

The Shift to SaaS: A high-value opportunity for ISVs

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THE SHIFT TO SAAS: A HIGH-VALUE
OPPORTUNITY FOR ISVS WAS
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Executive Summary

SaaS represents an opportunity for ISVs to fundamentally transform their business to deliver greater value to customers, sell software to a broader range of customers and streamline their internal operations. The market for software is quickly changing to demand this mode of delivery, as software buyers start considering total ownership costs, ease of use and flexibility in their purchase decisions. ISVs need to prepare for such a transition. This paper will discuss the benefits that stem from changes to an ISV's business model (how it competes in the marketplace) and operating model (how the ISV executes on its business model) as well as suggestions on how to prepare for a SaaS transition, based on the experience of 20 ISVs who successfully transitioned from a traditional software licensing and delivery model to SaaS.

SUMMARY OF KEY BENEFITS

ISVs who developed a SaaS version of their software were able to deliver additional value to their customers:

- **New customer segments open, thanks to lower adoption costs and operating costs:** ISVs were able to sell to customer segments who were previously unprofitable due to the reduced server costs enabled by operating SaaS on a public cloud
- **Customer TCO drops as infrastructure complexity falls under SaaS:** ISVs who adopted SaaS were able to reduce the overall cost of software use for their customer by eliminating the need for customers to build out and maintain supporting infrastructure
- **Integration of value-added cloud services improves ISV product offering:** Capabilities that previously would have been time and cost intensive for ISVs to develop are available through a cloud platform ecosystem with minimal integration and support requirements
- **Aggregation of usage data through SaaS model and data scale effects drive product improvements:** Collecting customer usage data provides ISVs with detailed insight into customer needs and pain points, while aggregated data sets enable benchmarking and rapid improvement of products and ISV algorithms

SAAS ISVS ALSO SAW CHANGES IN THEIR ABILITY TO CAPTURE VALUE:

- **Financial predictability improves as recurring revenue grows:** As ISVs shift customers to SaaS consumption from traditional licensed models, the proportion of recurring revenue grows, increasing the confidence and reliability of financial performance
- **New pricing models align ISV value with customers' business needs, driving increased revenue:** The flexibility of SaaS pricing models allows pricing to be tailored to customer needs to more closely tie revenue generation with usage, increasing the value ISVs can capture across their customer base

ISVS WHO SWITCHED TO SAAS ALSO REPORTED SIGNIFICANT OPERATIONAL BENEFITS:

- **The collection of product usage data increases the speed of product development by 33%:** Insights generated through application data collection focus product development efforts on the most important features to customers and support an iterative development process led by in-market experimentation.
- **Engineering efficiency increased 26% under a DevOps model:** Unification into a single software deployment environment with SaaS reduces development, testing and deployment activities needed, letting development teams focus more on high-value product feature development rather than on maintaining system infrastructure
- **Trial and end user engagement opportunities shorten sales cycles:** Customers are able to access trials of SaaS software and explore the potential value easily and with limited technical support, allowing sales teams to more rapidly convince customers of the software business case, without having to go through customer IT teams

Introduction

WHY ISVS SHOULD TRANSITION TO SAAS

SaaS models are seemingly everywhere and new SaaS vendors are regularly appearing on the scene with novel products. However, many ISVs still employ the traditional model of deploying licensed software on-premises. Technical challenges associated with migrating software to a SaaS model and business model challenges in converting from a conventional licensing model to usage-based or a subscription pricing model are blockers ISVs face. This paper outlines the business impacts ISVs realise in moving to SaaS in spite of complexities. These benefits are based on in-depth interviews with executives from 20 software companies who have adopted a SaaS model.

