Partner of the Future

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For over 30 years, the technology industry has created opportunities for channel partners to develop and implement IT solutions to help solve their customers’ needs.

But the IT industry is going through a dramatic change, and VARs, MSPs, SIs, ISVs, and other channels are being asked to bring new capabilities to their customers.

Part of the reason for this change is the advent of the 3rd Platform, which is underpinned by four key technologies: cloud, mobile, Big Data analytics, and social.

Cloud, in particular, has a disruptive impact forcing change in channel business models. When compared with on-premise solutions, cloud typically has a much lower upfront cost, quicker implementation cycle and is billed on a subscription basis. Because of its scaleability and flexibility, cloud has become fundamental to digital transformation, and its importance as a delivery platform, is rising exponentially as digital momentum grows. The digital transformation era is accelerating the impact cloud has on channel business models. This impact, and the changes it necessitates, will be covered in this InfoBrief.
Cloud at the Center of Industry Growth

Software revenue growth rate through 2017

- Higher cloud SW growth vs packaged SW

5.5x

The software cloud market will reach over $76 billion in 2017. Packaged on-premise software is expected to grow at a CAGR of 4.1% from 2013 to 2017, and the cloud software market at a CAGR of 22%. That means cloud software spending growth is over 5.5x that of packaged software.

Key software trends

- Customers are purchasing services, not servers, and using SaaS to extend or replace existing applications

- Predicted cloud software market size by 2017: $76.1B

- Cloud software market CAGR through 2017: 22%

- More cloud ISVs (CSVs) by 2017: 2.5x

- Of all software, services, and technology spending will be cloud based by 2020: 60-70%

- 10x more discrete “software” services available in 2017

Source: IDC CloudView Survey 2015, Public Cloud Tracker, other IDC resources
Becoming a Partner of the Future

To grow, to remain relevant to customers, and to remain profitable, IT channels (in all their forms) will have to master a number of business model transformations in the cloud and digital transformation era. IDC has developed a framework of key transformations that IT channels will need to address to be successful in the future – in effect, to become a partner of the future.

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The What

Technology — from 2nd Platform to 3rd Platform:
- All market growth is in 3rd Platform technologies.
- The 3rd Platform will grow at a CAGR of 12.7% from 2015 to 2020, versus a CAGR of -4.8% for 2nd Platform technologies.
- Basically this means that channel partners that remain in the 2nd Platform will be competing for market share in a declining market.

Focus — from broad to specialized:
- Customers want their IT partners to provide them with specialist skills and knowledge that they don’t have themselves, it is also becoming easier for customers to source specialist partners online, and the traditional physical restrictions of location are no longer an issue in the cloud world.
- Channels need to differentiate themselves by understanding a technology area, an industry, or a business process very well. These partners will be recommended by their clients and, most importantly, they will be able to command a premium for their deep capabilities.

Activities — from resell to services and building intellectual property:
- Margin pressure and the industry’s move to new models around cloud and managed services mean channels are moving away from purely reselling hardware and software in favor of providing more margin-rich services.
- As channel partners move up the services stack, so does profitability increase. From resell to professional services, to more automated managed services.
- The next stage in this evolution involves building intellectual property and monetizing a very repeatable type of business, either through homegrown applications and/or software that enhances or enables a solution.
The Who

Customer — from IT to business and IT:
- Channels will need to focus on building the skills in selling business outcomes to these business buyers, while retaining a strong relationship with the IT department.
- This involves either training existing sales people in the art of selling to business or hiring in net new skills from either line of business and training them in the art of technology sales.

Competition — from traditional to non-traditional:
- There is a slew of new “born in the cloud” startups and developers beginning to compete with traditional IT companies. They typically have none of the legacy and boundaries that traditional IT companies are challenged by. There also unconventional influencers emerging from the business community. Examples include digital agencies, accounting firms, management consultants and start-ups that are increasingly influencing their clients’ technology decisions.
- With the advent of cloud, we are also seeing a number of industries start to merge technology with their IP and become IT providers in their own right. There are a number of examples from industries as diverse as financial services, manufacturing, and life sciences, which are developing and selling their own industrialized IT solutions.

Alliances — from do-it-ourselves to collaboration:
- Closely linked to the need to specialize is the need to create more structured alliances. It is becoming increasingly difficult to be “all things to all people,” and partnering with other IT companies is one way of developing more holistic solutions. IDC research has also shown that there is a strong correlation between companies that do a lot of partnering and better business performance.

In 2015, IDC predicted that IT spending by groups outside of IT departments would grow at over 6% a year – almost 2.5x the rate of the IT department – led by marketing, customer service, and sales groups.
The How

Sales motion — from deal to relationship:
- In cloud subscription deals, there is no revenue at the point of transaction. Channels therefore need to restructure their sales organizations to move away from upfront “deals” to focusing on long-term customer relationships.
- Some companies have formed “customers for life” organizations or have created the roles of adoption consultants or customer success managers to put the focus on this new dynamic.

