

Take the pounds off

– the hosting guide to commercial fitness

Introduction

Hosting is bound to cost more than in-house. After all, Port@I have their overheads and a margin to add on; a popular, logical and intuitive notion, but a wrong one never the less.

The main reasons that organisations adopt hosting are to allow that organisation to retain ownership of the operation and benefit from hosting’s speed to market, flexibility, guaranteed delivery and ability to mitigate some of the weightier risks. Notwithstanding this, it is natural to want to assess hosting’s cost effectiveness. The difficulty is that most organisations do not know the in-house component costs of the delivery of a workstation, and fewer still understand the true cost of delivery.

Overwhelmed by trying to work out the real costs of delivery in a world that seldom stays constant (reorganisations, growth, product launches, seasonality, offshore capacity, delays, channel strategy to name but a few), the norm is for organisations to focus on a “like for like” scenario via a simplistic spreadsheet.

In this world of the spreadsheet our notional building is of course full over the entire term. And after some internal partially successful detective work into the component costs the cost per workstation per month is calculated.

In the process of creating this neat, boxed-off scenario much of the value of hosting is removed. Flexibility, risk mitigation and the actual delivery of the workstation to service level are all sidelined for separate consideration. There is normally acknowledgement that hosting is probably a more efficient delivery vehicle and so offsets at least in part the Port@I margin and overhead. And therefore, after much deliberation, one finally arrives at the not surprising answer that the in-house and hosted models are comparable in terms of cost.

It is entirely forgotten that the convenient scenario just created actually represents not only the best case for the in-house cost appraisal, but the worst case scenario for hosting.

Hosting has been developed to deal with the real world, a world of change and uncertainty, a world of the inconvenient, the imponderable and the unforeseen.

This case study details financial analysis of Powergen and a top five world bank. It does so by considering the real experiences of these two organisations and comparing the cost of delivery using Port@I with what it would have cost via the traditional lease route. This we would contest is a more valuable like for like comparison.

“Not only has the hosted solution enabled us to make changes to the business that simply would not have been feasible in the timescales involved but it has been undeniably highly cost effective. And that before the we attach pounds and pence to the considerable value Port@I has added through their expertise and responsiveness”.



port@I

Leaders in Occupier Solutions



PART 1

Powergen

Context

The Gas and Electricity markets in the UK were deregulated in the '90s. Up until that time customers were captive to the local electricity and gas supplier. Deregulation opened the market up not only to existing players in other regions but to new market entrants from both the UK and abroad. Everyone's customers were the target of the competition and the scene was set for a battle in which only the fittest would survive. This period represented unprecedented turmoil in the Utility market.

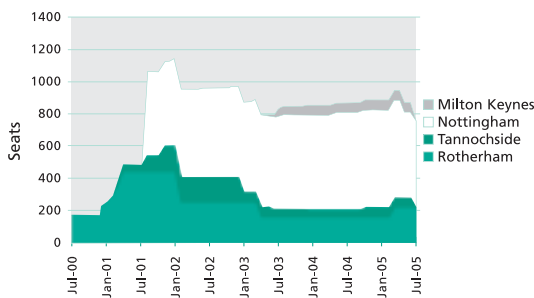
Powergen background

Powergen was formed from the power generation arm of the old Central Electricity Generating Board when the industry was privatized in the early '90s. Since then Powergen has expanded considerably by acquiring East Midlands Electricity, TXU, Midlands Electricity and others. In 2001 Powergen was itself bought by major European energy company E.ON. As is now common in this industry, Powergen also sell Gas and telephone products. Powergen was one of the first energy companies in the UK to take the logical step of combining gas and electric bills where customers take both services.

Hosting

Powergen realised that full-scale outsourcing of customer acquisition activity was not the answer and established a centre of excellence at Port@l's Rotherham facility in July of 2000. Since that time Port@l has worked with Powergen to deliver capacity out of its Glasgow facility, built a bespoke 600-seat centre in just 10 months, and opened and closed a centre in Milton Keynes. Over the period the numbers have swelled from an initial 175 in Rotherham to 1,150 at peak to 800 today, going through various ups and downs in between. The detail of these changes is depicted below.

