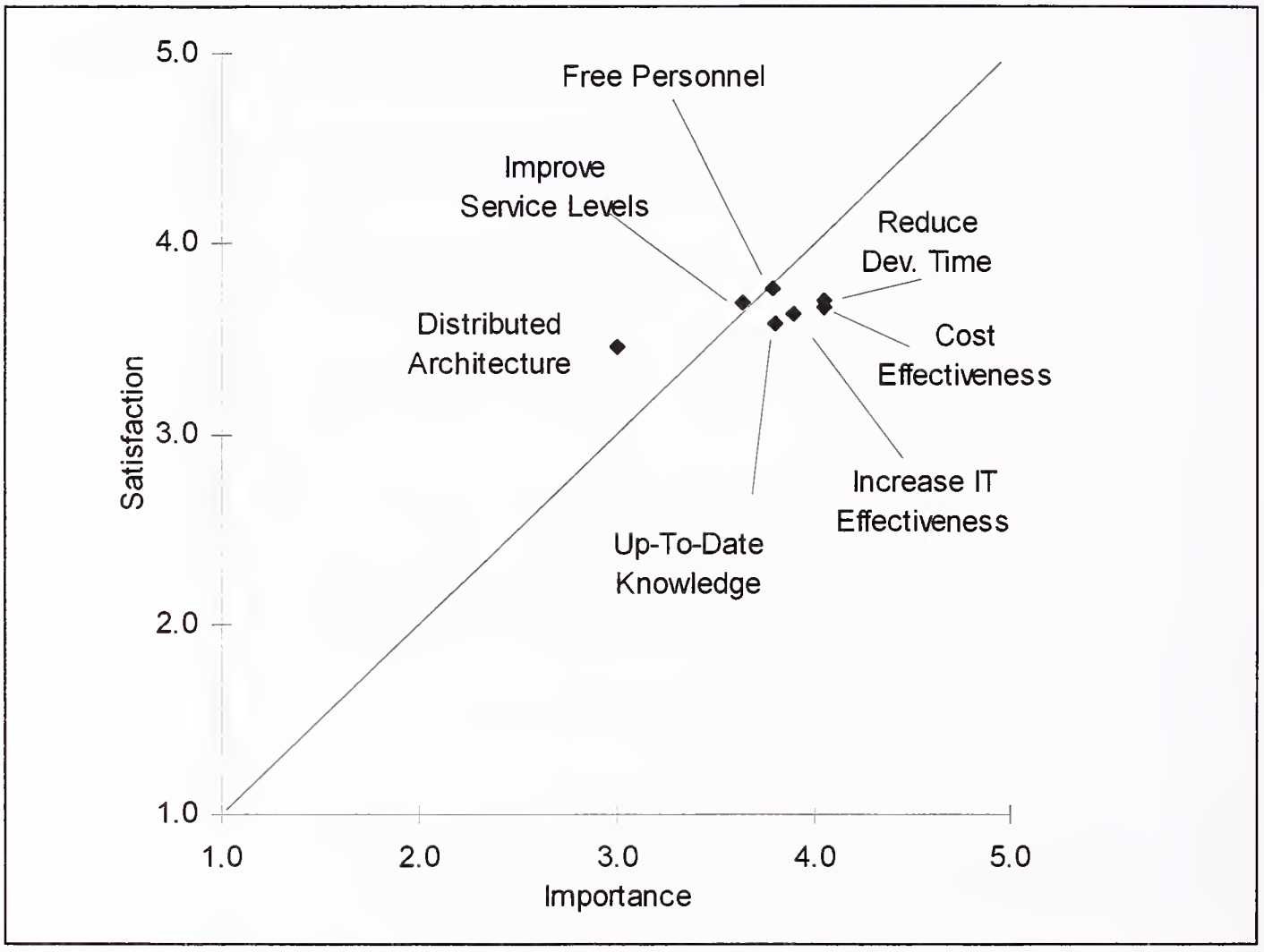
1. Satisfaction with Outsourcing in Meeting Goals

Users report general satisfaction with this type of outsourcing; goal attainment shown in Exhibit IV-10 is closer to congruence than in other segments reported. Users report that outsourcing falls short in terms of increasing cost effectiveness and reducing development time—complaints heard from other segments as well.

Expectations are not as excessive in this functional area as indicated by the 3.75-4.25 range. The unsatisfactory experiences most users have had with in-house development may have served to limit expectations. Even the goal of increasing the cost effectiveness of IT is more limited by these users. Vendors seem to be close to beating expectations in this outsourcing function.

