

## TAKING UP SERPENTS: HOW ASPS ARE CHANGING THE FACE OF CONSULTING



*"Asps. Very dangerous. You go first."*

—George Lucas, Philip Kaufman, and  
Lawrence Kasdan, *Raiders of the Lost Ark*

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### About the Author:

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The almost ubiquitous connection of organizations to the Internet has created a new business: Application Service Providers (ASPs). ASPs offer access to the same sort of high-end computer software that has been available for years—accounting, human resource systems, enterprise resource planning, etc.—but with a twist. ASP customers don't install anything; they just access a copy of the software over the Net. This new model threatens the business models of resellers, software vendors, consultants, and other businesses involved in the creation and delivery of software. How should these threatened companies respond?

### Snake in the Garden

Once, buying a new piece of industrial-grade software was a big deal. A delivery truck would drive to your site, and deliver large packing crates loaded with spools of magnetic tape. Highly paid specialists would load, install, and configure the software for your system; this process could take days or weeks, and your system might be unavailable while it was happening. Finally, your employees would need to undergo lengthy (and again expensive) training to use the new system.

Things have changed a lot. Today, software comes on CD-ROMs, not magnetic tape. Well . . . maybe things aren't so different. But ASPs could change software

enormously. Software runs on machines owned by the ASP, in a centrally managed facility; clients access the functionality of the software over the Internet. ASPs offer the promise that buying software can be as fast and easy as ordering pay-per-view, and will come at a much cheaper price than buying it the old way.

The advantages of ASPs are obvious. Clients are insulated from buying, installing, and managing hardware; they never need to upgrade or patch software; they don't need to hire system administrators to perform the often extremely complicated job of software, system, and network management. ASP specialization and economy of scale let them offer software at savings—some say significant savings—over the price of installing and owning it yourself. The advantages aren't just in cost and saved headaches, though: running software is the ASP's core competency, and probably isn't the client's. The ASP offers better software service, more rapid deployment, more flexibility, and access to newer technologies than the client is likely to offer on its own.

The disadvantages of an ASP may not be so obvious but are equally compelling. With an ASP, your critical business functions are now dependent on a functioning Net connection. Important data is out of your control, and in the hands of a company that could make enormous profits reselling it. ASPs offer a limited selection of software, and the packages they do offer are rarely customized.

These advantages and concerns play out differently for different target customers. Companies that only have a handful of employees don't need—and more importantly can't afford—powerful back-office functionality like enterprise resource planning (ERP) software, human resources and financial packages, or customer relationship management (CRM). In contrast, large companies have such specific needs and demands, and the resources to meet them, that standardized solutions hold little appeal. In between, in the middle market, growing companies are beginning to struggle with the complexities of managing a business, need immediate access to sophisticated software, but are realizing that systems management isn't a core competency. For these companies, the benefits of ASPs outweigh the concerns.

Are consulting companies scared? They should be. This is a classic instance of a disruptive technology, as described in Harvard Business School Professor Clayton M. Christensen's book, *The Innovator's Dilemma*. ASPs offer a service that is by many traditional measures—selection, customization, security—inferior to large customized implementations. And yet the ASPs—by lowering price and expertise barriers—make enterprise software products available to the middle market, for which they were previously out of reach. If the ASP market follows the historic pattern described by Professor Christensen's analysis, the sophistication of these disruptive technologies will increase, convincing higher and higher-end customers to switch, until IT consulting companies no longer have a viable customer base. As ASPs learn how to customize

What does a consulting firm get out of allying itself with an ASP? CGEY has partnered with ASP Corio. This way, Corio is able to work with a reliable partner, one with marketing muscle and powerful client relationships. The B2B Net marketplace provides an opportunity for such an alliance. An ASP-consulting alliance can offer services to initial participants in a Net market, and subsequently to each new company that wants to participate.

article abstract

applications without losing their economy of scale, there will be less system implementation and system integration work for traditional IT consulting companies. That might sound good to ASPs, but consulting companies—who have read Christensen—aren't resting on their hands.

