

EXCERPT

U.S. Application Outsourcing Services 2006 Vendor Analysis: Competitive Landscape and IDC Leadership Grid (Excerpt from IDC #204179)

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IN THIS EXCERPT

This IDC excerpt is taken from the IDC market analysis study *U.S. Application Outsourcing Services 2006 Vendor Analysis: Competitive Landscape and IDC Leadership Grid* (IDC #204179, November 2006), by Barry Rubenstein. All or part of the following sections are included in this excerpt: IDC Opinion, In This Study, Methodology, IBM Vendor section, and IDC Leadership Grid for U.S. AO Services. Also included are Table 16 and Figure 2.

IDC OPINION

The competitive landscape in the U.S. application outsourcing (AO) services market is highly dynamic, impacted by both a wide variety of macrolevel trends and the emergence of several newly competitive vendors, including ACS, Siemens, and Unisys. This study will examine these trends and how they are impacting the ability of leading vendors to increase their market share. With these points in mind, it is not surprising that the qualities that will define the market share winners of the next few years are not necessarily the ones that brought success to today's leaders. In the highly competitive U.S. AO market, only the vendors with a commitment to ongoing innovation — both for the low-cost delivery of high-quality services and to transform customer's IT environments — will succeed. This study identifies several trends that lead to criteria by which AO vendors can be judged:

- A commitment to ongoing investment in intelligently deployed global sourcing
- The ability to transform and modernize application portfolios to the service oriented architectures (SOAs) that tomorrow's agile business will rely on
- Capabilities in a broad range of industries, with breadth and depth being equally important
- A vision for the future of dynamic IT — laying out a road map for the modernization journey
- A strong ecosystem of technology partners
- The automated processes to maintain and manage application portfolios with the highest levels of quality for the lowest possible labor cost

IN THIS STUDY

This study analyzes the U.S. AO services competitive landscape by examining and comparing a select list of service providers. The purpose of this document is to help services vendors, their customers, alliance partners, and the financial community differentiate the capabilities of firms that compete in the U.S. AO market. The study looks at the performance of these firms in addition to their key growth strategies and future directions.

Methodology

Vendor Selection

To remain as objective as possible in choosing which vendors to include in this study, IDC used two criteria. First, we included the top 10 market share holders in the United States, as of 2005, excluding offshore pure-plays (see explanation in the Offshore Vendors section). A list of the top 10 market share holders in the United States and worldwide is included in *Worldwide and U.S. Application Management Vendor Shares, 2005: IDC's Top 10 Vendors* (IDC #203995, October 2006). Those vendors are (in alphabetical order): Accenture, Capgemini, CGI, CSC, EDS, IBM, Keane, Northrop Grumman, and Perot Systems.

Next, IDC reached out to a select list of vendors that are not top 10 market share holders, but that we believe are making a significant impact on the U.S. AO market. These vendors include: ACS, HP, Lockheed Martin, SAIC, Siemens, and Unisys.

Earlier this year, IDC contacted all of these vendors with a detailed request for information (RFI) that included both quantitative and qualitative questions on several topics. Of the 15 vendors contacted, all but two responded to the RFI. Those two, Lockheed Martin and SAIC, are not included in this study.

Once the RFI was completed, we gave the vendors the option of follow-up conversations to answer additional questions and put color around their written responses. Most, but not all, of the vendors agreed to these in-depth interviews.

Based on the information collected from the RFIs, the interviews, and from IDC's ongoing interactions with vendors and end users, we created a set of evaluation criteria and then set forth to analyze the competitive differentiation of the 13 included vendors, the results of which make up this study.

Evaluation Criteria

The competitive analysis conducted in this study has several dimensions. First, we evaluated the vendors in the written portion of this document. That evaluation is broken down into several sections:

- ☒ **AO business performance.** This part of the analysis examines the vendor's AO business performance over the past several years and provides IDC's prediction for performance in 2007 and beyond.