Exhibit IV-10

Users' Satisfaction with Applications Management Outsourcing



Source: INPUT

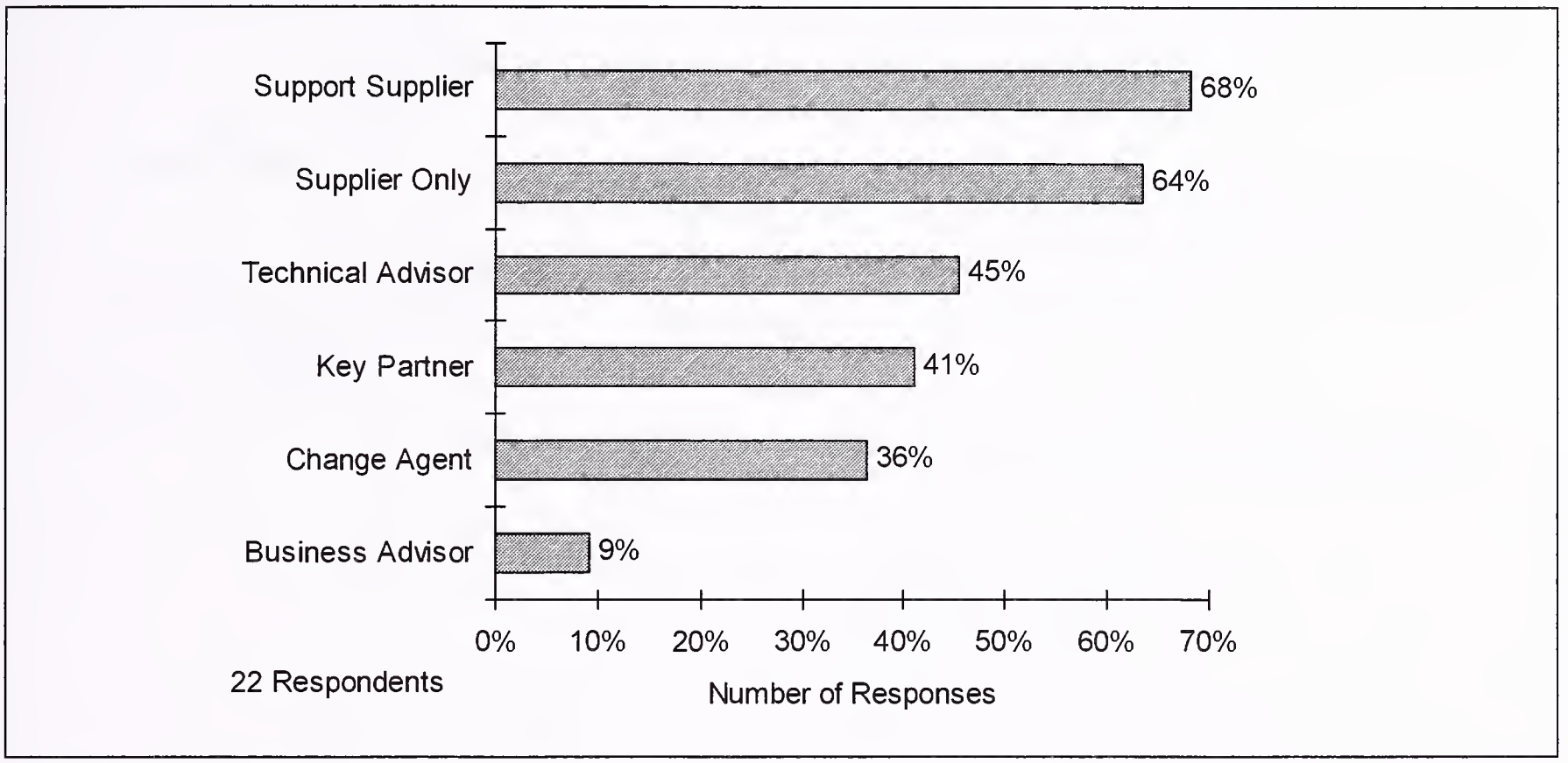
2. Vendor Roles Expected by Outsourcing Users

Expected roles for applications management outsourcers mirror those of other segments: first, a supplier; second, an advisor/partner; and third, a change agent. Business advising is less frequent and on a par with other segments.

The pure supplier role is not as strong in this segment; other roles are mentioned more frequently. Being technical advisors, for one, is required of vendors to ensure that applications are current with both hardware and software technology and easily ported to the next generation.