#### **The Coming ASP Shakeout**

*[to an asp] "With thy sharp teeth this knot intricate of life at once untie."*

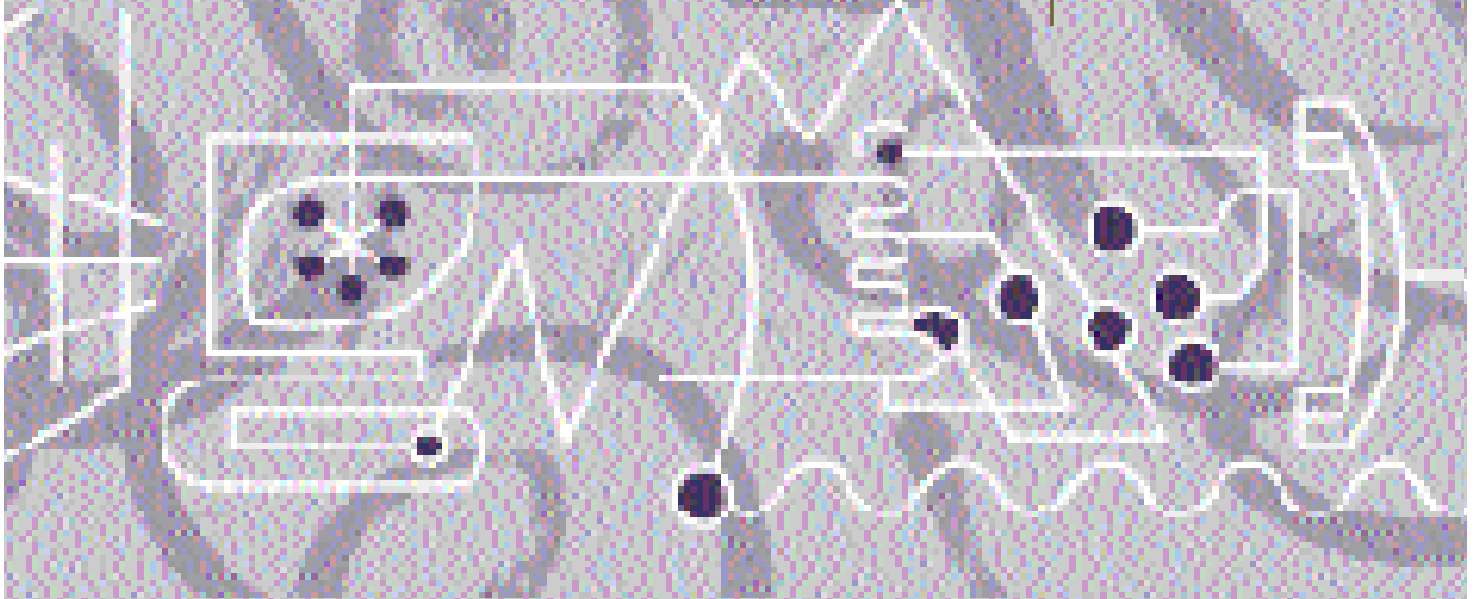
—William Shakespeare,  
*Antony and Cleopatra*, Act V, Scene II

Dataquest estimates the size of the ASP market in 2004 to be \$25 billion, a huge leap when you consider the estimated \$3.5 billion for 2000. That astonishingly high growth rate will surely be big enough to sustain any number of players. And yet there are as many as 600 companies claiming to offer some sort of ASP service, including telecom companies, software vendors, consultants, hardware vendors, and pure-play startups. Not all of these will be able to survive. A shakeout has started already, and isn't merely confined to poorly funded garage startups. Pandesic, a very high-profile ASP created as a joint venture between tech giants Intel and SAP, closed its doors in August of 2000. They likely won't be the last: GartnerGroup expects more than half of today's ASPs will shut down or be acquired before the end of 2001. Like most technology markets, pressures of competitive advantage, a limited supply of press attention and brand recognition, and network effects will continue to drive all but the top players out of the game.

The winners, however, stand to be major players in a multibillion dollar industry.