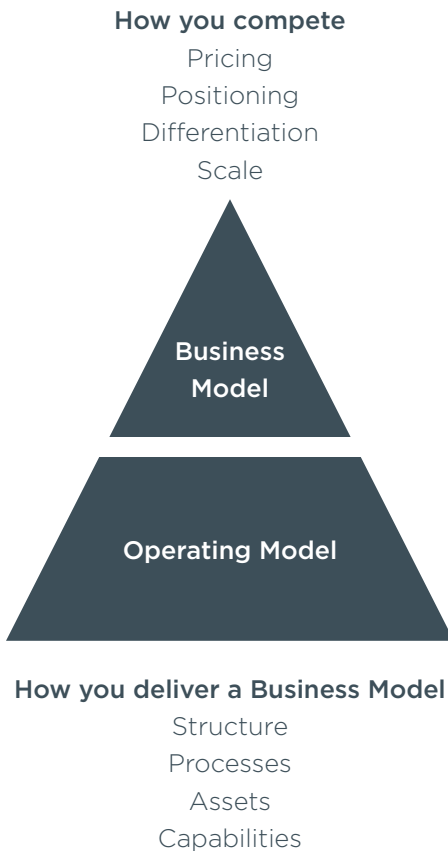
The promises of SaaS are enticing: lower development and support costs, streamlined sales cycles, unified deployment environments and new, data-driven insights into customer behaviour. This is driving growth in the industry. Gartner estimates that the total SaaS market is worth \$37.7B, growing at 20.3% per year.¹

While some of this growth stems from cloud-native SaaS start-ups, traditional software companies are capitalising on this trend. Flexera's research into licensing and revenue models among software companies finds that 70% of ISVs are planning to change their pricing and licensing models within the next two years, up from 56% 18 months ago.²

Interest in SaaS goes beyond changes to how companies deliver and license their applications. Bessemer Venture Partners, a Silicon Valley venture fund, noted in its State of the Cloud 2016 study that legacy software vendors are embracing the SaaS model aggressively. Legacy vendors are not only modernising their applications, but are also spending aggressively to purchase SaaS ISVs to gain access to the technology and talent they need. Legacy firms spent over \$50B annually to acquire SaaS companies³. Valuations for SaaS ISVs reflect the SaaS opportunity; while public legacy vendors are valued at 3.5× annual revenue on average, public SaaS ISVs are valued at 4.9× and private SaaS vendors at 11.2×.⁴

The software marketplace is experiencing a significant shift. For ISVs who sell software under a traditional, perpetual licensing model, it may seem intimidating to think about shifting to SaaS. It often requires a substantial change in how ISVs create, design, deliver and sell software, significant technical investment, changes to pricing and contracts and communicating these changes to customers. However, the benefits of transitioning to SaaS,

Business model impacts



including improved software performance, increased customer satisfaction, shorter sales cycles, improved revenue predictability and more efficient product development processes and greater engineering leverage outweigh these costs.

An ISV’s business model reflects strategic choices, such as to how to compete in the marketplace, how to deliver a differentiated product or service and how to capture economic value. In Keystone’s research, the business model encompasses two key elements: value creation and value capture. Value creation represents benefits the software delivers to end customers, such as the product’s feature set, its performance and ease of use. Value capture represents how much of the value ISVs can retain. An ISV’s value capture strategy is a product of the company’s pricing model and its cost model in serving its customers.

ISVs surveyed as part of this research highlight three value creation benefits in their migration to a SaaS delivery model. First, they are able to deliver improved product capabilities to customers, reduce the customers’ overall costs by working with cloud infrastructure providers and address new customer segments that they could not previously access with their traditional licensed software offerings.

SAAS ALLOWS ISVS TO DELIVER BETTER EXPERIENCES TO A BROADER RANGE OF CUSTOMERS

New customer segments are unlocked as a result of lower customer adoption and operating costs, reduced technical requirements and lower cost to serve.

One of the biggest challenges traditional ISVs face is getting a customer over the hurdle of initial installation and up-front capital costs. Customers typically pay for a perpetual licence in advance, which can be a significant capital expense. The cost only grows if specialised infrastructure is required to run the software. Especially for high-performance software solutions, this can dramatically limit the addressable market to large organisations with significant IT budgets and sophisticated in-house technical teams.

