

Purchasing an ASP Service

Lessons Learned from Executives

An IDC White Paper

Analysts: Jessica Goepfert and Meredith Whalen

Introduction

Since 1997, IDC has been researching Application Service Providers (ASPs), an application delivery model whereby buyers gain access to enterprise applications ranging from accounting and human resources (HR) to ecommerce and customer service. Under this model, a vendor prices and packages applications and related services to ensure rapid implementation and minimize the expense and risk associated with the entire application life cycle, which spans acquisition, implementation, and ongoing maintenance.

Today, the ASP model is steadily gaining acceptance. In the past year, we have witnessed major IT players such as IBM and Microsoft announce formal ASP strategies, bringing credibility to the model. Up until this point, there has been little history from which to learn. Both ASPs and customers were largely venturing into the unknown. Now, however, the first ASP customers, the early adopters, are speaking out, and ASPs, prospective customers, and the entire IT industry want to know: What are they saying? Is the ASP model delivering on its promise? What lessons can these customers share with future ASP customers about this burgeoning market?

In a recent study, IDC interviewed executives at 10 companies about their experience selecting an ASP, their satisfaction with the service to date, and their advice for future customers. This paper:

- Outlines the lessons learned from ASP customers
- Discusses the emerging need for services and service delivery by ASP providers
- Introduces Interpath, an ASP that appears to be positioning itself accordingly as a service-oriented ASP
- Analyzes the drivers for selecting an ASP and provides recommendations for how to procure the services of an ASP

Lessons Learned

A couple of years ago, ASPs entered the market pledging to reduce total cost of ownership and alleviate IT headaches; thereby allowing the customer to focus more on strategic business priorities. Have ASPs been able to live up to their promise? We asked business executives at 10 companies to discuss some of the benefits and challenges they have experienced since procuring an ASP service.

Benefits

Overall, the ASP customers we spoke with were pleased with the service thus far. From measurable benefits such as cost reduction to the more intangible improved communication, the executives easily cited many advantages of using an ASP.

- **Focus on core business.** The ASP model allows customers to focus on their core business. Although it's tough to put a dollar value on the freedom this model affords, several customers cited it as an immediate benefit. Executives and IT departments no longer need to concern themselves with day-to-day technology issues or staffing woes and instead can focus their energies on growing their business.
- **Rapid deployment and flexibility.** Speed is a critical factor for companies that want to compete in today's Internet economy. Customers appreciate the ASPs' expertise in implementation methodologies, which enables businesses to have a cutting-edge application environment up and running in record time. Likewise, they noted the scalability of the system and the ease of adding new users, applications, and technologies. Because ASPs essentially have "applications on tap," adding more users or new application functionality may be as simple as the ASP "turning the faucet open a little wider."
- **Improved information flow.** Other IDC research has shown that businesses, particularly in industries characterized by mergers and consolidation, are struggling with multiple, disjointed systems that cannot "speak" to each other. With everybody on one system and sharing the same data, it is easy to see how subscribing to an ASP service can address this concern by facilitating communication with employees as well as with customers.
- **Application expertise.** The combination of shorter application cycles and the IT staffing crunch presents a formidable challenge for businesses. An ASP that provides perpetual maintenance and

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the latest versions of an application helps companies to address both of these issues. According to one customer, using an ASP enables the company to “have expertise at their fingertips all the time.”

- **Total cost reduction.** Technology improvements are often viewed as either revenue-generating or cost-saving investments. The ASP model, which falls into the latter category, aims to reduce expenditures on hardware, software, and network components. A less apparent, but equally valuable, benefit is that employing an ASP can also help companies save on recruiting, staffing, and training costs. After conducting a cost analysis, one CFO commented: “It reduced the cost so much that we felt we couldn’t afford not to do it!”

Challenges

Potential customers and ASPs alike can learn just as much, if not more, from the problems ASP customers encountered as they can from the benefits they experienced. Four topics consistently surfaced when the executives were asked to share some challenges that they have encountered in dealing with ASPs:

1. **Finger-pointing.** When ASPs did not have the network under their control, they seemed to blame the networking company for connectivity problems and vice versa. As one executive said: “Off-site is fine, but connectivity becomes a greater issue.”
2. **Inexperienced companies.** Since the ASP is a relatively new concept, most ASP customers are still struggling and learning throughout the process. However, most executives added that they had their expectations set at the appropriate level.
3. **Communication.** Because of communication breakdowns, customers were sometimes confused about what was actually included in the service offering: “I thought we were going to get an ISP connection as well. As it turned out, we didn’t.” They also suggested that the ASP was not always aware of network issues: “Sometimes we are down and the ASP doesn’t even know it.”
4. **Lack of control and security.** In signing with an ASP, customers are entrusting control of their application environment to a third party. ASP customers we spoke with felt protective and concerned about the security of their data.