The driving strategy question for ASPs and consulting companies is how to survive the coming shakeout. Those ASPs that win, believes CGEY Group Managing Director Terry Ozan, will be the ones that distinguish themselves by offering a mature, integrated business solution. In his keynote address at the ASP World Conference 2000, Ozan categorized ASPs into three stages of sophistication. The first stage includes providers of generic, standalone packaged software. Second-stage ASPs provide multiple integrated packages, such as ERP or CRM, that require a good deal more technological and business process sophistication. Finally, third stage ASPs must move beyond offering just a technology solution, and help clients transform their business, offering a wide range of process, application, and strategic advice. Especially for high-growth midsize companies (those that need rapid development of capabilities), this transformation partner role will be a necessary service.

Already, ASPs struggle up the ladder; most position themselves as providing "Full Service," "Total Service," or "Business Services" rather than merely applications, and back those marketing slogans by offering strategy consulting, branding, customization, and more general IT consulting services. But few companies, whether small startups or large consulting firms, can truly offer the breadth of capability necessary to meet all of the application needs of rapidly growing clients.



### Building the Alliance

*"And these signs shall follow them that believe: they shall speak with new tongues; they shall take up serpents; they shall lay hands on the sick, and they shall recover."*

—Mark 16:17-1

There are three general strategies a consultant can use to provide a complete solution to clients, explains CGEY vice president Craig Johnson. You can build all of the capabilities yourself, you can tailor customer-specific best-of-breed solutions for each new client, or you can pick your partners and go to market with a steady alliance. While each has advantages and disadvantages, Johnson believes that alliances will emerge as the winning strategy for offering application services.

In March of 2000, CGEY established an alliance with Corio, a major player in the ASP market backed by venture capital wizards Kleiner Perkins Caufield & Byers. CGEY agreed to recommend Corio to clients as the preferred application server for most business applications; in return, Corio handed over an equity stake and agreed to send back-end system integration work to CGEY.

It's simply too difficult, expensive, and time-consuming to build or acquire an all-encompassing application service in just one company. New market demands emerge quickly, software platforms evolve at break-neck speed, and the necessary skills cover everything from application development and hardware management to strategic consulting and back-room legacy

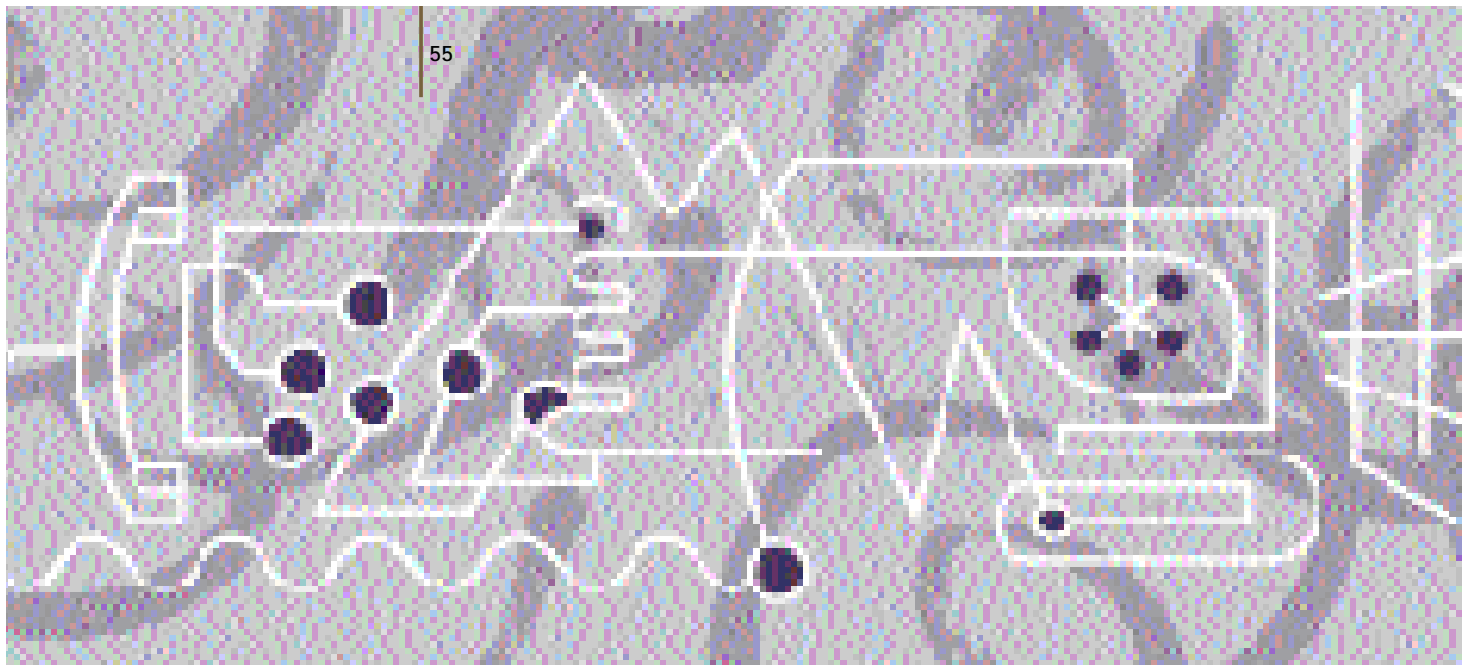
implementation. No one organization—not even large global consulting houses like CGEY—could sustain leadership in every necessary field.