In contrast, ISVs can deliver SaaS solutions to customers much more easily. Getting a customer set up on a SaaS solution is far faster than on-premises solutions, since there is little infrastructure to set up and configure. SaaS ISVs interviewed for this study quoted an installation time reduction of

“Our customers want data compliance at the level of SOX2 or ISO27001, since we are managing patient data. Microsoft Azure strongly complies with these requirements and Active Directory lets us provide detailed permission controls. As a result, security has been much less challenging than we expected, even with risk-averse customers.”

CTO, MEDICAL IMAGE
MANAGEMENT ISV

up to 75%, cutting down the time required to get customers running to 2–3 weeks from 3–6 months for an on-premises solution. This increase in flexibility lets ISVs offer a low entry cost for large customers, while also allowing rapid increases in adoption as cloud infrastructure scales to support.

Additionally, adopting a SaaS model that runs on the public cloud eliminates a number of barriers to geographic expansion. In a traditional model, vendors wishing to expand geographically would need to set up local partnerships or send a team of support engineers to client sites around the world, options that are expensive and time-consuming. In a SaaS model, ISVs can deploy the software easily and resolve customer installation and support requests remotely. Further, ISVs who deliver SaaS solutions using a major cloud PaaS/IaaS provider are able to take advantage of their global infrastructure and support to ensure higher performance and lower latency for end users as well as support for local data sovereignty and regulatory compliance requirements. Public cloud providers have invested significantly in infrastructure and services to meet the highest security and data standards; approximating this type of geographical infrastructure reach through global deployments and partnerships with hosters or co-location facilities is simply untenable for most ISVs.

Customer TCO is reduced as SaaS delivery model removes infrastructure complexity

In most cases, ISV customers realise significant savings in choosing a SaaS-based application due to reduced infrastructure costs. On-premises applications require customers to invest in a considerable amount of infrastructure to host software. Depending on the size of the company and the performance level of the application, these costs can easily spiral into the millions of dollars. On top of that, the customer has to continually invest in ongoing maintenance and support for these assets.

SaaS can free customers from the majority of these costs by taking on the responsibility for hosting software through a PaaS/IaaS partner. One ISV interviewed in this study who specialises in simulation software for engineering applications, described this as the primary benefit of SaaS. With an on-premises deployment, customers required substantial computational capacity to run advanced simulations such as stress tests for aeronautical designs. Each customer carried the cost of this infrastructure independently. After switching to a multi-tenant SaaS model,

“There are a few benefits of visualisation tools like PowerBI, which we use. We can build and publish reports extremely quickly, reducing the time between request and publication. It’s very visually appealing and the ability to filter data by clicking on elements is very nice. Exporting raw data to Excel is awesome.”

CEO, RETAIL POS ISV

the ISV was able to leverage the scale and efficiency of a public cloud provider’s infrastructure to offer equivalent or superior performance, saving customers up to 30% of their system costs.

SaaS ISVs can deliver new capabilities to customers through the cloud-based services

ISVs who migrated their software to a SaaS model were able to deliver a fuller set of features and capabilities than were possible with their traditional software. Advanced data analytics, business intelligence, visualisation and collaboration tools were capabilities companies added as they moved their software to the cloud. These services were incorporated either by integrating first-party services the cloud providers offer or by partnering with another SaaS company.

By rapidly incorporating this functionality into their product offerings, ISVs were able to augment their product capabilities without diverting resources from their product development teams. For instance, many of the ISVs included in this research indicated a strong customer demand for data analysis and visualisation tools. These capabilities can be very time consuming for an ISV to develop independently. Hence, nearly half of the software companies reported integrating these services into the SaaS product. Collaboration tools were another key area where ISVs sought to integrate cloud services offerings to meet customer demand. One quarter of ISVs deployed such services from their cloud provider or through a partner.

The ability to rapidly integrate and deploy composite applications expands the scope of what ISVs are able to deliver to their customers, thereby meeting customer requirements and allowing the ISV’s development team to focus on delivering new functionality core to the business.