Advice from ASP Customers

Now that customers have gone through the process, ironed out the wrinkles, and started telling their story, what insight do they offer to those considering using an ASP? When we asked our executives to share some lessons learned with future ASP customers, the prevailing theme was, “Do your homework.”

Before procuring an ASP service, the executives suggested that companies take the time to truly understand their business needs and what components and services they are getting from the ASP. According to one executive, every application should be evaluated for its pros and cons when choosing an ASP. “For some applications, it could be the best thing, and for some, it could be the worst,” he said. It is also important to recognize the different models and types of ASPs and the benefits and limitations associated with each.

More than once, executives pointed out that there was a natural liquidity risk involved in dealing with ASPs. Because ASPs are generally immature companies, a CIO suggested that the financial health of the vendor was one of the most important factors in selecting an ASP and should be investigated thoroughly.

Finally, as implied by the challenges encountered, customers agree that communication among all parties involved is crucial. Although probably true for every business decision, having expectations set realistically from the start can facilitate the entire process and is a proactive step toward preventing future frustrations.

An Emerging Trend: The Importance of Services and Service Delivery

One of the key themes that emerged from the ASP customer interviews is that services and quality service delivery are increasingly important to customers. Currently, ASPs are differentiating themselves primarily by the types of applications that they provide. IDC strongly believes that in time, ASPs will need to enhance their offering with services — both around the delivery and the ongoing management of the application.

In our interviews, ASP customers noted the importance of ongoing customer support. Regardless of the size of their business, they want the ASP to be quick to respond and customer centric. According to an executive from a \$100 million company, “The size of the ASP was not as important as the anticipated responsiveness to our company. We’re not GE. We didn’t want to be a small fish in a big pond.” Again, we see an unmet need and a chance for differentiation.

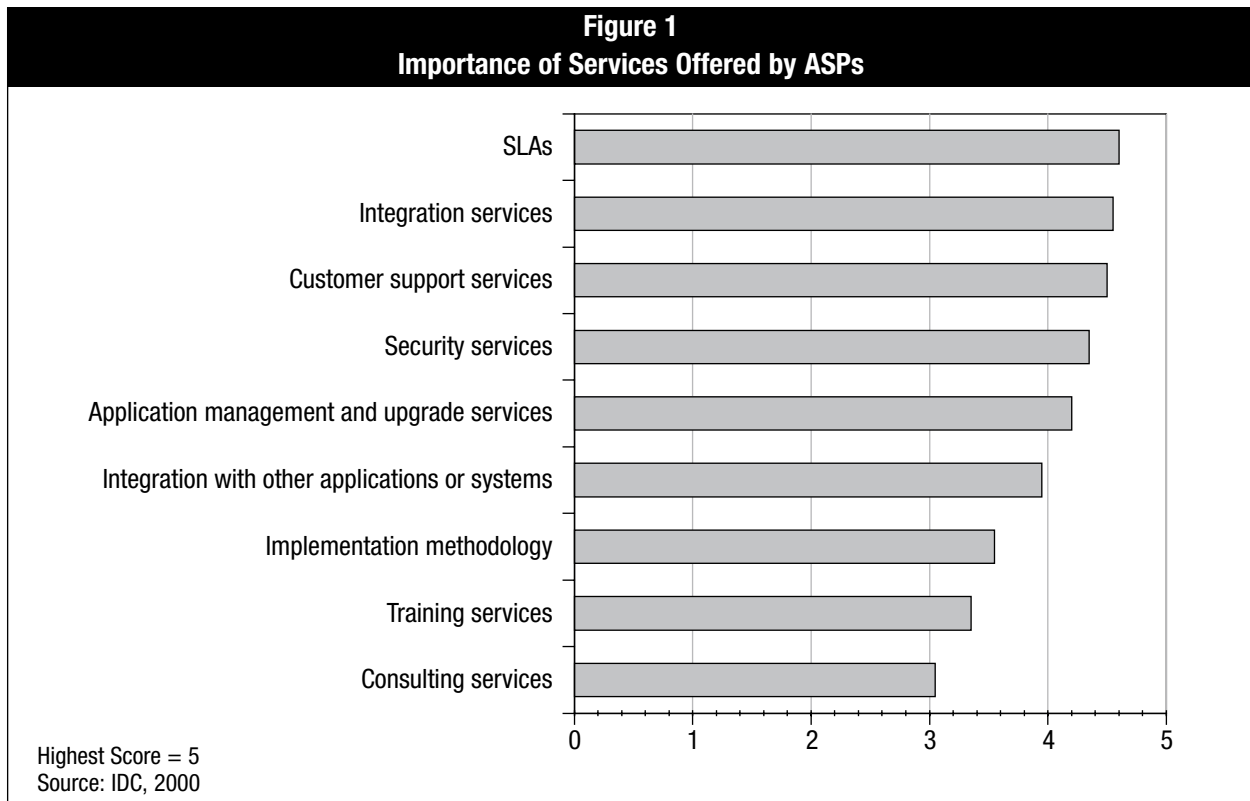
Given these findings, IDC recommends that ASPs find ways to expand and emphasize their services, either around the delivery (e.g., through a focus on customer service) or through add-on features (e.g., enhanced security components).