- ☒ **Global sourcing capabilities.** This part of the analysis evaluates the vendor's global development and delivery capabilities onsite, onshore, nearshore, and offshore. This category takes into account the vendor's global sourcing scale, ability to delivery globally consistent results, and investments in continued development of offshore delivery centers.
- ☒ **Transformation and modernization capabilities.** This part of the analysis examines the vendor's ability to modernize legacy environments, build SOAs, and transform customers' application environments into business-aligned modern architectures. This category also includes an evaluation of the vendor's ability to manage and optimize entire application portfolios.
- ☒ **Industry expertise.** This part of the analysis evaluates the vendor's vertical experience and specialized industry solutions. This includes an evaluation of the vendor's consulting and architecture capabilities.
- ☒ **Menu of services.** This part of the analysis examines the vendor's overall menu of outsourcing services, including infrastructure management, hosting, and BPO.
- ☒ **Tools and methodologies.** This section of the analysis evaluates the vendor's toolsets, processes, and methodologies for delivering globally consistent AO engagements and automating the labor-intensive aspects of AO.
- ☒ **Vision.** This part of the analysis examines the vendor's vision for the future. Has the vendor placed a "stake in the ground" that tells customers where it is taking them in terms of technology and business agility?
- ☒ **SWOT analysis.** Summarizing the above sections, the SWOT analysis highlights the vendor's strengths (its competitive differentiators), weaknesses (areas that need improvement), opportunities (areas where the vendor should invest), and threats (potential disruptions to the vendor's business). Many of the threats included in the SWOT analysis are common to every vendor in the AO industry and thus are repeated for each vendor.

I B M

AO Direction

IBM is in every way the 900lb gorilla of the AO market. It has the largest market share, the largest number of customers, the largest number of employees, the largest scope of capabilities, and the largest global sourcing network. One clearly thinks of scale when considering IBM, but one should not equate that enormous scale with an inability to adapt to rapidly changing market and competitive conditions. Quite the contrary, IBM continues to show itself as a nimble and innovative competitor in the AO market.

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AO Business Performance

Application management has been one of the relatively few bright spots in IBM's IT outsourcing business over the past year. Its performance has been good, though its

growth rate has been slowing, and as Accenture continues to gain market share, IBM faces the (still somewhat distant) threat of becoming the number 2 revenue earner in the U.S. AO market. IBM is clearly facing some major challenges in its infrastructure outsourcing business, which has served as a significant pipeline for AO deals. As that business has slowed, so has that pipeline. IBM has done an admirable job, however, of building up the standalone AO pipeline by expanding the range of services it offers, becoming more price competitive, and leading the way in innovative areas such as preconfigured solutions built on SOAs.

Global Sourcing Capabilities

IBM's commitment to global sourcing is absolute, with Sam Palmisano publicly announcing earlier this year that the company would be investing \$6 billion in India over the next few years. IBM currently has over 40,000 employees in India, with nearly 80% working in global delivery. IBM is also making significant investments in Brazil and China, both of which are up-and-coming global delivery centers for infrastructure, applications, and business process outsourcing.

Beyond scale, though, IBM also leads in its ability to shift work from center to center as customer and delivery needs dictate. This is the holy grail of global sourcing: the ability to seamlessly shift work around the world. The system is not yet perfect, but IBM has demonstrated impressive capabilities. IBM is also utilizing its service presence in emerging markets such as Brazil, Russia, India, and China as a beachhead for clients looking to enter those markets. Indeed, this is one area where IBM's vast global presence is an even greater competitive differentiator than it first seems. Not only is IBM able to deliver services from nearly any offshore location, it is also able to use that presence to help clients become more global themselves. It's that two-way street that truly unleashes the power of globalization.

Transformation and Modernization Capabilities

IBM features a range of high-value services that complement its traditional AO offerings. These include portfolio optimization services, SOA-based preconfigured solutions, legacy modernization, and application hosting services.

In legacy modernization, IBM offers a full range of services, depending on how much change a client's application portfolio requires. These project-based services, which often occur inside of outsourcing contracts, include code documentation and clean-up to reduce maintenance and operational costs, conversion and replatforming, Web enablement, and full application renovation to modern architectures. IBM differentiates itself in the breadth of its legacy modernization offerings, depth of experience in all industry segments, and ability to use IBM software assets, including WebSphere and Rational tools.

IBM then takes legacy modernization a step further by adding a rapidly growing menu of SOA-based software solutions for industry-specific problems. Building on the Component Business Model, which seeks to decompose business processes into more manageable Web services, these SOA solutions are being developed in India and elsewhere with the input of IBM consultants worldwide. In many ways, IBM is getting into the applications business, one component at a time, creating a powerful value proposition to clients that want to modernize their application portfolios to SOA.

