

CSC Australia – Has Renewal Success enabled it to break free from the Peloton?

Author: Phil Hassey

Date: April 23, 2007

KEY POINTS

- CSC Australia had a successful renewal completion cycle in 2006 with strong ongoing engagement with key outsourcing clients.
- Renewal is the first stage. Proof of future performance requires focus on two factors: ongoing contract execution and the development of new business opportunities in an increasingly competitive marketplace.
- CSC Australia's growth is too reliant on the Paxus business. It is a corporate "gift" to have such a successful subsidiary, as long as it does not diminish focus on driving growth in the core business.
- While historically CSC has not been an aggressive company from a branding perspective, the company's global cycling sponsorship and the success of Team CSC has been a boon to the brand and a possible pointer toward further investment in corporate sponsorship.
- CSC appears to be on an even keel now that acquisition discussions have receded into the fog of corporate history (although it must be remembered fog can clear in an instant).

INTRODUCTION

CSC has long been an organization that has stayed under the radar of many enterprises and industry watchers alike. CSC's strong client base has typically characterized the company as a solid provider of services with excellent execution, but limited customer intimacy. CSC is not flashy. Typically it will not exceed client expectations by a significant margin, but more importantly it will rarely fail to meet customer expectations. CSC clients, particularly those in the public sector, hire and admire the company for this reputation. Services vendors can become the micro culture of their clients, notably in outsourcing. It is clear that clients of CSC, especially in the Public Sector hire and admire CSC for these attributes in no insignificant way.

This document will look at CSC from a corporate level, but is focused on their performance in Australia. Current projections show CSC will exceed the AU\$1B revenue mark in 2007 - a significant milestone, and become the third Australian IT services company to surpass this number, following EDS and IBM.

CSC GLOBAL PERFORMANCE

The tables on the following page highlight CSC's global performance for fiscal years 2005 and 2006, as well as year to date for FY2007. CSC's current fiscal year ends March 30th, 2007.

The data below highlights CSC's solid market performance, although as the first level of revenue breakdown shows there have been some inconsistent performers,

especially quarter on quarter. For clarification, "Other International" includes Asia and Australia, which are separate business units unlike most other vendors, although arguably their fiercest competitor EDS has its ANZ business largely separate from that of Asia Pacific.

Total revenues for 2006 were US\$14.7B. This ranks CSC as the 6th largest IT services company globally.

CSC splits its business into a Commercial and US Government group to highlight the performance of these varied client types.

Table 1: CSC Performance Overview

	Revenue (US\$B)			Growth	
	2005	2006	2007 YTD	05-06	9 Months 06 vs. 9 Months 07
Commercial Revenue					
U.S Commercial	3.8	4.0	2.9	5.3%	-4.9%
Europe	4.3	4.2	2.9	-2.3%	-4.2%
Other International	1.2	1.4	1.1	16.7%	10.8%
Commercial Revenue Total	9.3	9.6	6.9	3.2%	-2.5%
US Government Revenue					
Department of Defense	2.9	3.4	2.6	16.8	6.8%
Civil Agencies	1.8	1.7	1.2	-7.6%	3.9%
U.S Federal Government	4.8	5.1	3.8	7.4%	5.8%
Total CSC Revenue	14.1	14.7	10.7	4.6%	0.4%
Contract Signings (US\$B)	16	12.1	12.6		

Source: Springboard Research, 2007;

Note: All Values, US\$ Billion 2007 is for first 3 fiscal quarters

OVERVIEW OF AUSTRALIAN PERFORMANCE

CSC does not detail its Australian revenue breakdown as it does with its other business units. (Note that CSC does not have a New Zealand practice – this was sold to Hewlett Packard in late 2001, a lifetime ago in the technology services industry). Based on its interaction with CSC, Springboard Research provides the below revenue estimates for CSC's Australian operations. Please note that the revenues shown below are reported in calendar years and in Australian Dollars.