Aggregation of data enables application performance improvements and new customer insights

A fourth driver of value creation is associated with data ISVs are able to collect. Data aggregated from across SaaS customers can identify inefficiencies in the product experience, causes of customer churn and unmet needs. As an example, a revenue management ISV interviewed described how they not only used customer data to improve the workflow in their application, but also to provide benchmarking services to their users. Usage data from the application showed the adoption of the pricing and quote tools by each sales team; the ISV was able to inform customers

how much additional revenue could be achieved if all teams fully utilised the software. The additional value created for the customer through these insights exceeded the annual cost of licensing the software several times over.

Perhaps more importantly, the data ISVs are able to aggregate across customers enables them to develop and optimise their algorithms at scale. Where ISVs might not have access to this data in an on-premises model, a multi-tenant SaaS model provides for these types of scale effects. One ISV focused on cancer detection realised especially significant gains from the data it collected from its customers. This ISV, serving speciality clinics and hospitals in the US, Europe and Asia, aggregated medical scans and clinical observations to improve the reliability of its cancer detection algorithm. Using the cloud, the company was able to increase the number of patients whose scans could be interpreted accurately by 10%. This dramatically cut down on hospital costs and improved patient outcomes.

SAAS ALLOWS ISVS TO EVOLVE THEIR VALUE CAPTURE AND PRICING STRATEGIES

SaaS changes the way ISVs produce value for their customers and it presents opportunities to evolve their monetisation potential. Over half (57%) of the ISVs interviewed introduced significant pricing changes as they moved to SaaS. SaaS pricing models varied from per user subscriptions to freemium to outcome-based pricing to sophisticated two-sided market models. Regardless of the pricing model chosen, SaaS presents a means for ISVs to closely align pricing to the value customers receive. Of the ISVs who reported changing pricing models, every one also reported an improved ability to capture net new revenue from heavy users that previously represented value left on the table in a traditional licensing model.

SaaS creates recurring revenue streams for ISVs and improves financial predictability

One of the primary benefits for ISVs switching to SaaS is a smoothing out of revenue streams as customers start paying on subscription or consumption plans. Traditionally licensed software vendors often struggle with 'lumpy' revenue streams, which can be hard to plan around or communicate to investors. Recurring revenue on the other hand is much easier to forecast, even considering customer turnover.

One caveat on this topic however; the initial transition can be difficult. Revenue recognition rules mean that ISVs will not be able to book the expected value of the contract up front, creating a short-term revenue reduction. As such, many ISVs planned the customer transition over 3-5 years to reduce the impact of changing from up-front sales to recurring payments on the business top line, only changing over 20-30% of customers over to SaaS each year.

SaaS value capture and pricing approaches align vendors with customer success

ISVs who switch to SaaS pricing models closely align their results with their customers' success. Vendors who price their software using value metrics that are aligned with how customers realise value from the software are better placed to grow and succeed than in an on-premises model, driving revenue growth as customers' increase usage.

Software that is priced in alignment with the way that customers realise value is much easier for customers to justify purchasing. The nature of flexible SaaS pricing is such that if the software delivers value to customers, they will use more of it. This is one of the most significant changes in the dynamic between ISVs and customers under SaaS. In a traditional model, customers considering purchasing a perpetual licence were forced to consider if they would use software enough to justify the licence fee. In a SaaS model, customers of all sizes can adopt software and use it to the appropriate extent for their needs. Customer size and preferences should influence the pricing model; ISVs reported that enterprises preferred pricing models that provided predictability (e.g. subscription or user-based models), while smaller customers valued the flexibility that comes with usage-based pricing.

ISVs who take advantage of this change are able to unlock substantial value from heavy users that would be left uncaptured in a traditional licensing model, as well as adding new customers who would not use software enough to justify a full licence purchase. SaaS pricing models also simplify the process for customers who wish to add new users, workloads or features, reducing chances for drop-off or competitor evaluation.

