

Focus Point**Authors**

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SAP Business ByDesign: Tentative Steps Forward

Springboard Perspective

BACKGROUND

Representing the company's first fully on-demand ERP suite, SAP Business ByDesign was launched to much fanfare in September 2007. After an initially tentative embrace of the software-as-a-service (SaaS) model, SAP began aggressively pushing its SaaS offering on a global basis and immediately began extending its software-as-a-service (SaaS) rollout across the world throughout the first quarter of 2008.

However, the initiative received a setback with SAP's April 30, 2008 announcement to financial analysts that SAP had elected to modify its SAP Business ByDesign rollout strategy to 'ensure a more focused and controlled ramp-up process,' <http://www.sap.com/about/investor/press.epx?pressID=9406>.

In particular, SAP announced that it was immediately cutting 100 million Euros in Business ByDesign 'accelerated' investments for 2008 and was not planning any future accelerated investments specifically targeted towards Business ByDesign. