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BrainTrust Query: Is the ASP Model for IT Services Inevitable?

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By [Bill Bittner](#), President, BWH Consulting

As I sat in the NRF's CIO Innovator's Panel discussion at the Big Show in New York City, I was struck by the dichotomy. Two long-term IT users from the supermarket channel (Price Chopper and Raley's) were teamed with a specialty retailer (Charlotte Russe) that focuses on young women's clothing. The discussion was driven by an AMR survey which asked 127 retailers to categorize their IT expenses. The study tried to normalize the results by using clear definitions of what costs should be included in each line item and adjusting the numbers where necessary to make responses comparable.

As the discussion went on, the disparities between the channels became more distinct. When the supermarket execs, Dick Bauer, CIO of Price Chopper and Eric Wilson, CIO of Raley's, discussed the challenges of maintaining their infrastructure and the significant portion of their budget it represented, the specialty retailer, Ed Wong, EVP of Charlotte Russe, did not really find it a problem because they outsourced the whole effort. As the supermarket retailers discussed the challenges in finding good development talent, the specialty retailer said they did not really have a lot of developers because they bought packages, avoided modifications and used third party vendors on a project basis to integrate them.

I know it is a little like comparing an elephant to a mouse. They're both mammals, but that's about where the similarities end. Supermarkets and specialty retailers are at both ends of the retail spectrum, but maybe there is something to be learned from both their approaches to IT.

The old argument for avoiding the application service provider (ASP) model has been that business managers are afraid to give up control of their data to an outside data bank. This argument simply no longer makes sense. New managers use online services to do all their personal banking. They use SalesForce.Com to manage one of their most valuable assets (contacts and leads). The next generation of managers have their whole personal lives exposed to the world on MySpace.com or Facebook.com. These people are not going to be afraid to have their business data stored somewhere outside the four walls of their business.

One of the challenges for the supermarket CIOs was finding good developers. Whenever I hear anyone say they can't find people to do a job, my first reaction is that they are not paying enough. This got me thinking about how I would feel graduating with a computer science degree today. These graduates are faced with a very challenging decision -- whether they want to go to work with a network based solution provider like Google, with their email, spreadsheet, and word processing applications all available through a browser, or go to work for the IT department of a retail business. Let me see -- Google, with stock options potentially worth millions, dog care in the office, free gourmet cafeteria, etc. -- or Retailer X, where the net profit margin is two percent and IT is regarded as an expense department within a company whose business culture is entirely different. It is kind of like asking a mechanical engineer to work in the motor pool. (But then we have already outsourced the motor pool, so it is like asking them to become a mechanic.)

Discussion Question: As the technical barriers continue to crumble and society becomes more comfortable with putting their data on outside data banks, does the application service provide (ASP) model become inevitable?

I think the writing is on the wall for the in-house IT department. As technical improvements in the network continue to increase reliability and speed, there is no need for local data storage. As "Digital Rights Management" techniques continue to improve for protecting movies and music served online, those same techniques will be applied to protect proprietary business data. Finally, the ability for network based solution providers to offer such huge rewards for working with them means they will continue to be able to steal talent from the non-network based businesses.

IT services are likely to become an oligopoly, with a few big providers offering their services online and local technicians doing the implementations and maintenance for business consumers. This will take quite a while as new technology and user training must permeate the business landscape. The transition will be challenging for the retail CIOs who have to keep the old stuff running while they watch the role of their department change from designers to implementers. It is particularly challenging when you consider that "getting rid of their department" may be the best thing they can do for their organization. They are going to have to deal with the personal and personnel issues associated with their drastically changing role.

The other challenge will be for society, as a whole lot of computer science engineers become redundant.

- [CIO Innovators Forum - National Retail Federation](#)
- [CIO Innovators Panel \(PowerPoint presentation\) - National Retail Federation](#)

Comments

Very simple math proves Bill Bittner's prognosis. Retailing is growing at single digit rates, while Asian outsourcing is growing at double digit rates. More and more, retailer IT departments are responsible for strategy and purchasing of packages and services. Implementation and daily operations are getting automated or being outsourced. The fastest growing technology firms aren't hardware, software, communications or consulting providers. They're Asian outsourcers like Wipro, Cognizant, Tata, and Satyam. And they don't just run telephone call centers. They're the systems department.