A learning management ISV used its move to SaaS to evolve its pricing strategy and realise more value. Their software hosts learning content, such as videos and presentations of lectures, as well as supporting interactive features like quizzes and assignments. When they switched to a SaaS model, their pricing team ran hundreds of analyses on possible pricing

models using customer data to assess a range of outcomes using different pricing metrics, costs per metric and usage. This process helped them understand which customer segments drove the majority of their results and clarified how the model needed to work in the future. They landed on a hybrid model that combined a subscription fee and a flat content delivery fee. The subscription fee was based on the total number of clients and expected churn, while the flat percentage delivery fee distinguished between light and heavy users, a model that reflected how its customers used their software to generate value and priced it in a way that made it easier for them to expand and grow usage and revenue.

Operating model impacts

“What were the benefits of SaaS? We can provide greater quality solutions faster, avoid fighting over versioning, provide targeted add-ons for users and manage our deployments better”

VP PRODUCT DEVELOPMENT,
AUDIO/VIDEOCONFERENCING ISV

“We’ve seen a huge improvement in our product development efficiency - it’s been the core benefit for us in transitioning to SaaS”

VP PRODUCT MARKETING,
IT OPS ISV

ISVs migrating to SaaS achieved multiple benefits in their Operating Model. That is, the processes and capabilities ISVs have to develop, launch and support their products and services. While SaaS improves how ISVs are able to deliver and capture value, the impacts are equally significant in internal operations.

APPLICATION DATA COLLECTION PROVIDES DETAILED INSIGHT INTO PRODUCT USE, IMPROVING THE PACE AND RELEVANCE OF PRODUCT DEVELOPMENT CYCLES

One of the most transformative aspects of the shift to SaaS is the requisite change in product development and engineering cycles. On the product side, the change to an integrated, Agile-based methodology drives an increase of up to 33% in product development speed, assisted by greater integration with engineering and R&D functions. Additionally, the decisions made in product development can be guided by data collected from users on a SaaS platform - data that was previously challenging for product teams to obtain.

Platform data collection improves pace of product development

All of the ISVs interviewed explained that the combination of continuous product development methodologies and greater visibility into customer usage through app data collection has led to improved product development cycles, saving up to one-third of the time required for a typical product release. ISVs who use continuous integration and continuous deployment (CI/CD) methods are able to plan a more structured product update cycle for their customers. In fact, the shift to Agile led several interviewed ISVs to note that now they are able to release product updates faster - ISVs have moved to a monthly or quarterly release cycle in place of the conventional 12-18 month cycle.

“We’ve migrated +800 of our databases to a mixture of standard and premium elastic pools which allow us to offer tiered performance and pricing options to our customers. Since the migration, we’ve closed two datacentres. SQL Database brings huge cost savings to us in the long run – in the 2016 financial year alone, the adoption of elastic pools will save us a quarter of a million dollars.”

VP TECHNOLOGY, PROCUREMENT
AND SUPPLY CHAIN ISV

SaaS allows for a more iterative development approach with in-market experimentation

Alongside faster product development cycles and more rapid product releases, half of ISVs reported that the SaaS model permitted them to do more in-market experimentation to guide development and obtain customer feedback. Through experimentation and A/B testing, engineers are able to tune the implementation of features to improve the customer experience and engagement.

An IT Ops ISV reported cutting its product development cycle time by 50% by testing out new features on subsets of customers and monitoring usage data. Their design teams prioritised product roadmaps in accordance with the results of these experiments, focusing development effort on features that survived customer testing in the real world.

UNIFIED INFRASTRUCTURE REDUCED SERVICE AND MAINTENANCE NEEDS, IMPROVING ENGINEERING EFFICIENCY BY 26% ON AVERAGE

Unified infrastructure streamlines development, testing and support activities

One of the single biggest benefits of shifting to SaaS delivery is the reduction of variety and complexity of customer hardware and infrastructure into a single, unified infrastructure for application deployment. Across an ISV’s on-premises customer base, there can be a wide array of combinations of hardware, operating systems, installed versions and supporting software. Even worse, the customer infrastructure may be spread across multiple client locations and managed by different teams. When a service issue arises, ISV support teams have to identify a huge range of potential factors linked to all the unique attributes of that single installation.

