



B2C Technology Story

Web Summary:

Outsourcing Services and ASPs

by Leon A. Enriquez

Reading Time:

7 minutes

Reader Benefit:

- ◆ Understanding the ASP software rental model;
- ◆ Insights about the ASP solutions;
- ◆ Would an ASP be the answer to your software application problem for your business operations?

What are Application Service Providers? Put simply, ASPs manage and distribute software-based services and solutions to customers across a wide area network from a central data centre. Software is rented on a Pay-Per-Use or fixed fee basis. Essentially, ASPs enable small- and medium-sized enterprises (SMEs) to outsource some or almost all aspects of their IT needs. Thus, ASPs may be commercial ventures that cater to customers, or not-for-profit or government organisations, providing service and support to a group of end-users.



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ASPs may be categorised into five sub-categories as follows:

1. Enterprise ASPs – deliver high-end business applications;
2. Local/Regional ASPs – supply wide variety of application services for smaller businesses in a local area;
3. Specialist ASPs – provide applications for a specific need, such as website services or human resources;
4. Vertical Market ASPs – provide support to a specific industry such as healthcare; and
5. Volume Business ASPs – supply general small- and medium-sized businesses with pre-packaged application services in volume.

With the advent of the ASP, the cycle of computing trends has come full circle. The outsourced Web-based shared resource business applications has brought us back to the bygone era of service bureaus and time-sharing.

Only now, the computer applications have changed – from payroll to ERP, CRM, Business Intelligence, Call Centre operations, etc. And the communications connection have changed from private-line dial-in to IP-based Internet, intranet and extranet access.

The main beneficiary of ASPs is the mid-tier segment of the market.

It is worthwhile to note that for small businesses, outsourcing business application software and computing services to an ASP is not always cost-effective. After all, the business applications in this market segment are few and simple.



Thus, the small business can improvise economically with a small LAN and a PC-based desktop and server environment – using the Web for wide area communication. However, the small business may usually outsource their website and e-mail operations to a hosting and Internet ASP.

The majority of large enterprises have already outsourced or are contemplating outsourcing internal IT operations to a trusted third-party and their Web applications to an ASP. Economics drives the ASP market.

Yet, application control, security and legacy data force the high-end segment enterprises to adopt a dedicated operations environment rather than a shared multi-company environment. The large enterprise will flourish, with demands for increased bandwidth, reduced response time and new Web-based transaction and/or database applications driving the upgrade of the desktop, local- and wide- area networks, and servers.

This leaves the mid-tier segment market. Most enterprises in this market cannot afford to outsource IT operations. In addition, this segment needs business-critical applications that exist in the large enterprise, such as ERP and CRM. These compelling factors make mid-tier companies the natural target market for the ASP.

Access to the ASP will be via the Web for extranet applications and a VPN (virtual private network) for intranet applications. Notice that in the world of ASPs, both personal computing and the enterprise will survive.

Small businesses will continue to rely more on services from suppliers, e.g., vendors, banks, accountants, etc. Such firms will use the Web as a business tool – rather than a communications tool. However, the main applications of small businesses will still be in-house on their premises on a local area network, server and PC.

The mid-tier segment, though outsourcing to an ASP, will change its operational characteristics. Such mid-sized companies will place less emphasis on IT operations and development, but more on business growth through the productive use of IT. Here, managing and monitoring the ASP's performance will replace operations and applications development.



The ASP business remains a realistic value-proposition – but practical adoption on a large scale will be a gradual process.

When the ASP idea first emerged about 1999/2000, most industry watchers predicted that the ASPs would become a big business. IDC predicted that the compound annual growth rate of ASPs to be 91 percent, going from zero in 1998 to US\$2 billion by 2003.

Unfortunately, the adoption rate has been slow thus causing the demise of many ASPs – all due to lack lustre demand and uptake of ASP services, and partly due to the business model.

Research analyst firms have indicated that ASP market estimates on a worldwide basis are accurate in the short-term, but not for the long-term. Considering just the mid-tier market segment – the target market for ASPs – is much larger overseas as compared to the U.S. As with all Web-based technological evolutions, the ASP business which started in the U.S., is expected by market analysts to become a booming business in Europe by 2003 and in Asia by 2005.

Going by the ASP take-up rate of the past two years, slower than expected corporate adoption has dampened rate of progress throughout the world. This is due in part to present, weak economic conditions. Yet, many expect that as the general world economy recovers, competitive market pressure will most likely witness an acceleration in ASP adoption. And many are keeping watch as the ASP model evolves further.

What seems clear is that although the ASPs are a natural evolution of the computing marketplace – but until the demand meet the deliverables with a nice critical mass, the ASP market will continue to underperform. No doubt, the surviving ASPs will be here to stay, and will serve the market well – as a more productive iteration of the old idea of service bureaus in the past.