Since its acquisition of Corio, IBM also has one of the most advanced hosted AO offerings available, IBM Applications On Demand (AOD). Despite the "On Demand" moniker, this service is not multitenant software as a service (SaaS), but rather single-tenant application hosting and management. Essentially, AOD is a standardized service for packaged enterprise application implementations, including a pay-as-you-go pricing model. Though hosted AO is not the focus of this study, it is important to note that IBM has a fully realized service offering for customers to transform their environments to.

Industry Expertise

One of the most important assets that IBM gained when it acquired PwC Consulting back in 2002 was a tremendous amount of industry expertise in application services to add to its already impressive portfolio of knowledge. Today, IBM has industry-specific AO solutions for 17 verticals, a portfolio that is unmatched by any competitor. Though IBM has particular strength in banking, insurance, healthcare, and manufacturing, there are very few industry segments where IBM lacks experience, knowledge, and technology assets, and this creates a significant barrier to entry into the AO market for competitors.

Menu of Services

Once again, scale is the name of the game, with IBM having the broadest possible range of IT project and outsourcing services, including application development, systems integration, business and IT consulting, and hosting in cutting-edge datacenters. The aforementioned AOD services use the economies of scale and industrialized processes of a highly standardized hosting and AO offering to give customers even greater flexibility and cost savings than traditional AO. The service is currently limited to somewhat standard deployments of common packaged applications from SAP, Oracle, and others, but its capabilities are expanding rapidly.

For IBM, the sum of these broad capabilities is indeed greater than the parts because regardless of where a customer wants to go, IBM is there, with no major gaps in its portfolio. Additionally, beyond simply having a broad range of services, IBM offers customers a road map and a vision for where it is taking them on the journey to the next generation of dynamic IT. More on this vision, called On Demand, is presented in the Vision section of this profile.

Tools and Methodologies

Much like HP, IBM's software business provides the company with a wide range of tools to be used in the delivery of AO services. The crown jewels in this portfolio are Rational, which includes Rational's development and program and portfolio management tools, and Tivoli for systems monitoring and management. Though both of these products are available to competitors, the IBM AO team's close working relationship with its software colleagues means that IBM gains early access to innovations in those tools. IBM also has a wide array of proprietary tools, including dashboards for customers to monitor system and project status, as well as automated tools for application management and maintenance tasks. Additionally, IBM labs are constantly investing in services innovation, which translates into continued developments in automation for services delivery.

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Vision

IBM has publicly been at the forefront of many of the innovations in IT over the past several decades. That tradition has continued, with IBM being the first vendor to put forth a vision of on-demand computing and the critical role that a flexible, componentized IT architecture has in keeping businesses competitive. Of late, IBM has somewhat backed off of the on-demand messaging and has instead shifted its visionary focus to a more generic commitment to innovation. Without delving too deep into the perils of marketing around IT services, it is sufficient to acknowledge that the promises of on demand are a bit behind schedule. There are a number of reasons why this is so, including customer reluctance, limited budgets for the transformation required, technological limitations, and the unwillingness of major software vendors to change their licensing models to subscription and pay as you go. Regardless, IBM has more clearly articulated where it is taking its customers than any other IT outsourcing vendor. With a firm view of the role that SOA will play in the enterprise, and with its Component Business Model (which at the simplest level breaks down business processes and thus applications into logical components), IBM is investing heavily to create repeatable assets to solve common customer problems. Unlike some of its competitors that rely too heavily on marketing alliances, IBM uses its own internal prowess in technology and services R&D to create true solutions and not just marketing "solutions."

SWOT Analysis

Table 16 lists IBM's strengths, weaknesses, opportunities, and threats in the U.S. AO market.

TABLE 16

SWOT Analysis of IBM

Strengths	Weaknesses
<ul style="list-style-type: none"> • IBM has unmatched scale in terms of size, capability, experience, and scope of services. • IBM has an unwavering commitment to global sourcing, not just as a source for low cost labor but also as a source of customer competitive differentiation. • The company has a broad range of transformational capabilities for nearly any type of IT environment. • IBM has a cohesive vision for how to transform customers to a componentized, flexible IT architecture. • IBM has large investments in services innovation and R&D. • IBM is far ahead in developing repeatable solutions utilizing both IP and IBM technologies to solve 	<ul style="list-style-type: none"> • IBM is highly leveraged in India and investing in other geographies, but is it at the cost of investments in automation to reduce labor content entirely? • IBM's infrastructure outsourcing business is experiencing weakness; it may drag other services down with it. • Many customers — rightly or wrongly — question IBM's commitment to technological neutrality, believing that the services business will push IBM products unnecessarily.