Setting aside the challenge of identifying the cause of a service issue in a customer-managed environment, just getting access to the customer’s facilities can be a significant challenge. ISV support teams need to find the right location, travel, get on-site access and then set about the task of identifying and rectifying the problem. In contrast, a multi-tenant SaaS environment is a single installation on a single infrastructure stack. As a result, engineering teams no longer have to worry about multiple dev and test environments or build management for deployments and have to manage fewer releases. Additionally, the shift to a DevOps model creates

“SaaS increases the speed and ease of deployment; you don’t need a separate install and configuration for each customer. You eliminate enough stuff to fill a 500-page book”

VP PLATFORM,
MARKETING AUTOMATION ISV

“We have a mix of developers around the world and we use Microsoft Visual Studio to manage code and deploy – being able to do this work remotely is very helpful for our costs and flexibility.”

CEO, RETAIL POS

a closer link between engineering and user experience and operability, brought about by the reduction in back-end maintenance work.

Deployment of updates is simpler and faster

Deployment of updates or new features is much easier and faster. Separate installation and configuration for each customer is no longer necessary. A single update to the SaaS installation takes care of all customers simultaneously. Similarly, when performance issues are identified, engineers can easily diagnose and resolve problems by accessing the customer environment, potentially resolving issues in minutes. As bug fixes or performance improvements are identified, they can be rolled out to all customers simultaneously, relieving pressure on service organisations who might otherwise have to field dozens of calls about the same issue.

DevOps model and reduced maintenance and version management needs let developers focus on the customer

The transition to SaaS gives developers new tools and techniques that allow them to focus their engineering teams on higher value activities related to the product itself, rather than on activities to maintain infrastructure. The impact of CI/CD methodologies was noted as having a positive impact on engineering efficiency alongside the impact on product development. The impact on engineering is primarily due to the reduction of time spent testing and fixing errors, thanks to the rapid cycle of testing and deployment and the use of automated testing tools.

Other engineering benefits came from the unification of disparate customer environments into a single multi-tenant installation. Reducing the need for regression testing with automated testing, for example, was consistently identified as a major source of time savings for engineering departments at ISVs who transitioned to SaaS. Similarly, DevOps teams are able to monitor all customer environments that run on the same IaaS platform via platform dashboards, rather than managing multiple deployments in different locations.

Finally, the switch to a public cloud-based infrastructure let ISVs more easily handle the seasonality of customer demand. Public cloud infrastructure is able to scale to match peak loads at an optimal cost, saving ISVs the cost and challenge of building out hosting infrastructure to handle expected peaks and unforeseen spikes in usage.

The net effect of these factors is a significant resource savings in the engineering costs of ISVs who switch to SaaS. ISVs reported a range of efficiency gains depending on the complexity of the application and the ongoing maintenance responsibilities, with an average of a 26% improvement in engineering efficiency.

SALES PROCESS IS SHORTENED THROUGH TRIAL AND BETTER ENGAGEMENT WITH END USERS

ISVs reported that while new SaaS software often solved the same technical or business problems, the sales and marketing approaches, targets and compensation changed dramatically to reflect the new model and business approaches. Interviewed ISVs described changes that required redefinition of sales and marketing training, metrics and compensation, affected the channels through which they went to market and the sales cycle.

Business owners are now purchasers, allowing ISVs to focus more on user experience and business need

The purchaser of SaaS products is typically the end user or business owner, rather than the IT department, as is common in traditional sales. In the past, sales leads generally spoke with customer IT leaders to discuss the cost of licences, the required infrastructure and maintenance needs and the integration with other software that the customer used.