Mark Lilien, Consultant, Retail Technology Group - Braintrust Panelist

Microsoft's Bill Gates projected the ASP approach as the future about 4 years ago. A decision of this size is never simple. For some reason, every retailer thinks they are different, when in fact most are different in name only. All too often package software is purchased, highly customized and then does not stand the test of time. With the ASP approach, updates are easy and everyone benefits at a fraction of the on-site cost. Over the next 5 years I expect ASP to greatly increase in market share. Company financials and operations will move to ASP. Customer marketing (data base) etc., will remain with the company's IT department.

W. Frank Dell II, CMC, President, Dellmart & Company - Braintrust Panelist

The ASP model is not only the wave of the future but in most cases, it is the only future. As Bill so aptly stated, where is the bright young creative programmer going to go to work, given a chance? With the War for Talent heating up, those bright creative people are going to go where they see opportunity to learn new skills, work on neat stuff, and increase their value as a saleable commodity in today's every changing employment market.

As retail is a world of buying and selling and we are always looking to buy the best product for the best price, to offer to our customers the best value. IT should be doing the same thing for their customers and that means making a true comparison of what will continually deliver the best product for the money on an ongoing bases.

Just look at some of the benefits of an ASP Model.

- Shared development--conserve resources and take advantage of "best in class"
- Consistent approach, but one that offers management controls that could be defined to meet the business needs of the organization
- Continuous enhancement
- Designed with key architectural priorities
- End-user response time
- Security
- Reliability and Availability
- Throughput and Scalability

All of the reasons listed above--and more--make the future one where ASP and those who adopt it are the winners.

Mel Kleiman, President, Humetrics, LP, a division of Deploy Solutions - Braintrust Panelist

I don't hear the data argument for ASP anymore. What I hear is a power struggle. Business leads go out and find an ASP or SaaS provider for something they desperately want because they can't get it on the priority list for their IT department. Then IT gets wind and tries to shut it down. Why? Because if the business lead gets their SaaS project, then IT won't have "control" of it.

The irony is, these IT departments are so slammed with just the basics that they can't be a strategic partner to the business. If they would just give up the basics, they would have that time to be a strategic partner. And you know what? That's a much more powerful position within the company.

Nikki Baird, Senior Analyst, Forrester Research

The issue of confidentiality of a grocery retailer's data will be addressed once the grocers understand that they can now utilize all of the data that they have been collecting on consumers and transactions. This data has not been fully utilized by any retailer due to cost, manpower resources etc. Efficient outsourcing will allow marketing people to develop critical outputs and reports that will give them better insight into their shoppers and transactions and more importantly, use the information to better brand their business and market to their customers. Who will lead in this endeavor?

J Peter Deeb, Partner, Deeb MacDonald & Associates, L.L.C. - Braintrust Panelist

More firms are using the term "Software as a Service" (SaaS) to describe what used to be called the ASP model. This is a viable alternative for many retailers and is being beneficially applied as we speak by dozens of firms in at least two areas I am familiar with: price optimization and e-commerce.

Comparing this with the outsourcing of IT departments to Asia is not quite accurate. SaaS software providers host essential business applications on their servers, where they are responsible for functionality, security and software updates. Client businesses port their internal systems to the SaaS applications using a secure communications link. From the end user's perspective, the application behaves as if it is on the local server.

The SaaS arrangement poses several advantages to retailers. Since the software host bears the burden of maintaining state-of-the-art servers, there is no in-house hardware to purchase, maintain, replace or depreciate. Software development and updates are handled entirely by the host. Costs are variable, not fixed. IT head counts are reduced or applied to other objectives.

The old objections die hard, however. Retailers worry about hosting essential data off premises, even if the security measures applied by the software provider are vastly superior to those in-house. There may be some turf issues. And of course, the reliability and continuity of the hosted application must be absolutely assured.