Exhibit IV-11

Roles Expected of Applications Management Outsourcing Vendors



Note: Number of respondents = 22

Source: INPUT

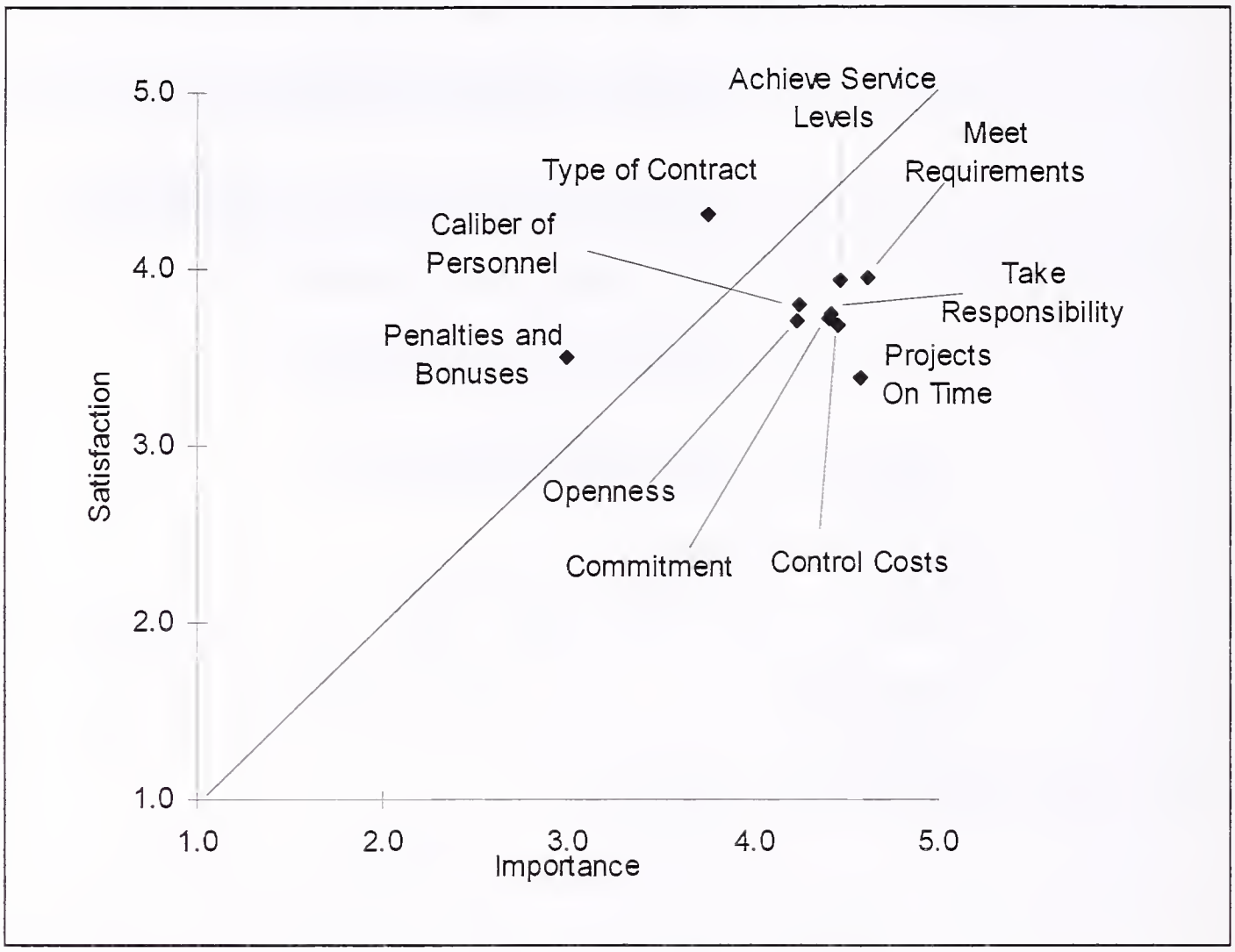
3. Users' Satisfaction with Outsourcing Vendors

Exhibit IV-12 shows a cluster of measures for which vendor satisfaction of criteria is less than expected. These criteria deal mostly with vendor performance, either in terms of the work itself or in terms of the user-vendor relationship.

Outlying these are dissatisfaction with the vendor's ability to meet requirements and specifications and, worse, lack of on-time delivery. The former has high performance against high expectations, a condition in which improvements may be "requested" by users, but current performance will not be a deal breaker. On the latter, however, the perception of poor performance is considerable, even though expectations are high. Users may demand improvement.

Exhibit IV-12

User Expectations versus Applications Management Vendor Performance



Source: INPUT

E
Performance in Business Operations Management

Business operations management is the least frequent outsourcing activity (at 8% of the total types of outsourcing services mentioned) according to these respondents. Still, large companies find benefits to moving whole functions such as accounting or fulfillment to an outside supplier; average revenue size for this segment was $2.8 billion.

1. Satisfaction with Outsourcing in Meeting Goals

Except for improvement in IT cost effectiveness, goals are modest (see Exhibit IV-13) and satisfaction is, correspondingly, greater.