Valuable ASP Services

The fundamental principle behind the ASP model is that software is now being delivered as a service. Customers are looking for more than just access to and functionality of the application. Herein lies the chance for an ASP to distinguish itself from the hundreds of other

ASPs that clutter the market. Most ASPs have not yet focused on services, as they have been busy putting together their business models, selecting partners, and signing up their first customers. ASPs can enhance their offering by adding services, such as training, or by increasing their focus on customer support. Which of these features do customers value the most? What services should you look for when evaluating ASPs?

While customers consider all the services we listed important, service level agreements (SLAs), integration services, and customer support services topped the list — practically in a dead heat (see Figure 1).



- **Service level agreements (SLAs).** When you are outsourcing your mission-critical applications, chances are you have little tolerance for downtime. Thus, negotiating the SLA is key to protecting your investment. SLAs are contracts between you and the ASP outlining the quality and performance levels you can expect from the ASP. Components can include metrics such as application availability, response time, security standards, and provisions for recovery and outages.
- **Integration services.** As your company grows, you will need to adapt your IT platform to meet new business challenges. Customers are seeking an ASP that can provide services to seamlessly integrate new applications with their existing operations — legacy software and all. ASPs that offer such services can position

themselves as a flexible and scalable partner, ready to meet their customers' current and future needs.

- **Customer support services.** The executives we spoke with sought assurance that they could count on the ASP for ongoing support. When the need arises, customers expect a rapid response. They do not want to waste valuable time trying to figure out whom they need to contact. Given the high customer acquisition costs and age of the market, it is imperative that the ASP you choose concentrate on satisfying its clients.

Interpath: A Service-Oriented ASP

Company Background

Interpath Communications Inc. (www.interpath.net), located in Morrisville, North Carolina, is one example of a business that has recognized early the importance of being a service-oriented ASP. The company was founded in January 1998 by Carolina Power & Light (CP&L) and currently employs about 300 people. In June 2000, Bain Capital Inc. purchased 65% of the company, with CP&L maintaining a minority ownership. Bain and CP&L have recently invested another \$100 million in Interpath, giving the company the necessary financial resources to operate for the next few years.

Interpath provides the following solutions:

- eBusiness applications, including applications from Vignette, BroadVision, and Microsoft
- Customer relationship management, including applications from Pivotal Software
- Managed hosting and networking
- Data services
- Comprehensive ebusiness development services

Additionally, Interpath began its global expansion with the August 2000 acquisition of Alta Internet Business Centres, one of Australia's leading ASPs.

Executive Team

Interpath's senior management team has strong roots in the wireless, network, and ASP industries. Chairman and CEO Joel Schleicher spent 11 years in the technology and communication services sectors. Among other notable positions, Schleicher served as COO and President of Nextel Communications Inc. from 1989 through 1995, growing the wireless company from \$17 million to \$400 million in revenue. Schleicher is surrounding himself with people steeped in ASP industry experience, further strengthening the potential of the company.