Tailored best-of-breed solutions, in contrast, seem like a powerful offer. For each client, this strategy offers a customized solution including the best providers for software, application development, application management, hardware hosting, network architecture, system implementation, and so on. Sounds compelling, until the client realizes that these vendors may never have worked with each other before, that the methodologies may be incompatible, and that the client might have to wait while the vendors painstakingly climb the learning curve.

ASP-consulting alliances are the happy medium between these extremes. From the vendor's point of view, it works with reliable partners that it's worked with before, and alliances have the marketing advantage of pointing to previous engagements with the same team. The clients perceive lower risk and faster delivery. CGEY will let Corio be the ASP, a field in which Corio has already established itself as a leader, while CGEY delivers what it does best: system integration, operations, and consulting.

### Going to Market

The B2B Net market sector provides a golden opportunity for such an alliance. Marketplaces generally run a software platform from a vendor such as Ariba or CommerceOne to perform the matching of buyers and suppliers. While participants can access the market-



place through a standard browser, the real efficiency gains of Net markets only take effect once companies more closely integrate their own back-end software with the market. This means not only that they need access to standard "buy-side" or "sell-side" software packages, but need customized implementations bridging these software packages to their own systems such as ERP, databases, workflow, and procurement management. ASPs are ideal delivery channels for standard software like buy-side e-commerce software, but complicated back-end integration requires the services of a larger IT consulting company. Once a Net market is established, and participants decide on the technical and software standards, the ASP-consulting alliance can offer its services to each new company that wishes to participate in the Net market.

Enporion, a Net market for the energy and gas sector, was a major win for the Corio-CGEY alliance. Established in the summer of 2000, the Net market runs CommerceOne, hosted by Corio, and uses SAP, a popular ERP system, on the client side. This arrangement creates opportunities for CGEY to perform back-end system integration not only in each of the founding participants, but in other suppliers and buyers that eventually join the marketplace. Not coincidentally, this gives CGEY a large incentive in the future success of the market, an arrangement that undoubtedly sits well with the management of Enporion.

CGEY intends on repeating this strategy with other B2B exchanges. ASP-hosted software will be a key enabler for new buyers and sellers to join the exchange, but in the long run not sufficient. As such exchanges become more sophisticated, integrating with more of the participants' back-end services such as fulfillment, credit, staffing, and new product development, the implementation services of companies like CGEY will become more and more a critical factor for a new participant joining the exchange successfully.

#### The Future

Business models for ASPs will undoubtedly continue to evolve and change. Networked application hosting will take its place as one element in a broader range of services. Application management covers the entire life cycle of providing software to a client: strategic advice, architectural development, business process development, implementation, maintenance, and, yes, hosting. As the story plays out, some capabilities will emerge as critical for success; others may not fare so well. And although it's impossible to know for sure which models will succeed in the future, Johnson is comfortable with CGEY's strategy. "We're getting revenue in the short term. In the long term, we'll be identified as a leader."