According to CSC's predictions it will break the AU\$1 Billion level for the first time in 2007. This shows some growth and momentum, with CSC claiming 2005-2006 growth of 13.7% and projected growth for 2007 of 11%. This is above the industry growth of 6-

7%. Significantly and in some terms worryingly, growth is coming overwhelmingly from the Paxus employment and contracting business. This provided \$275M in revenue in 2006. This growth needs to be put in context. Without the impact of Paxus, it is realistic to expect that CSC would be experiencing flat growth despite the renewal success. This is readily assumed to be a factor in the recent executive level changes at CSC Australia.

Table 2: CSC Australia Revenue (AU\$M) – 2005 & 2006

	2005	2006	Growth Rate
CSC Australia Revenue	870	990	8%

Source: Springboard Research, 2007

Table 3: CSC Australia Revenue by Contributor (AU\$M) – 2006

	(AU\$M)	% Breakdown
Paxus	275.0	27.7%
Professional Services	101.2	10.2%
Outsourcing	613.8	61.0%
CSC Australia Revenue	990	100%

Source: Springboard Research, 2007

AUSTRALIAN OFFERING AND SOLUTION AREAS

For a service provider of its size, CSC's offering areas are relatively focused and concentrated. This is in part due to the large and mature capabilities in the US Federal Government. For the Australian market, CSC has the following key solution areas:

- Labor Supply (Paxus)
- Consulting
- Systems Integration
- Infrastructure Outsourcing
- Application Services

In the opinion of Springboard Research, CSC Australia differentiates itself from other IT companies in the following solution areas.

- Labor Supply (Paxus)
- Infrastructure Outsourcing
- Consulting

The other solution areas are in general more of an enabling tool than providing a leadership position or point of differentiation. They do of course enable CSC to provide integrated capabilities to clients which is only offered by a handful of service providers in the local Australian marketplace.

From an industry or vertical market point of view, CSC describes itself as serving the following verticals:

- Telecommunications
- Defense
- General Public Sector
- Financial Services
- Mining and Resources
- Manufacturing
- Other Industrial

In the opinion of Springboard Research, CSC Australia has potential points of differentiation in the following vertical industries:

- Defense
- General Public Sector
- Insurance (as a "subset" of Financial Services)
- Mining and Resources
- Manufacturing (notably Steel)

In Springboard Research's view, business activity in the other verticals tends to be opportunistic.

RENEWAL/RE-BID ACTIVITY

As with all major IT services vendors in Australia, CSC had a significant renewal schedule in 2005 and 2006, with more renewals planned for 2007. CSC has had a strong performance in this regard (as have many IT players despite claims by some to the contrary). The major loss came from the Federal DIMA deal (Department of Immigration and Multicultural Affairs), who awarded a desktop and helpdesk contract in January 2007 to Unisys. In addition, the large and highly sought-after BHP Billiton renewal is in the final stages of decision (at the time of this report). While the resources sector is traditionally not a proportionally large user of IT (excess capital is used in machinery and similar process enablers), the BHP Billiton contract provides significant status for whoever wins it. At the time of publishing CSC has been successful with the Application Management part of the engagement, with infrastructure yet to be announced.

CSC is the incumbent for the BHP Billiton bid and has recently established a "Mining and Resources Center of Excellence" in Sydney to help facilitate deeper relationships with this industry. In addition, CSC has been successful in developing a number of point solutions for the industry such as underground traffic management, which is a best practice solution developed in collaboration with a range of unique partners.

VALUE OF TEAM CSC FOR CSC CORPORATION

CSC commenced sponsorship and naming rights of the Team CSC cycling team in 2001. This was initially undertaken to raise CSC brand awareness in Europe, largely, although not exclusively for participation in the Tour De France. From a cycling and race results perspective, the team has grown and is now considered a leading force

in the cycling world providing multiple winners of key races and race stages. As an American company, CSC also was an indirect beneficiary of the ongoing success of Lance Armstrong in the Tour de France.

Team CSC's value to the broader CSC organization has not yet reached its full potential. The fact that CSC does not sell products is a disadvantage, but as IBM and Atos Origin showed with the Olympics and historically Unisys with the Rugby Union World Cup, event product showcases have potential. It is only recently that CSC Corporation has begun to leverage Team CSC's potential, and while the benefits typically are not technology based, CSC has been able to showcase wireless solutions and Internet tools used to track riders at all stages of a race.