Box Story 1:

ASPs – Facts You Need to Know

Let's briefly explore the benefits of the ASP model:

1. *Benefits:* To summarise, data security and reliability are two significant issues to consider when evaluating a hosted solution from an ASP.
2. *Rapid Deployment:* End-users can be installed and running in just a few minutes with Web-based hosted applications provided by an ASP. Assuming web browsers are in place, little additional work is usually required.
3. *No Software Ownership:* Unlike traditional client/server applications, there is virtually no software to own. Consequently, there can be a substantial reduction in software management tasks and related costs. Again, the hosted application is accessed over the Web with the ASP vendor hosting both the application and the database for a monthly per-user fee. This can reduce both software and system administration costs while providing clear cost of ownership data.
4. *Virtual Network:* Web-based hosted applications offer the ability to instantly network sales and marketing groups. By definition, these applications are accessed over the Internet or through a firm's own Intranet. For companies lacking network assets and other systems resources, this option offers a compelling reason to employ Web-based applications via ASPs.
5. *Reduced Management:* The ASP model can substantially reduce many of the tasks associated with maintaining traditional client/server applications. Generally, the application vendor will handle all system maintenance tasks, including backup and recovery, upgrades, network management, and user additions and deletions.
6. *Trade-Offs:* Depending upon your viewpoint, many of the benefits mentioned may also be viewed as some of the trade-offs. Three related and somewhat obvious trade-offs exist, namely, control, network dependence, and ownership.



Clearly, giving control to an ASP is a double-edged sword. Although an ASP will generally manage all systems-related tasks, loss of control and management oversight is assumed. You are trusting the ASP to follow good systems procedures for disaster recovery, user support, system upgrades, bug resolution, version control, and data security.

Network dependence is another trade-off. Unless the Web-based application can operate in a “disconnected mode”, i.e., not connected to the Internet or Intranet – then all users are dependent upon their connection to the network. This raises concerns about network reliability, privacy, uptime, and connection speeds.

Lastly, not owning the application could indeed be a trade-off for some firms. Ownership provides control, and control can provide comfort. By definition then, application hosting implies some loss of control. However, as the application hosting market matures, confidence and comfort levels will follow.

In the meantime, ask your ASP vendor to clearly document how they intend to address your concerns. In particular, what guarantees can be provided that your data will be secure and that the application will perform reliably over the Internet.

7. *Summary:* In short, look for service level agreements, documented disaster recovery procedures, data security statements and descriptions, scalability benchmarks and proven technical support. Just as important, ensure the ASP you are considering is financially fit – so that your data will not be held hostage in the event of a bankruptcy or other catastrophic failure.

Box Story 2:

Analyst’s Views on Outsourcing

According to Gartner Dataquest, as the IT services industry works through a difficult year 2002, the IT outsourcing industry will look to applications services to drive growth in 2003/4.

A November 2002 survey among 36 outsourcing vendors showed that offshore application management was ranked as the highest growth service opportunity for vendors in 2003, followed by near-shore application management. With the focus on lowest costs, there is a growing adoption of offshore outsourcing, primarily for applications, but also emerging is BPO (business process outsourcing) and IT infrastructure management.



Offshore outsourcing accelerated during the past year, and it will continue in the next two years as a means to offer alternative lower-cost labour. Gartner Dataquest analysts said services vendors will look for more partnering opportunities with offshore companies, as well as acquisitions.

“Already some of the larger services companies have responded to offshore players in the area of applications support by acquiring or setting up their own offshore delivery capabilities through acquisition or significant alliances with lesser-known players,” said Allie Young, chief analyst for Gartner Dataquest’s IT Services program.

The Gartner Dataquest report noted that while low-wage countries are attracting attention with application services, IT infrastructure outsourcing activity is hot on a grand scale around the world. As of year-end 2002, there were at least 14 mega-deals worth a total of US\$28.4 billion compared with nine mega-deals in 2001 worth a total of US\$15.1 billion. There are at least four pending mega-deals, worth an estimated total of US\$15.3 billion.

“Despite concerns that mega-deals in outsourcing were drying up, 2002 saw an above-average number of contracts worth US\$1 billion or more,” said Bruce Caldwell principal analyst for Gartner Dataquest’s IT Services program. “We’ve seen ample evidence that the 10-year deal is no longer the standard, and that multibillion dollar contracts, as well as consortia or alliances of vendors are increasingly common.”

As of year-end 2002, IBM had won seven of the 14 mega-deals awarded in 2002, and shared an eighth deal with Keane. CSC has won one and EDS won two deals, but both were in final discussions for several, separate mega-deals. HP and Fujitsu landed their first mega-deal, and CGI landed its third.

Gartner Dataquest’s review of the past 12 years of mega-deals indicates that EDS and CSC were clear early leaders in this field – but IBM quickly surpassed them, and now has a total of at least 32, which is quite close to both EDS (21) and CSC (15) combined.



About the Author

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