Capacity Utilisation



Period under consideration

01 July 2000 to 31 July 2005.

Cost comparison

The subsequent paragraphs draw out the impact of the changes in seat numbers on the hosted and in-house costs over the period under consideration. The costs used for the in-house option are based upon the Port@l sites that the operations have occupied and are therefore absolutely accurate and directly comparable with hosting. Both hosting and in-house costs use the same constituent parts at the same basic cost e.g. in

terms of rent, the cost of a PC etc. The hosting pricing quoted is inclusive of set-up costs, margin and overhead. Stand alone projects (e.g. expansion of the comms room on one of the sites), moves and changes have been omitted from both models on the basis that these are common to both solutions and likely to be of minimal consequence anyway.

With the in-house costs, where the depreciation term is longer than the period of occupation to date, as long as that occupation is ongoing as of Jul 05, only that part of the depreciation that falls within the period under consideration is included. However, where a site has been exited, as in the case of Milton Keynes, the full costs of the fit-out and technology investments have been included.

Property related

As can be seen, the delivery of capacity has involved 4 premises in total. Because of the different properties, start times and durations of the requirements each has been governed by a separate contract. In all cases Port@l has taken responsibility for the residual space and lease commitments, which has allowed Powergen not only to flex the seat numbers (up & down) but also to make a clean i.e. zero cost exit, from premises.

In contrast had the capacity been procured through traditional means it would have involved 4 leases and in due course exit costs (dilapidations and legal fees). Considering the blue chip nature of the organisation, it is highly unlikely that terms of less than 5 years would have been obtained and of course each property would have had to be able to accommodate the peak requirement of that operation as summarised in the table below.

Location	Term (years)	Period included in cost calculation	Peak sq.ft. (gross)
Milton Keynes	7	7 ¹	4,790
Nottingham	5	Aug 01 - Jul 05	52,000
Glasgow	5	Jan 01 - Jul 05	16,250
Rotherham	5	Jul 00 - Jul 05	35,000

As with the space requirement, expenditure on fit-out in the in-house model would need to be made for the peak requirement. In contrast, the hosted model allows (within the bounds of the contract) the client to pay only for what is being used.

Had Powergen used traditional methods to provide for their capacity requirements then the property related costs alone would have been as follows:

"This case study speaks for itself. We have used Port@l on several occasions because the speed to market, flexibility and compatible term of engagement that they bring to the table. This in fact demonstrates in no uncertain terms the value that they bring in terms of cost too".

¹ All 7 years are included because of occupation of the site being terminated

Location	Capital investment	Rent/rates/service charger over period	Total
Milton Keynes	£493,818	£1,398,852	£1,890,672
Nottingham	£3,558,996	£7,110,000	£10,668,996
Glasgow	£988,610	£1,080,300	£2,068,910
Rotherham	£2,624,934	£5,908,300	£8,533,130
		TOTAL	£23,163,706

Technology

The types of workstation that have been delivered vary markedly from back office to fully blended, and indeed have changed considerably over the period. Whilst Port@l charges different amounts for seats of different functionality, clients are largely protected from the full quantum of the investment in the various technologies. This is because Port@l takes the view for example that the cost of the central technology such as the switch can be shared or dialler licences redeployed for use by other clients. This is in stark contrast to the in-house model in which once purchased the business is saddled with the cost (initial investment plus annual manufacturer's support) whether or not the equipment is being utilised.

Had Powergen gone the traditional route the total technology costs would have been:

Location	Capital investment	Manufacturer's support over period	Total
Milton Keynes	£409,500	£1,038,500	£1,448,000
Nottingham ²	£0	£0	£0
Glasgow	£1,421,000	£1,253,000	£2,674,000
Rotherham	£3,356,500	£1,529,500	£4,886,000
		TOTAL	£9,008,000

Services

Even though we know that we deliver services (facilities management, reception, security and IT managed service) at 30-40% less cost than in-house, this is harder to justify and therefore for the purposes of this comparison we have assumed a cost neutral position.

Overall

Model	Total workstation months delivered	Total cost Jul 00 to Jul 05	Effective cost per workstation per month
In-house	51,162	£32,171,706	£620.82
Hosting	51,162	£23,036,000	£450.26

Summary

1. Most organisations would not, given the time constraints, have been able to deliver the range of capacity solutions at all
2. The true like for like costs show that the in-house cost in this case have been 40% more than the hosting solution
3. Hosting has enabled Powergen to adapt to market and business changes much more quickly and cost effectively than would otherwise have been the case. Not only has this saved significant costs but adds a considerable value component to the solution

PART 2

Top 5 world bank

Context

City expectations place an onerous mantle on results. In the cutthroat world of financial services mergers, acquisitions, product development, FSA regulation, interest rate decisions, consumer confidence and government policy all make for a volatile environment. Speed to market, adaptability and a keen eye for an opportunity are essential in creating daylight from the competition.