Value Proposition

Interpath's mission is "to be the leader in delivering outsourced application development, integration, and hosting solutions that enable customers to win." The company is focused on delivering comprehensive solutions and forming long-term partnerships with its clients. Interpath has devised a three-pronged strategy to achieve this goal. The company will:

1. Provide state-of-the-art solutions through a full suite of industry-leading enterprise applications
2. Partner with systems integrators to expand the breadth of its product offerings and to obtain expertise in new applications
3. Continue to build world-class monitoring and application management capabilities

In February 1999, Interpath opened the Interpath Operations Center (IOC). Within the walls of this 90,000 square foot facility is the company's state-of-the-art "Mission Control" room, from which the company monitors and manages its customers' networks, systems, and applications on a 24 x 7 x 365 basis.

Customers

Interpath has minimized its downside risk by building a customer base of stable and secure companies. Clients include Ericsson, First Union, Glaxo Wellcome, Nucor Steel, Pergo Flooring, Quintiles, and Woolworths.

The Interpath Difference

In the flood of ASPs entering the market, Interpath differentiates itself through its end-to-end application ownership and a service-oriented approach.

End-to-End Ownership

Through its "Mission Control" room in the IOC, Interpath provides customers with an end-to-end application solution, including processing infrastructure, network, application skills, and overall management. Interpath takes care of everything from design to delivery and works closely with its partners every step of the way to ensure a seamless process.

Since partnerships are important to the delivery of the ASP service, Interpath seeks to partner with companies that are leaders in their market and that have proven methodologies, strong references, and deep breadth of experience and capabilities. The company also requires that partners have embraced the ASP model and devised a formal market strategy.

A Focus on Services

Interpath provides a full suite of services around its ASP offering. Interpath's customer-centric focus is driven by Schleicher, who has a very proactive attitude toward customer satisfaction. The company will regularly meet face-to-face with customers to learn their needs first-hand, and it has a director-level employee whose primary job is to follow up with customers to ensure they are always satisfied. Every employee's compensation is formally tied in part to the company's overall customer satisfaction levels, an approach that aligns all Interpath workers. An in-house team monitors and manages the application environments to ensure that customers' systems are available and running smoothly. Customers have access to technical support on a 24 x 7 x 365 basis. Additionally, Interpath works with best-of-breed system integrators in an effort to bring clients the latest expertise and newest applications.

The IOC and high-quality infrastructure enable Interpath to offer a secure environment and performance guarantees. Security services and provisions include:

- Managed firewalls
- Intrusion detection systems
- Response services
- Disaster recovery
- Redundant fire detection suppression system

Interpath's Strengths and Challenges

Interpath's ASP solution addresses several of the customer demands and market needs revealed by our research. In particular, the company's focus on services plays directly to many of the concerns voiced in the interviews.

- **A forward-thinking company.** Recognizing the importance of services, Schleicher has clearly positioned Interpath as a service-oriented ASP, providing end-to-end solutions complete with a suite of service offerings. Additionally, Schleicher brings wireless expertise to Interpath, which suggests that the company will be an early player in the emerging wireless ASP arena. Bain Capital's investment in Interpath brings both capital and management expertise to the company, enabling long-term decision making and strategies.
- **Customer-centric focus.** Starting with Schleicher, the company's customer-centric vision permeates the organization. Escalation procedures ensure that the CEO knows about critical incidents within four hours. In fact, Schleicher has been known to give his home telephone number to clients, assuring them that Interpath's priority is to better serve them. Additionally, Interpath has developed a hiring process to identify, recruit, and retain employees with a customer-centric focus.

- **Single source.** Interpath owns the application environment, from the processing infrastructure and network to the application skills and overall management. Therefore, customers can turn to Interpath as the single source for a turnkey solution, leaving little room for finger-pointing. Given that Carolina Power & Light, a utility company, founded Interpath, the ASP inherently has infrastructure expertise. The IOC was built with the latest hardware, backup generators, and redundant networking to bring peace of mind to Interpath customers. The performance of this infrastructure is backed by SLAs, which ensure security, reliability, guaranteed uptime, redundancy, and several other components. Interpath provides system integration competencies through its partnerships with leading system integrators. The company works closely with system integrators throughout the entire process; thereby learning first-hand the intricacies of each customer's application environment.

While Interpath's approach aligns well with the evolving, more service-oriented ASP market, strategy execution will not be without challenges. In its go-to-market plan as a turnkey solution provider, Interpath must be careful not to follow in the footsteps of other ASPs that failed to deliver on their promise of seamless end-to-end service. Forming and managing tight strategic partnerships can mitigate such pitfalls.

Next Steps: Lessons for Procuring an ASP Service

Now that early ASP customers are beginning to talk about the selection process, benefits, and challenges of the service, it is up to you to decide if there is a place for ASP services in your organization.