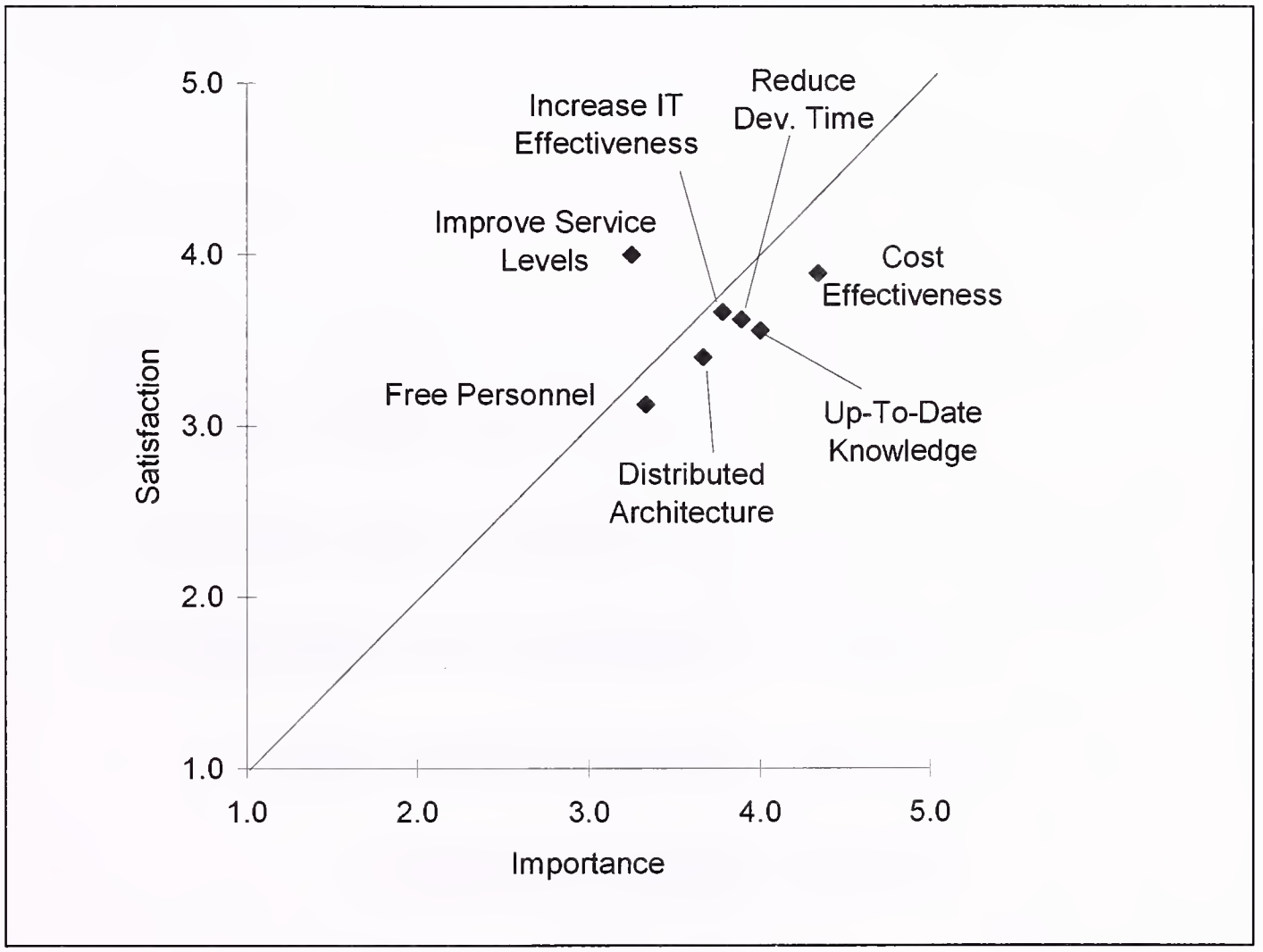
- Service levels are reported to be improved beyond users' expectations. Any caution that users had before deciding to outsource may have been overcome by strong vendor performance in executing the business functions outsourced.

- These improvements to the business function, however, were to some extent negated by less-than-expected performance in the improvement of development time, freeing personnel, creating a distributed architecture, adding up-to-date knowledge to the organization, or increasing overall IT effectiveness.

- Worse, vendors underperformed in delivering cost-effective solutions to the function. It should be noted, however, that ratings of both importance and performance were relatively high, indicating that vendors performed well, yet could not match the clients' requirements.

Exhibit IV-13

Users' Satisfaction with Business Operations Outsourcing



Source: INPUT

2. Vendor Roles Expected by Outsourcing Users

As might be expected of users who choose to outsource an entire business function rather than a piece of the operation, users require multiple roles of their vendors. All roles were frequently mentioned (see Exhibit IV-14).