Now, sales teams are able to communicate the value provided by the software to the end users who are increasingly becoming the purchaser of SaaS applications (or at least becoming more influential over the final decision). Frequently, end users are driving sales decisions, allowing SaaS vendors to differentiate themselves relative to on-premises solutions that have less compelling user experience and performance characteristics.

This does require some changes in how sales and marketing efforts communicate the value provided by software to potential customers. Sales and marketing activities that previously focused on IT departments and the overall cost, maintainability and integration need to adapt to a different mind-set held by business owners. The end user of the software is primarily interested in the product usability and business use case and may not have the technical background that sales teams are used to dealing with. Interviewed ISVs described building out new sales materials that targeted end users as well as adapting existing sales materials aimed at IT decision makers. This took multiple forms, such as new documentation and literature that extolled the business benefits and key value points. It also

“We want to be in the marketplace. It’s a good way to support demonstrations and generate leads independently. It also shows that you’re committed to a platform – our solution is in the marketplace and natively compatible with Microsoft Dynamics, which shows we’re serious.”

VP CUSTOMER VALUE,
REVENUE MANAGEMENT ISV

included taking advantage of the ease of access presented by SaaS to add self-service demonstrations or on-site trials as part of the sales process, allowing end users to test and understand the software.

Sales cycles are shorter thanks to simplicity of trial and demonstration

ISVs reported that the complexity and complications that came with trying to demonstrate software for potential clients was frequently an impediment to sales in a traditional delivery model. Setting up a demonstration often requires prior access to potential client infrastructure through local IT teams, arranging time for engineers to set up and prepare a demonstration environment and then removing the installation after the demo. Demonstration becomes much simpler in a SaaS environment. Sales teams can quickly display a demonstration environment with minimal configuration at short notice (including potentially on a mobile device). Potential clients can test out the software immediately and explore how it may work to solve their needs. ISVs also noted the value of showcasing their software in cloud marketplaces, enhancing discoverability.

Customer-facing teams can take advantage of this ability to demonstrate software easily to drive additional usage by engaging with customers to offer guidance on how to make the most of the software. ISVs who reported a successful transition described adjusting their compensation models to reflect this by rewarding sales teams for landing net new usage contracts and rewarding customer support and success teams for expansion of existing contracts.

Successful SaaS ISVs take advantage of reseller networks to drive active usage

ISVs that previously relied on resellers for lead generation, sales and support found that the shift to SaaS dramatically changed their interactions with these partners. SaaS uses a much more direct pattern, and at its most extreme, sales that previously came through a network of resellers happen directly with customers through self-service web portals, changing the entire sales cycle and the players involved. However, this does not mean that resellers become irrelevant following a shift to SaaS.

Interviewees highlighted efforts both at their own companies and at other ISVs that they see as successful to work with resellers to refine their role in the sales and marketing cycle. The ISVs described as the most advanced in this aspect were those that help to transition their resale partners into a network of managed service providers. These partners offer

Preparing for the transition to SaaS

their customers managed IT solutions that include the SaaS product. By engaging resellers into the SaaS model, these ISVs are maintaining the reach of the partner network and co-opting the relationships those partners have with end users to drive more usage. Compensating partners for this type of resale is more complex than in an on-premises model, but interviewees explained that time-bound referral fees (e.g. payable once customers had been in place for 6 months) or revenue share agreements both worked to incentivise partners to drive ongoing active usage with customers.

The software marketplace is changing dramatically as more software companies shift to SaaS. ISVs who have not made the transition to SaaS should plan to adapt their business models to reflect these changes, enabling them to sell their software more broadly and better monetise the value of their IP. When preparing for this change, ISVs need to consider a few immediate actions.