Time horizon — from short term to long term:
- Related to the above is the need to have a much longer-term outlook. In a subscription-based “as-a-service” world, channels will have to shift from a short-term, quarter-by-quarter outlook to a much longer-term, three-to-five-year outlook with retention driven sales structures.

Marketing — from traditional to digital:
- Customers are self-educating (online) and never has it been more important for channels to invest in the right content online.
- Forward-thinking channels are investing in digital marketing, and especially in digital content. They are focusing their efforts on things like search engine optimization, pay-per-click ads, banners, videos, webinars, white papers, blogs, social media, and landing pages.

Source: IDC’s Future-Readiness Enterprise Study | June 2015
Channels Are Active in Cloud, But Business Impact Concerns Are High

Of all the 3rd Platform technologies, cloud is the most popular, with 64% of software channels already selling some kind of cloud solution.

But there are those that are not … and the reason given is that they are challenged by the impact it has on their business model, particularly in terms of potential revenue loss.

Reasons for not offering cloud solutions:
- It doesn’t fit with our business model: 54%
- There is not enough customer demand: 17%
- Not financially viable for us: 8%
- We don’t have the IT skills to implement private cloud or manage public cloud services: 7%
- Immaturity of cloud: it is a new technology: 4%
- Difficulty in switching from project revenue to a recurring revenue model: 3%
- Customer concerns about security: 2%

Source: IDC Software Channels Survey, Fall 2014, n = 603
Can a Cloud Business Be Profitable for Channels?

Building a cloud business requires careful planning. Moving too fast can impact cash flow, but not moving at all can impact growth and new business. However, a successful cloud business can help your business to build more predictable, recurring revenue streams, augment recurring revenue streams from managed services, open doors to new customers, enable you to extract higher revenue per employee, and create a number of upsell opportunities.

Although most channels acknowledge the momentum and growth in cloud, many are concerned about the impact cloud will have on their business — particularly in terms of revenue growth and the impact moving to a recurring revenue model has on cash flow.

Resellers are often hit the hardest, as larger upfront license deals are replaced by smaller, recurring revenue cloud deals with either a referral fee and/or smaller resell margin.

While loss of topline revenue is often a big inhibitor for cloud, partners that have successfully made the transition report a number of benefits, including:

- More predictable, recurring revenue stream
- Quicker sales cycles
- Higher revenue per employee
- Higher gross profit
- Higher new customer acquisition
- Faster growth
- More upsell opportunity
- Geographic expansion without the physical restrictions of the on-premise world
Essential Guidance: Making Money from Cloud

Look at ways to replace revenue: Revenue generated by resale will decline over time. Resale could turn into referral, hardware sales to cloud. Proactively replacing lost revenue is critical.

- **Cloud** typically has a lower upfront cost-of-sale, and should be **used as a door-opener** for other solutions and services. Typical upsell opportunities include security, mobile device management, managed services, and network and other optimization services. Look at ways of bundling SaaS with your own IP and create new products and homegrown solutions.

- **Building a portfolio of services** wrapped around your cloud business can be lucrative and make it easier for your sales people to upsell. Create a portfolio of targeted business consulting services, training and adoption services, managed services, and, importantly, integration services.

- **Lead with cloud** but maintain expertise and skills in **on-premise**. Few, if any, customers will move 100% to cloud; in reality, most customers will have a mixed environment of both on-premise and cloud. Integrating and managing this **hybrid** environment is really the sweet spot for the channel and provides significant value to your customers.

Optimize delivery and sales operations: doing more with less in a repeatable manner is critical in a recurring revenue model.

- **Optimizing sales operations**: Customer retention and scale are the key. Prioritize doing more deals by investing in strong inside sales and telesales capabilities, and combine this with outbound demand generation activities. Focus your investments online to create a sales operation that is higher volume and lower touch.

- **Optimize incentive structures**: Revising incentive structures is a sensitive process and requires careful planning. It is also advisable to ensure incentives are in place for repeat business. Consider commission models that provide a percentage of the first year’s revenue upfront, with a percentage paid on recurring revenue in the second year.

- **Optimize delivery**: SaaS implementations are often less complex than on-premise, and building repeatability and automation into delivery is key to success. Consider fixed-fee implementations using less expensive staff and reallocating more expensive resources to higher-margin services.
Call to Action

1. Prioritize – pick one or two transformations to action within the next 3-6 months, another two over the next 6-12 months and so on.
2. Specialize: pick one or more industry and/or horizontal solution to develop deep expertise in.
3. Scale: create efficient sales and delivery mechanisms, invest in digital marketing, and focus on prospecting online.
4. Replace lost revenue with higher-margin services. Look to replicate your solutions and try to productize your IP to create new revenue streams.
5. Train or hire employees in the art of selling to line of business.