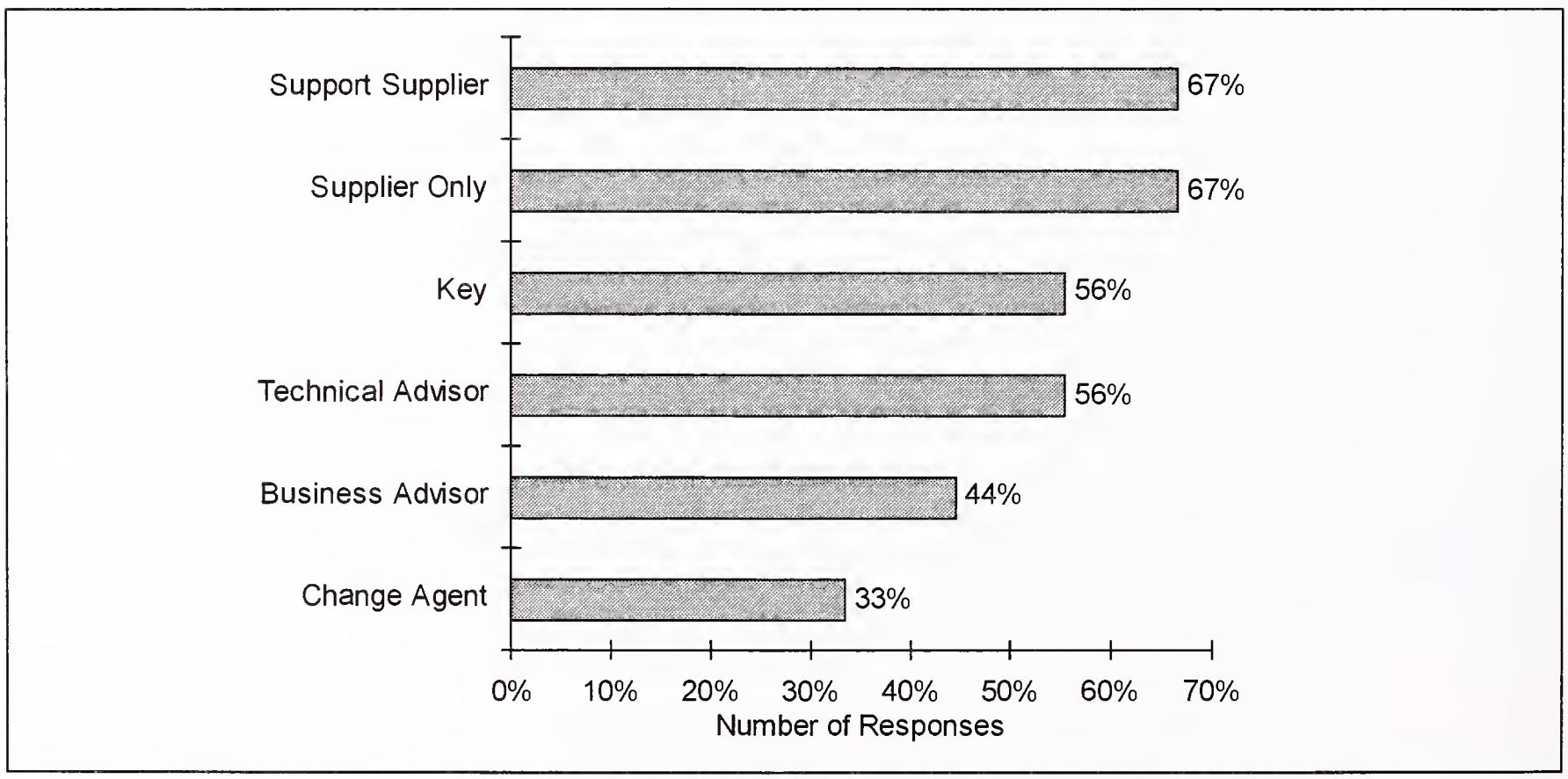
- These users are similar to those in other segments in expecting their outsourcing vendor to be a supplier first. Managing the outsourced business operation is clearly the number-one goal.

- Partner and technical advisor roles were secondary to these users, as they were to users in the other segments. However, unlike the other users, these users reported that these roles are more frequently expected. As the scope of the outsourcing increases, the expected scope of the vendor increases as well.

- This is confirmed in the expectations for change agent and business advisor roles. Though these roles were tertiary, users reported that they were more frequently required in this segment of outsourcing. Acting as a business advisor, in particular, was a strong expectation, being expected by nearly 50% of the respondents. The indication is that users allow, even expect, broader roles for the outsourcing vendor when entire business functions are involved, but desire more limited roles when outsourcing is focused on only IT-related activities. The implication of this finding is that vendors need to capture the business function outsourcing to release the opportunities in other areas.

Exhibit IV-14

Roles Expected of Business Operations Outsourcing Vendors



Note: Number of respondents = 10

Source: INPUT

3. Users' Satisfaction with Outsourcing Vendors

In working toward these opportunities there are perils, however. As indicated in Exhibit IV-15, users are generally dissatisfied with vendor performance vis-à-vis expectations. (In this particular gap analysis there were so many discrepancies at the 0.5 level that the threshold for inclusion was raised to 0.7 to facilitate the graphic presentation of results.)

- The largest discrepancy was reported to be in the vendors' inability to control costs as expected. Users outsource for reasons of cost effectiveness and report that vendors are not able to deliver on this critical issue.