First, ISVs should plan out the business model changes to support a SaaS model

- **Pick complementary products or features to develop for SaaS:** Select a narrow focus for the first SaaS product to avoid cannibalisation of existing product lines and maintain a manageable technical scope for the first deployment.
- **Deploy to a subset of customers to get market feedback:** Think about the customers who will be most willing and able to try out a SaaS version. Deploying to a small set of willing customers creates the opportunity to test out the process and get customer feedback without committing the entire organisation to a transition. Be ready to capture the data and feedback gathered from customers, since it will likely guide the next evolution of your SaaS model.
- **Be prepared to experiment on pricing and value capture models:** There is a great variety of SaaS pricing options that ISVs can implement and the choice can be daunting. ISVs reported that they made ongoing changes to their pricing and value capture models as customers became more familiar with SaaS and as they added new features.

- **Consider new features that could improve customer value:** The transition to SaaS opens up the opportunity to integrate services from public cloud platforms and their ecosystems. ISVs should evaluate where those services provide better performance or offer new capabilities, such as collaboration tools, that solve customer pain points and understand how to integrate them into a SaaS offering.

Second, ISVs should prepare internally for the changes in operations that are required to support a SaaS model

- **Be ready to evangelise usage through customer facing teams:** Success in a SaaS model is driven by active customer usage. ISVs preparing for the transition to SaaS need to incentivise sales and customer support teams to drive usage, rather than closing deals or support tickets. Each customer interaction becomes an opportunity to expand the customer's understanding of what is possible and drive incremental usage. Trial programmes should be as low-friction as possible, whether self-service or initiated through contact with sales, to allow potential customers to experience the full range of value enabled by software.
- **Identify resellers that have customer knowledge and access:** In the transition to SaaS, resellers of traditionally licensed software may appear to be less important partners and therefore overlooked as a resource. However, resellers often have deep customer understanding and reach. ISVs should consider instead working with resellers as cloud partners, focusing them on identifying new customer opportunities and driving usage with existing users. ISVs can transition these partners from cost-plus resellers to value share partners.
- **Prepare for engineering teams to increase focus on product development:** As ISVs adopt a DevOps model to support SaaS development, they should prepare to allocate a greater proportion of engineering resources to product development challenges while reducing traditional engineering responsibilities for release management, systems administration and QA.

“We selected Azure because it met all our criteria, from manageability and scalability to familiarity and cost-effectiveness. Each Azure VM environment has its own Azure SQL Database instance, with all the instances in elastic database pools. By separating databases between development, staging and live environments, we can offer our customers robust performance isolation matched to scale – a huge win.”

TECHNICAL LEAD,
CONTENT MANAGEMENT SYSTEM ISV

• **Identify cloud partners who can support SaaS transition and growth:**

As ISVs prepare for SaaS, it is important to select a cloud platform that can be a partner in growth. First, ISVs should consider the infrastructure performance of a partner, starting with essential cloud services such as compute and storage, as well as geographic reach and security and reliability, since customers frequently consider the cloud platform SaaS applications run on as part of their vendor selection process. Second, ISVs should explore the value added services provided by a cloud platform. This extends beyond the core cloud services into areas like advanced data analytics, BI and visualisation, and communication and collaboration tools. ISVs should also consider the breadth of services available from other SaaS vendors in the platform ecosystem that could facilitate the development and performance of their software. Finally, a good platform partner should offer go-to-market support. This can include access to their network of sellers and cloud partners who can package an ISV’s software as part of a solution to other customers on the platform, support for lead generation through marketplace promotion and access to a wide range of enterprise customers.

Methodology

Keystone interviewed 20 senior executives at leading software companies who have experience in making the transition from a traditionally licensed, on-premises software model to a SaaS model hosted on Infrastructure- or Platform-as-a-Service cloud platforms. Interviewees were technical and business leaders in senior decision making roles. Their responsibilities include overseeing product development, sales and marketing, business development and corporate strategy.

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¹Gartner, "Forecast: Public Cloud Services, Worldwide, 2013-2019, 4Q15 Update", 25th January, 2016

²Flexera, "Software Licensing 2016: Seismic Shifts - Shaky Foundations", 26th July, 2016

³Bessemer Venture Partners, "State of the Cloud Report 2016", 7th September, 2016

⁴Ibid