Is an ASP Right for You?

ASPs offer a compelling value proposition to companies competing in today's new economy. Pressure to deploy ebusiness, rapid changes in technology, and a lack of in-house expertise are just a few of the factors driving the growing popularity of ASPs. While there are several advantages to the ASP model, when we asked customers to rank them according to importance, the following four benefits topped the list:

1. **Ability to focus on core business.** Running a business is all about priorities. Having a vision and inspiration for your company is crucial for your organization, employees, and customers. Yet, too many companies find themselves being sidelined from their main priorities because of distractions with issues around day-to-day operations. Technology is often one of the worst offenders when it comes to business distractions, particularly for the IT department.

Customers turn to ASP services to eliminate the need for IT departments to manage application environments. As a result, IT resources are free to be deployed on initiatives that are strategic to a company's overall business goals (e.g., initiatives that support the creation of new products and that spur innovation).

2. **Access to applications.** Consistent with previous IDC research, affordable access to applications is one of the top drivers in the decision to use an ASP service. Historically, packages from vendors such as SAP, BroadVision, and Vignette have been perceived as expensive and complex for small and midsize businesses, with licenses running a company up to millions of dollars. Our interviewees clearly valued gaining affordable access to applications previously outside their budgets. An ASP solution levels the playing field; bringing the latest technology to their businesses and allowing them to more effectively compete with larger firms.
3. **One-stop shopping and support.** Companies are tired of managing multiple vendors and of the inevitable finger-pointing that occurs when something goes wrong. They are looking for a single point of accountability. Although there are various components to the ASP service, they are packaged together and sold to the customer as a single offering. In the customer's eyes, the ASP alone is responsible for delivering on the contract. This is an attractive remedy to making multiple calls to vendors when your system is down.
4. **Lack of in-house expertise.** IDC estimates that there will be over 760,000 unfilled IT positions this year. With such a shortage of IT skills, IT departments are overburdened. The result is that they spend more time on support and maintenance and less time on strategic business issues. New versions of already complex applications flood the market before IT departments fully digest the previous release. It is no wonder that executives are turning to ASPs.

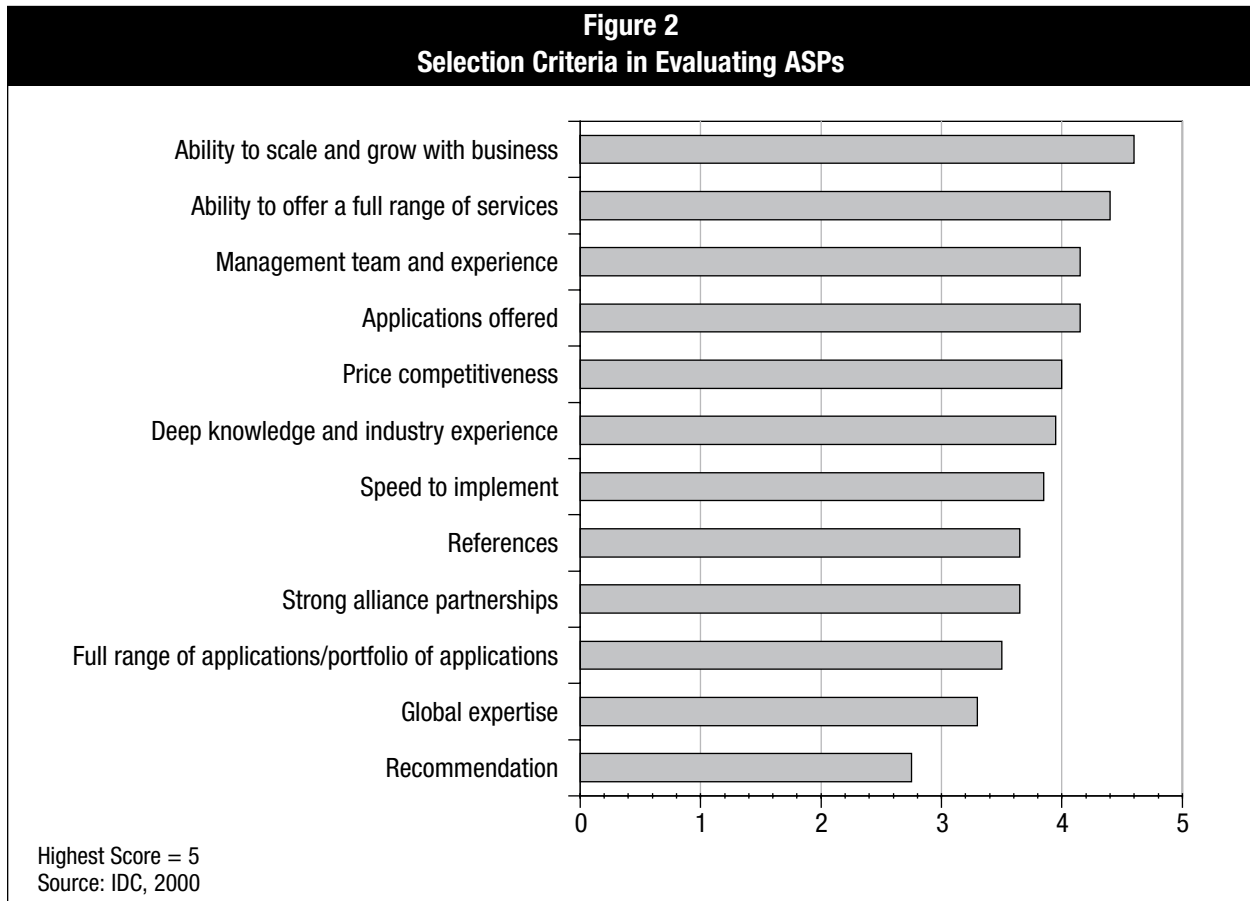
By outsourcing to an ASP service, you can relieve your IT personnel of many of their support duties, including application upgrades, management, and support, and they can focus on technology to execute your core business strategy. However, some smaller businesses do not have an IT department. For these companies, an ASP is a total IT solution, instantly providing experienced personnel, robust applications, and a sophisticated infrastructure.