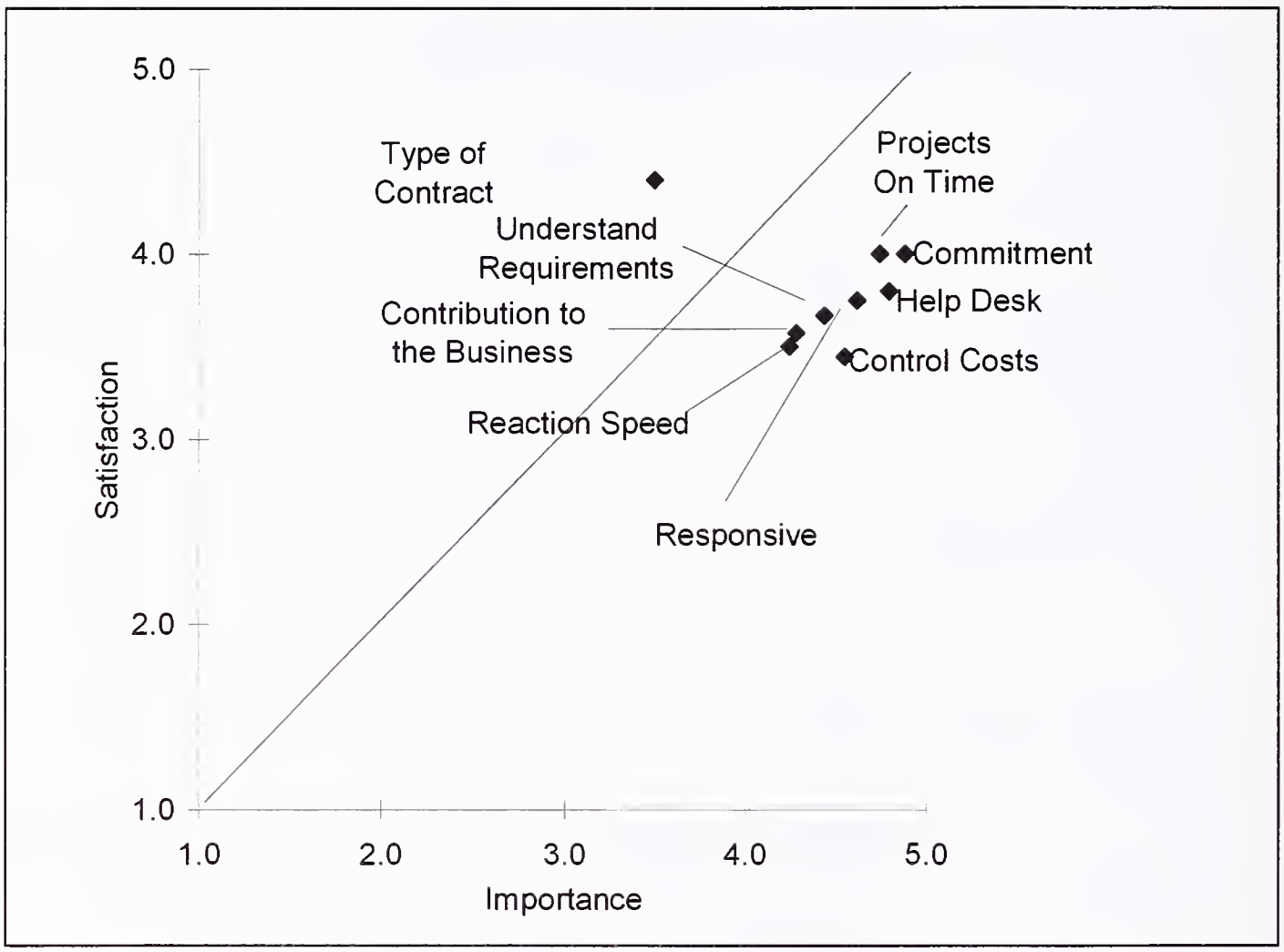
- Some implied reasons may be lack of commitment or less-than-satisfactory responsiveness on the part of vendors. These criteria both showed wide discrepancies between expected and actual performance. A related issue, contribution to the business, while not as distinct as the former two, also suggests the general concern of users over the ultimate benefits of business function outsourcing. This finding is made all the more troubling in light of the fact that users offer expanded business-related roles to these vendors.

- Specific problems that users point to include the quality of the help desk offering, inability to deliver projects on time, lack of understanding of requirements, and slow reaction time.

- The single positive discrepancy of any size was the type of contract offered by vendors. While this was less important to users, they recognized the contribution of vendors in this regard. This recognition is unlikely to weigh heavily against the negatives reported by users.

Exhibit IV-15

User Expectations versus Business Operations Vendor Performance



Source: INPUT

F
Conclusions

A number of observations can be made from these results:

- Achieving cost effectiveness is a key motivator for deciding to outsource. But users report that the inability of vendors to control costs and make on-time deliveries makes cost effectiveness difficult to achieve.

