



ACS to restart federal business unit

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By VICTOR GODINEZ / The Dallas Morning News
vgodinez@dallasnews.com

Affiliated Computer Services Inc. is ready to reboot its federal business segment.

Five years ago, the Dallas-based outsourcing company sold its nearly billion-dollar federal unit to Lockheed Martin Corp. and signed a noncompete agreement with the defense giant.

That agreement expires at the end of next month, and on Nov. 24, ACS will be allowed to dive back in.

But while the company hopes the federal division will regain that billion-dollar status within five years and keep on growing after that, analysts say ACS could find it tough to keep its profit margins up.

Tim Conway, senior vice president and managing director of ACS' federal solutions group, said the original federal division was focused on mere "staff augmentation."

In other words, ACS didn't really use its own technology or business processes to make the federal agencies more efficient. Instead, ACS just went in and took over management of the employees in a particular department. When a different outsourcing company would take over the contract, the logos on the shirts would change, but not much else.

"It had gotten to the point where it was just under a billion dollars, and it was no longer a growth business," Mr. Conway said.

The new federal division, though, will focus on completely revamping the operations of clients, improving efficiency, adding technology and cutting costs.

"We're going to go back in in much more the ACS style," Mr. Conway said.

For example, ACS will offer a service to digitize paper documents, making it easier to store, search and archive those files.

The company will also sell its higher-end customer service call centers, since, as Mr. Conway notes, ACS currently handles about 1 million customer calls per day for its other clients.

Electronic payment – replacing regular paper checks to Social Security recipients, for example, with rechargeable debit cards – is another service ACS will pitch.

There were a handful of exemptions in the noncompete deal with Lockheed Martin that allowed ACS to do business with a few federal customers, such as the Department of Education, and the division currently has sales of about \$350 million.

But it was a scattershot approach, with employees and expertise throughout ACS.

So in the middle of last year, ACS decided to centralize its federal work into a single internal department with about 3,200 employees now, and Mr. Conway was brought on board from IBM.

ACS could well see its revenue from federal customers jump over the next few years, said Sanford Bernstein analyst Rod Bourgeois.

The challenge will be in pumping up the profit margins, he said.

"They definitely needed to find other avenues of growth, and the federal government market is a logical one," Mr. Bourgeois said.

But "government IT services contracts tend to command relatively low operating margins, and that will be a challenge ACS will face."

Mr. Conway said he thinks the federal division is capable of growing both its revenue and profit by 10 percent or more each year for at least the next several years.

"It's an exciting challenge, I've gotta tell you," he said. "You get to go in and set your own success. You're not coming into something somebody else built or somebody else's problems."