ASP Selection Process

Once you have made the decision to outsource your application environment to an ASP, the question then becomes "Which ASP?" The selection process should not be taken lightly. You are, in effect, relinquishing direct control over your data, handing it off to a company that claims it will be available and secure. As a business professional, it is your duty to perform due diligence when evaluating ASPs. A poor choice could lead to months of wasted time and thousands of lost dollars.

While many of the customers we spoke with did not have a “formal” process for evaluating ASPs, some common themes emerged from the interviews. Executives formed cross-functional teams representing the various business areas that would be most affected by the decision. They gathered research, eliminated ASPs that did not offer the desired applications, and conducted cost analyses. A C-level executive usually made the final decision.

We found more conformity when we investigated *why* they selected a particular ASP (see Figure 2).



Our survey revealed the following four criteria were most important in the decision-making process:

1. **Ability to scale and grow with the business.** Regardless of the industry your business is in, the fact is that both your company and the market will change and grow. To stay competitive, your business needs the flexibility to respond and adapt to these changes. Most likely, you will engage in a multiyear contract with an ASP. Thus, choosing a service provider that can scale and grow with you over the years is paramount.

The relationship with the ASP is best thought of as a partnership, not as the typical customer/vendor association. The ASP must have a willingness to work with you to understand your current and future business needs and exhibit the capability to meet those needs. As one executive noted: “You’re making a bet that these people will be a part of your company and that they will act like a partner ... That’s why we looked so closely at them from a lot of different angles.”

2. **Ability to offer a full range of services.** In choosing to use an ASP, you are physically moving your mission-critical data out of your direct control. With such high stakes, you want a true service provider, not just a company selling software in a new way. Your demands go beyond reliability and connectivity to user support, security, and problem resolution. A true service provider will have expertise in project management, application integration and management, and overall customer support. If an ASP is lacking in any of these service competencies, it is important they have tight partnerships in place to round out the offering. Most importantly, the organization should be responsive and work to solve the issue, not pass the blame.
3. **Applications offered.** Obviously, the ASP must support the applications necessary to run your business. Equally important are the applications they plan to offer in the future. Over time, business needs change, and systems need to be expanded and adapted accordingly. As you delve further into the evaluation process, you should investigate the ASP’s level of application expertise — in terms of implementation, integration, and ongoing management experience. The core of the ASP’s value proposition is access to and management of applications. You want assurance that the applications will be up and running when you need them.
4. **Stable, experienced management team.** Given the immaturity of the ASP market, it can be difficult to find an ASP with a proven track record. Therefore, executives are examining the management team as part of the review process. As indicated earlier, in signing with an ASP, you are gambling that it will be around in a few years. A look at the skills and experience of the existing management team can give prospective customers a good feel for the ASP’s strengths and weaknesses.