- The expected roles of vendors expand in proportion to the scope of the outsourcing service: limited functionality outsourced limits roles primarily to the supply of service, while outsourcing primary business functions invites broader roles for vendors that go beyond the provision of service and into the role of business advisor.

- Terms and conditions, including price and ease of transfer of employees, are secondary considerations for users. Beyond cost effectiveness, they want improvement of operations that were not attainable in-house.

- Except for cost effectiveness, expectations are not inordinately high (e.g., "good" or "excellent" performance range), yet vendors are generally given credit for only average performance.

G
Recommendations

User Satisfaction with Outsourcing

- Vendors should focus on cost effectiveness issues in selling outsourcing services, as this issue is the single most important one to buyers. If vendors can't deliver cost effectiveness, the customer must be repositioned to other vendor benefits.

- While emphasizing net savings, however, vendors must avoid setting customer expectations for cost effectiveness changes that are unrealistic and unattainable by the vendor.

- Vendors may be able to charge a premium for their performance in freeing customer personnel and implementing distributed architecture as performance currently exceeds requirements. An alternative approach is to reduce the emphasis on delivery in this area.

Vendor Performance Across Outsourcing Types

- Vendors selling outsourcing should focus on their ability to get the job done and on their intention to engender a quality relationship with the customer that fosters effective and efficient operations.

- Then, vendors must deliver on both of these criteria. In fact, vendors should focus on these and worry less about depth and breadth of offering or the terms and conditions of the deal. These other issues are not as important to the customers either during the sale or after the start of outsourced operations.

- If there is a single key ingredient for success, it is offering solid proof of the ability to meet, even exceed, requirements. A proven track record of success in outsourcing is paramount. Getting the job done on time and within budget are the two measures of vendor performance on this issue.

- Commitment to the customer and the outsourcing project are also important and should be a central premise in the sales positioning and an obvious ingredient among the deliverables.

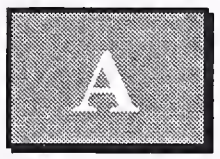
Vendor Performance Within Outsourcing Types

- Though it may seem obvious, the closer the outsourced activities are to the core of the company, the more customers are likely to demand from the vendor. Vendors who take on the entire business function, for example, should be prepared to deliver high levels of commitment—as if the performance was for their own company. This commitment is not only in the attitude of how things are done, but what is done: delivering on time, exceeding requirements, etc.

- Within each type of service outsourced, cost effectiveness is a key concern of customers. Vendors must be vigilant to ensure that they are adding value above and beyond what customers could reasonably expect to do on their own.

- If vendors are not going to deliver on cost effectiveness to the satisfaction of customers, the customers may demand more cost control. Vendors may want to anticipate this requirement and find ways for customers to participate in general project management, resource allocation, budgeting, etc.

Overall, vendors should be pleased with the general level of user satisfaction with outsourcing. While there are still serious discrepancies between expectations and performance, vendors have proven that they can deliver satisfactory outsourcing work.



Definition of Terms

Information Services

Information Services are computer/telecommunications-related products and services that are oriented toward the development or use of information systems. Information services typically involve one or more of the following:

- Use of vendor-provided computer processing services to develop or run applications or provide services such as disaster recovery or data entry (called *Processing Services*)
- A combination of computer equipment, packaged software and associated support services which will meet an application systems need (called *Turnkey Systems*)
- Packaged software products, including systems software or applications software products (called *Software Products*)
- People services that support users in developing and operating their own information systems (called *Professional Services*)
- The combination of products (software and equipment) and services where the vendor assumes total responsibility for the development of a custom integrated solution to an information systems need (called *Systems Integration*)
- Services that provide operation and management of all or a significant part of a user's information systems function under a long-term contract (called *Outsourcing*)
- Services that support the delivery of information in electronic form—typically network-oriented services such as value-added networks, electronic mail and document interchange (called *Network Applications*)

- Services that support the access and use of public and proprietary information such as on-line data bases and news services (called *Electronic Information Services*)

- Services that support the maintenance and operation of computer and digital communication equipment (called *Equipment Services*)

In general, the market for information services does not involve providing equipment to users. The exception is where the equipment is part of an overall service offering such as a turnkey system, an outsourcing contract, or a systems integration project.

The information services market also excludes pure data transport services (i.e., data or voice communications circuits). However, where information transport is associated with a network-based service (e.g., electronic data interchange services), or cannot be feasibly separated from other bundled services (e.g., some systems operations contracts), the transport costs are included as part of the services market.

The analytical framework of the information services industry consists of the following interacting factors: overall and industry-specific business environment (trends, events and issues); technology environment; user information system requirements; size and structure of information services markets; vendors and their products, services and revenues; distribution channels; and competitive issues.

Outsourcing Services

Over the past few years a major change has occurred in the way clients are buying some information services. The shift has been labeled *Outsourcing*.

