Do vendors include transaction characteristics in their risk estimation?

Using unique archival data on 81 projects from a major ERP vendor, we study whether transaction characteristics are included in the vendor’s estimation of risk to project profitability. We hypothesize that project size, contract type, strategic importance, and client familiarity are included in the risk estimations. Regression analysis suggests that, surprisingly, vendors do not include all transaction characteristics in their risk estimation: While we found that larger projects and fixed price (FP) contracts are significantly associated with the vendor’s risk estimation, strategic importance and client familiarity are not. Our data set also incorporates data on project profitability that presents us with the opportunity to test the efficiency of the risk estimation. We found that the vendor’s risk estimation is efficient with regard to project size and contract type. Finally, the efficiency analysis also suggests that vendors deliberately accept profitability losses when conducting strategic projects.

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