TABLE 16

SWOT Analysis of IBM	
common business problems.	
Opportunities	Threats
<ul style="list-style-type: none"> • The midmarket is nearly untapped and represents a major opportunity. • IBM's hosted applications business is still quite small, but has the potential to grow with proper investment. • Continued growth in IBM's BPO business can serve as pipeline for AO. 	<ul style="list-style-type: none"> • Indian vendors are threatening to move up the value chain from application maintenance into more strategic AO deals. • The growth of software as a service could potentially threaten the entire AO industry over the long term; vendors must adjust strategies over time as customers move to an on-demand model.

Source: IDC, 2006

IDC Leadership Grid Positioning

IBM is positioned in the Leadership quadrant of the IDC Leadership Grid for U.S. AO services. IBM and Accenture are the undisputed leaders in the U.S. AO services market and are far enough ahead of their competitors to stand in a class unto themselves.

Future Outlook

IBM leads the AO market in many ways beyond sheer size and market share. It arguably has made the largest relative commitment to global sourcing. It leads in services and technology innovation. It leads in developing SOA-based frameworks and componentized solutions. And it leads in overall scope and capability. It is not surprising, then, that all other vendors in the market are following IBM's lead on a variety of fronts and that all other competitors, whether they admit it or not, envy IBM's resources and continued ability to dominate the market. So where does such a clearly dominant vendor go from here? Obviously, IBM cannot rest on its laurels because there are hungry, nimble competitors — particularly Accenture — looking to usurp its lead in the AO market. We believe that the most important thing for IBM to do to maintain its lead is to continue investing in global sourcing and, more important, in services automation and innovation. As AO services increasingly become commoditized, it is becoming more important than ever to deliver those services in a profitable manner, which means with minimal labor content. Additionally, IBM will need to continue refining its vision of IT transformation. Though the on-demand vision has not been accepted as IBM had hoped, it still remains valid. In its currently more mature form, consisting of the Component Business Model, SOA, virtualized infrastructure, hosting, and SaaS, IBM has a clear road map of how to bring customers to a more dynamic and agile IT environment. AS IBM executes on that vision, IBM's competitors will have a hard time catching up.

IDC Leadership Grid for U.S. AO Services

The IDC Leadership Grid for U.S. AO Services represents IDC's opinion on which vendors are best positioned to gain market share over the next few years. Positioning in the upper right of the grid indicates a high potential to gain market share, and positioning in the lower left indicates low potential. Positioning on the x-axis reflects the vendor's current capabilities and menu of services and how well aligned it is to customer needs, with a position toward the right indicating better opportunity alignment. Positioning on the y-axis indicates where the vendor is investing to capture future opportunities and how adaptable the vendor is to changing market conditions.

Figure 2 shows the IDC Leadership Grid for U.S. AO Services. The leadership grid is divided into four quadrants. The quadrants are:

- ☒ **Leadership.** These are the vendors that have both the size and the momentum to be dominant forces in the U.S. AO market. They have a broad scope of capabilities and are best positioned to react well to current and future market trends and that we believe will continue to gain market share.
- ☒ **Leader Potential.** Vendors in the Leader Potential quadrant are on strong growth paths and are gaining market share. To become leaders, they need to broaden their capabilities and partnerships.
- ☒ **Niche.** Niche vendors tend to have significant market share and dominant capabilities in a few market segments or industries, but are not competitive in the entire AO market.
- ☒ **Needs Investment.** Vendors that need investment are ones that have the potential to gain significant market share, but are still limited in their scope of services, their capabilities, or their ability to execute. This often includes new entrants into the U.S. AO market. This quadrant can also include vendors that already have significant market share, but for one reason or another are faltering.

It should be noted that no vendors are in the lower-left, upper-left, or lower-right corners of the leadership grid. A vendor that had such low scores in one of both dimensions of this evaluation would naturally not be selected for inclusion in the study.

FIGURE 2

IDC Leadership Grid: U.S. Application Outsourcing Market, 2006



Source: IDC, 2006

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