Conclusion

Keep in mind the valuable lessons we learned from speaking with current customers, and perform your own reference checks in your search for ASPs. Although this is a truism, it cannot be emphasized enough in this emerging market. Don’t expect the ASPs to have many years of experience, as this is a new market. But do look into their roots, staff expertise, and committed partners.

As more and more ASPs offer the same or similar applications, look for those that complement their offering with services. Understand the components of the SLA. Are the standards higher than what could be accomplished in-house? Inquire whether they have experience in implementing and managing applications, as well as monitoring and managing a network. Make sure you are comfortable with the security precautions and services, as this is where your company's data will reside.

Most likely, the ASP contract you sign will be for a three- to five-year period. Does the ASP have the integration services and capabilities to meet the needs of your growing business? Look beyond the current offering and consider the expertise of the management team and where the ASP may be a few years down the road.

Lastly, take into account the attitude and focus of the ASP. The actual contract is words on a sheet of paper. What counts is the spirit behind the words and the mindset of the people who will ultimately be delivering the service. Though definitely a qualitative and subjective factor, you want reassurance that the ASP is determined to serve its customers for the life of the relationship.

Although the ASP market is just a few years old, it is already beginning to evolve into a more service-oriented environment. It did not take long for customers to recognize that the value of the ASP model lies in its ability to incorporate services and provide immediate relief from IT pressures. The degree to which the customer will benefit from the access to applications and technology hinges on the responsiveness of the ASP. An ASP that does not work with clients to satisfy their needs and help their companies grow cannot expect to build customer loyalty. The ASP needs to invest in its customers as much as its customers are investing in it. The relationship is truly a partnership, and it needs to be treated as such for both parties to benefit.

NORTH AMERICA

Corporate Headquarters

5 Speen Street
Framingham, MA 01701
508-872-8200

IDC Canada

36 Toronto Street, Suite 950
Toronto, Ontario, Canada M5C2C5
416-369-0033

IDC Irvine

18831 Von Karmen Ave, Ste 200
Irvine, CA 92612
949-250-1960

IDC Mtn. View

2131 Landings Drive
Mountain View, CA 94043
650-691-0500

IDC New Jersey

120 Wood Ave South, Suite 509
Iselin, NJ 08830
732-632-9222

IDC New York

2 Park Avenue
Suite 1505
New York, NY 10016
212-726-0900

IDC Texas

100 Congress Ave, Suite 2000
Austin, TX 78701
512-469-6333

IDC Washington

8304 Professional Hill Drive
Fairfax, VA 22031
703-280-5161

ASIA/PACIFIC

IDC Asia/Pacific (Hong Kong)

12/Floor, St. John's Building
33 Garden Road
Central, Hong Kong
852-2530-3831

IDC Asia/Pacific (Singapore)

71 Bencoolen Street, #02-01
Singapore 189643
65-226-0330

IDC Australia

Level 4, 76 Berry Street
North Sydney, NSW 2060, Australia
61-2-9922-5300

IDC China

Room 611, Beijing Times Square,
88 West Chang'an Avenue, Beijing,
P.R. China, 100031
86-10-8391-3456

IDC (India) Limited

Cyber House
B-35, Sector 32 - Institutional
Gurgaon - 122002, Haryana, India
91-124-6381673 to 80

IDC Japan

10F The Itoyama Tower
3-7-18, Mita Minato-ku
Tokyo 108-0073, Japan
81-3-5440-3400

IDC Korea Ltd

Suite 704, Korea Trade Center
159-1, Samsung-Dong, Kangnam-Ku
Seoul, Korea 135-729
82-2-55-14380

IDC Malaysia

Suite 13-03, Level 13, Wisma KiaPeng
No. 3, Jalan Kia Peng
50450 Kuala Lumpur, Malaysia
6-03-2163 3715

IDC New Zealand

Level 7, 246 Queen Street
Auckland, New Zealand
64-9-309-8252

IDC Philippines

7F, SEDCCO 1Bldg
Rada Street Corner
Legaspi Street
Legaspi Village
Makati City, Philippines
632-894-4808

IDC Taiwan Ltd.