The real value of team sponsorship, particularly outside of Europe, is in leveraging the multicultural dynamics of Team CSC to highlight for clients the value of teamwork in cycling and the extension of that philosophy to CSC's solutions set. It is not a unique use of sponsorship, but for a company that is reticent in its marketing communications, it is a step forward. In markets such as Australia, CSC has also been active in using Australian team riders in seminars to highlight the dynamics of professional cycling and how this can be applied to business and IT management.

BUSINESS BALANCE – OUTSOURCING AND PROJECT-BASED WORK

As highlighted in the offerings section above, CSC Australia has a range of capabilities – and some are more effective than others. CSC Australia typically has two distinct yet integrated service delivery mechanisms: Global Infrastructure Services and Global Technology Services. While there has been some growth in the consulting business albeit through Paxus, it is clear that the outsourcing market is the more active of the two. This is not surprising given CSC's focus on renewals for the Australian outsourcing marketplace in the last two years.

In terms of future offerings, business process outsourcing (BPO), e.g. insurance claims management, is a challenge for CSC and the industry in general. CSC is looking to provide focused solutions for this market but feels that as vertical depth is its key services differentiation, there is limited expectation that it will look to enter the horizontal BPO market, such as human resources or customer care management.

GLOBAL DELIVERY

CSC has gained a strong reputation among its clients for delivering on its promises. This is a strong brand attribute. However, the organization is still a conservative firm (matching its atypical client list). This reflection of its client culture has perhaps been a key reason why CSC has been relatively slow to embrace global delivery. CSC does have global delivery capabilities in markets such as India and Malaysia and a capability-based service delivery model, but in comparison with their peers such as IBM, Accenture, EDS and HP, they have been comparatively slow to accept the benefits of global delivery. At the end of 2006, CSC had approximately 7,000 employees in India, and 17% of employees located in offshore environments. This demonstrates a rapid upscale in the last 12 months, but is still behind the levels of competing firms.

For the US and Australian Department of Defense, relative under-development in global delivery resources is not of concern. But for enterprise customers, geographical diversification is an important company strategy and one CSC needs to prioritize. Whether this change in focus is organic or a decision for the CSC board, it's recommended that current global ramping up should continue, to provide greater diversification of resources within India and globally.

FUTURE GROWTH OPPORTUNITIES

The historic performance of CSC Australia has been robust with some excellent client partnerships and client management, interspersed with more problematic challenging clients. This is nothing new for CSC or outsourcers in Australia, although in some regards the natural conservatism of CSC makes this less of an issue than for some of its competitors. However, the relatively narrow client base that CSC Australia serves is a problem moving forward.

For future revenue growth, Springboard Research will be looking for CSC to aggressively tackle new engagements in the market. There is an irony here of course. The relatively strong trend to remain with incumbent providers in the current outsourcing renewal cycle has benefited CSC and EDS in Australia, but as CSC's strong sales teams disengage from renewal activity and move toward untapped business, new clients will fuel CSC's continued growth.

CSC will need to be aggressive in the enterprise and major public sector areas and carve out new business with a push into the medium enterprise space. CSC has had some success in the medium-sized government sector, but that needs to shift to the enterprise sector - and quickly - for CSC to maintain the growth rates of recent years, without reliance on Paxus.

CONCLUSION

CSC Australia has a strong and deserved market position as one of the leaders in Australia's IT Services industry. To grow its business and reputation, CSC should pay attention to several factors. These include, but are not limited to:

1. Shift to "New Business" engagement from a renewal cycle
2. Continue to focus on core verticals (potential conflict with factor 1 above)
3. Escalate creation of global delivery networks to increase integration for clients in Australia
4. Increase investment in marketing and promotion of the CSC brand
5. Focus on ongoing corporate stability

The fickle nature of the outsourcing marketplace means that the above will not be easy for CSC to achieve in Australia. In Springboard Research's opinion, the outsourcing market in Australia is comparable to Canada and the U.K as the most competitive environment globally. Everyone at CSC from Mike Shove to the most recent graduates need to be aware of this and ensure that they deliver on current capabilities while at the same time position the company for growth in the future. It is a delicate dance for a A\$1Billion firm to achieve.