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

INPUT defines outsourcing as a long-term (greater than one year) relationship between a client and a vendor in which the client delegates all, or a major portion, of an operation or function to the vendor. The operation or function may either be solely information systems outsourcing-based, or include information systems outsourcing as a prominent component of the operation (at least 30% of the budget).

INPUT considers the following subcategories to be outsourcing-type relationships and in aggregate to represent the outsourcing market.

- *Platform Systems Operations*—The vendor is responsible for managing and operating the client's computer systems.

- *Applications System Operations*—The vendor is responsible for developing and/or maintaining a client's applications as well as operating the computer systems.

- *Network Management*—The vendor assumes full responsibility for operating and managing the client's data communications systems. This may also include the voice communications of the client.

- *Application Management/Maintenance*—The professional services vendor has full responsibility for developing and/or maintaining some or all of the applications systems that a client uses to support business operations. The services are provided on a long-term contractual basis.

- *Desktop Services*—The vendor assumes responsibility for the deployment, maintenance, and connectivity between the personal computers and/or intelligent workstations in the client organization. The services may also include performing the help-desk function. The services are provided o a long-term contractual basis.

- *Business Operations*—Business operations outsourcing (also known as business outsourcing or functional outsourcing) is a relationship in which one vendor is responsible for performing an entire business/operations function, including the information systems outsourcing that supports it. The information systems 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 outsourcing market.

(Blank)

B

Questionnaire—Outsourcing Vendor Performance Analysis

1. Which of the following functions does your company outsource and to whom?

	OUTSOURCED (Y/N)	VENDOR(s)
Day-to-day operation of mainframe and/or standalone mid-range computer equipment)		
Desktop services (i.e. Day-to-day management of the personal computer infrastructure including servers and local area networks)		
Network management (i.e. Day-to-day management of the corporate data network)		
Application management (e.g. Support and maintenance for in-house development applications; Responsibility for new systems development as a preferred supplier)		
Business operations management (e.g. Business functions such as accounting or fulfillment)		
Other (please describe		

2. On a scale of 1-5 with 5 being very important, how important to your company was each of the following goals in your decision to outsource?

3. How successful has outsourcing itself been in helping you achieve each of these goals (1-5 with 5 being very successful)? This is not necessarily how satisfied you are with the vendor, but rather the concept and benefits of outsourcing.

	Q#2 IMPORTANCE AS A GOAL	Q#3 SAT.WITH OUTSOURCING
Become more cost effective in using IT		
Improve operational service levels		
Introduce up-to-date technical knowledge		
Reduce the time taken to implement new systems		
Free in-house personnel for other work		
Adopt a distributed, rather than a centralized, architecture		
Increase effectiveness in applying IT to the business		
Others (list)		

4. Which of the following roles do you perceive your outsourcing vendor providing to your company (check all that apply)

____ Supplier of agreed service, and nothing else

____ Business advisor

____ Technology advisor

____ Agent of change

____ Supplier of support services

____ Key partner

____ Other:

5. On a scale of 1-5 with 5 being very important, how important to your company is each of the following vendor criterion:

6. What outsourcing vendors did you evaluate for this outsourcing contract?

7. What vendor did you choose? (Fill in names in the chart below of chosen and next top candidate.)

Vendor Criteria	# 5 Importance	# 8 Vendor	# 8 Candidate	# 9 Vendor Satisfaction
Scope of operational capability				
Ability to meet requirements/specifications				
Cooperation with other vendors				
Vendor reputation				
Innovative approaches to requirements				
Caliber of personnel				
Capability of help desk				
Achievement of operational service level agreements				
Delivery of projects on time				
Ability to control costs				
Continuity of personnel				
Speed of reaction to requests				
Responsiveness to day-to-day issues				

Understanding of your business requirements				
Ability to contribute to business benefits				
Commitment to achieving agreed-upon requirements				
Openness of communication				
Willing to take responsibility for problems				
Willingness to compromise				
Price				
Contract flexibility				
Type of contract				
Terms of transfer of employees				
Ease of termination				
Penalties and bonuses				
Service level agreements				
Sharing of risk with vendor				
Geographical coverage, etc.				

8. Prior to choosing a vendor, how would you have rated the abilities of the top two candidates in the following areas?

9. Now that you have been using (the chosen vendor) for your outsourced project, how satisfied are you with them in the following areas?

10. Would you describe the process that your company went through in making the decision to go with an outside vendor for these services, and then how you selected and outside vendor, identifying any challenges that you may have experienced?

11. What would you do differently next time?

12. What issues might prevent you from using an outsourcing vendor in the future? (e.g., control, budget, no vendor available with the capabilities you need, inflexibility of contracts, etc.)

13. Are you considering any changes to the scope of this current outsourcing arrangement? If so, what do you plan to change? Why?

14. Are you considering changing outsourcing vendors? If so, why?