10F, 31
Jen-Ai Rd, Sec 4,
Taipei 106, Taiwan, R.O.C.
886-2-2731-7288

IDC Thailand

27 Soi Charoen Nakorn 14
Charoen Nakorn Road, Klongtongnai
Klongsan Bangkok 10600, Thailand
66-2-439-4591-2

IDC Vietnam

37 Ton Duc Thang Street
Unit 1606
District-1 Hochiminh City Vietnam
84-8-910-1235

EUROPE, MIDDLE EAST, AND AFRICA

IDC Austria

c/o Loisel, Spiel, Zach Consulting
Mayerhofgasse 6
A-1040 Vienna, Austria
43-1-50-50-900

IDC Benelux (Belgium)

29 Avenue Louis Gribaumont
B-1150 Brussels, Belgium
32-2-779-46-04

IDC Benelux (The Netherlands)

A. Fokkerweg 1
1059 CM Amsterdam
The Netherlands
31-20-669-2721

IDC Central Europe (ECE)

Male Namesti 13
Praha 1 110 00, Czech Republic
420-2-2142-3140

IDC Central Europe (Germany)

Nibelungenplatz 3, 11th Floor
60318 Frankfurt, Germany
49-69-90502-0

IDC Central Europe (Switzerland)

Niederlassung Züerich
WTC, Leutschenbachstrasse 95
CH - 8050 Züerich
Switzerland
41-1-307-1000

IDC Egypt

39 Iraq Street
Mohandesseen, Cairo, Egypt
20-2-336-7355

IDC France

Immeuble La Fayette
2, Place des Vosges, Cedex 65
92051 Paris la Defense 5, France
33-14-904-8000

IDC Hungary

Bajcsy-Zsilinszky út. 57
Building 3, Rooms 103-104
H-1065 Budapest, Hungary
36-1-153-0555/ext. 165, 166

IDC Israel

4 Gershon Street
Tel Aviv 67017, Israel

IDC Italy

Viale Monza, 14
20127 Milano, Italy
390-2-284-571

IDC Nigeria

House 2, 'C' Close
403 Road, 4th Avenue
New Extension, Festac Town
Lagos, Nigeria
234-1-883585

IDC Nordic (Denmark)

Jagtvej 169B
DK-2100 Copenhagen, Denmark
45-39-162222

IDC Nordic (Finland)

Jarrumiehenkatu 2
FIN-00520
Helsinki, Finland
358-9-8770-466

IDC Nordic (Sweden)

Box 1096 Kistagången 21
S-164 25 Kista, Sweden
46-8-751-0415

IDC Poland/ProMarket

Wrobla 43
02-736 Warsaw, Poland
48-22-644-4105

IDC Portugal

Av. Antonio Serpa, 36 Piso 9
1050-027 Lisbon
Portugal
351-21-796-5487

IDC Russia

c/o PX Post, RDS 186
Ulitsa Zorge 10
Moscow 125525
Russian Federation
7-501-929-9959

IDC South Africa

c/o BMI-TechKnowledge
3rd Floor, 356 Rivonia Blvd.
PO Box 4603, Rivonia, 2128
South Africa
27-11-803-6412

IDC Spain

Ochandiano, 6
Centro Empresarial El Plantio
28023 Madrid
34-91-7080007

IDC Turkey

Tevfik Erdonmez Sok. 2/1 Gul Apt.
Kat 9D; 46 Esentepe
Istanbul, Turkey
90-212-275-0995

IDC U.K.

British Standards House
389 Chiswick High Road
London W4 4AE
United Kingdom
44-20-8987-7100

LATIN AMERICA

IDC Miami

Latin America Headquarters
5301 Blue Lagoon Drive
Suite 490
Miami, FL 33126
305-267-2616

IDC Argentina

Trends Consulting
Rivadavia 413, 4th Floor, Suite 6
C1002AAC, Buenos Aires, Argentina
54-11-4343-8899

IDC Brasil

Alameda Ribeirão Preto, 130 cj 41
01331-000 São Paulo
SP Brazil
55-11-253-7869

International Data Corp. Chile

Luis Thayer Ojeda 166 Piso 12
Providencia, Santiago 9, Chile
56-2-231-0111

IDC Colombia

Carrera 40 # 103-78
Bogota, Colombia
571-533-2326

IDC Mexico

Select - IDC
Av. Nuevo Leon No. 54 Desp. 501
Col. Hipodromo, Condesa
C.P. 06100 Mexico, D.F.
52-5-256-1426

IDC Venezuela

Calle Guaicapuro
Edif. Torre Seguros Alianza
Piso 6, Ofc. 6-D, El Rosal
Caracas 1060, Venezuela
58-2-951-3270

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