Bank background

A recent acquisition gave rise to an opportunity where a new product could be launched using the brand of the acquired company and the execution capability of the acquirer. However, as with most large organisations size often equates to inertia and missed opportunity. On occasions this can be overcome by adopting innovative solutions.

As the market opportunity developed, the Bank realised that it had no spare capacity in the right locations to accommodate the new operation. The Bank recognised that despite all the property they owned and the enormity of resources at their disposal that their traditional delivery mechanism would not deliver a capacity solution within the 3-month timeframe that had been stipulated. Had time not been such a crucial factor the normal solution would have been to sign a lease on a new facility.

At the time of launch the plan was to start with 200 seats and grow to approximately 400 seats over approximately 2-3 years. In other words the size of facility sought would have been of the order of 32,000 sq.ft. (based on 80 sq.ft. gross per workstation).

² At Nottingham Port@l delivers a diluted hosting solution in which Powergen has assumed responsibility for technology

Hosting

Within 9 weeks of contract sign off on a 2-year term, Port@l had delivered the 200-seat new centre to the Bank, including a bespoke and discrete comms room. The Bank's aspiration at that time was that its operations would grow to fill the site and that the Bank would potentially take the site from Port@l in due course. Indeed it was only a matter of weeks after the operation went live that the Bank approached Port@l to grow its base by 75 seats. In fact this growth never did happen and a slowing of the economy sent the operation into reverse. Space became available in one of the Bank's other facilities in the area and a decision was taken to relocate the operation to avoid incurring double infrastructure costs.

Period under consideration

The 2 years of the contract.

Cost comparison

The subsequent paragraphs compare how an in-house solution with hosting in terms of the costs incurred. The costs used for the in-house option are identical to the Port@l site concerned and are therefore both accurate and directly comparable. Both hosting and in-house models use the same constituent parts at the same basic cost e.g. in terms of rent, the cost of a desk etc. The hosting pricing quoted is inclusive of set-up costs, margin and overhead and, in this case, VAT³. Stand alone projects, moves and changes have been omitted from both models on the basis that these are common to both solutions and likely to be of minimal consequence anyway.

Considering the in-house scenario, the entire cost for technology and fit out have been included because the exit after 2 years was less than any of the depreciation periods.

Property related

The hosting model is very straightforward. The Bank just paid for its contractual obligations, 201 seats over 24 months with Port@l taking responsibility for the residual space, lease and investment commitments. Not only did this give the Bank the ability to flex the seat numbers (up & down) but also to make a clean exit (i.e. zero cost) from the premises at the end of the term.

In contrast, had the Bank gone the traditional route and taken a lease then this would probably have been for 32,000 sq.ft. on a term of no less than 5 years.

In contrast with the space requirement, we have assumed that expenditure on fit-out in the in-house model would only have taken place just prior to expansion and therefore we have limited expenditure to the first 201 seat.

Location	Capital investment	Rent/rates/ser vice charger over period	Total
Glasgow	£1,370,418	£3,323,700	£4,694,118

Technology

The hosting solution largely protects clients from the full quantum of the investment in technology. This is because Port@l takes the view that the cost for example of the central technology such as switch can be shared or dialler licences redeployed for use by other clients. This is in stark contrast to the in-house model in which once purchased the business is saddled with the cost (initial investment plus annual manufacturer's support) whether or not the equipment is being utilised.

Had the Bank used traditional methods to procure capacity then the total cost of technology would have been:

Location	Capital investment	Manufacturer's support over period	Total
Glasgow	£393,960	£756,280	£1,150,240

Services

Even though we know that we deliver services (facilities management, reception, security and IT managed service) at 30-40% less cost than in-house, this is harder to justify and therefore for the purposes of this comparison we have assumed a neutral impact.

Overall

Model	Total workstation months delivered	Total cost Aug 04 -Jul 06	Effective cost per workstation per month
In-house	£4,824	£5,844,358	£1,211
Hosting	£4,824	£2,120,920	£440

Summary

1. A traditional property lease would not have given the Bank such a pain free route to restructure its capacity
2. The normal in-house route would have cost 176% more than the hosting solution
3. Hosting delivered on time, delivered over time, and delivered this time a solution that enabled the Bank to readily adapt to unforeseen change

³VAT is 93% irrecoverable for Financial Services companies and therefore a real cost