If you use online banking for your personal accounts, or if you maintain an email distribution list using one of the many fine browser-based services presently available, you already may appreciate the benefits of SaaS.

James Tenser, Principal, VSN Strategies - Braintrust Panelist

Working on various sides of the issue, I have always viewed IT outsourcing as inevitable. The argument that information is such a valuable asset that it needs to be managed by the organization is full of holes. Information management will continue to mature to the banking model.

The asset (money--an arguable important asset) is at the bank. Experts efficiently manage the asset. Companies choose their bank to manage their asset based on cost, performance and fit.

Individuals who are good at working with the asset work at banks. Those individuals are rewarded for their performance because they are a profit center for the bank, not a cost. Banks compete for the best talent to keep ahead of the competition which creates a higher bar and pull for the best and brightest in the field (leaving the less qualified to work elsewhere).

Banks compete for business which requires them to stay current in their field, stay current with their infrastructure, operate efficiently and hire the best. That leads to highly efficient banking.

The companies who employ banks get the best talent and resources applied to their banking needs in the most cost-effective manner. If they don't, they move their business to another bank.

Replacing bank with techbank and you have a pretty clear view of the future of IT.

John Hennessy, VP Sales and Marketing, Concept Shopping, Inc. - Braintrust Panelist

I contacted my business partner, Chris Moschovitis (christos@tmg-emedial.com) for help in answering this question. CEO of tmge*media, Chris consults with companies at the highest level to determine the best models and strategic fit for technology. Here's what he had to say:

"It is true--the old model of being afraid to give up your data to an outside facility no longer makes sense. That said, completely relinquishing application control does not make sense either. There are many valid reasons ranging from the old: data security and availability, to the new: business process control (affected by ASP versioning) and compliance (affected by legislation, audits, etc.). Like all things, there are no black-and-white solutions for IT. One size will never fit all, and it shouldn't. The ASP model makes sense for certain types of applications and certain types of businesses, and it should be part of a healthy, well balanced diet."

Anna Murray, President, e*media division - Braintrust Panelist

The trend towards Software-as-a-Service (SaaS), or what has evolved from the ASP model of years past, is inevitable, but any industry-wide change of this sort does not happen over night--there are vested interests in the old way of deploying information technology. Enterprise software giants have huge businesses deploying their products behind the customer's firewall, and they will be cautious at best in pursuing any potential threat to that business. Internal IT can also be a proponent of outdated deployment models as has been mentioned. So where you see SaaS taking off is in areas of innovation such as price optimization, retailer-vendor deal management, and others where there aren't compelling offerings from vendors with both feet planted in the past. In those cases, retailers realize they can get best-in-class functionality for a lower total cost of ownership, and, if the vendor is good, at less risk and with (ironically) greater control over the success of the deployment.

Mitch Kristofferson, VP, Marketing, DemandTec, Inc. - Braintrust Panelist

"SaaS"/Packaged apps may be good, implementable out of the box and cheaper due to development costs shared between user companies but they don't give any of the user companies a competitive edge.

The competitive edge can only be derived by a self-owned system, whether it be developed and maintained by internal IT or an outsourcer. The search for the competitive edge is what drives progress.

'keentoknow'

I have been espousing the outsourcing of any non-core functions in retailing for years.

When I say outsourcing, I am NOT talking about programming functions. I refer to day-to-day functions that are more of a distraction and a burden than of value (like hiring data center managers, worrying about back ups and redundancy, making sure that payroll checks are printed, etc.).

My rule has been simple. The core business functions of retailers are to buy and sell stuff. Everything else is a distraction from the main focus. As to the costs of outsourcing, including the ASP model - if one were to do a true activity-based costing (ABC) analysis of what it costs to run these functions in-house - including the larger size building you need to lease just to house all these people - I guarantee that one would find that it is no more expensive to outsource than to run in-house. This does not even take into consideration the intangible but real "distraction" factor.

The hardest companies to convince are those that have made huge investments in infrastructure over the last 10-40 years. Newer retail ventures don't waste too much time thinking about this issue.

Robert Amster, Principal, Retail Technology Group

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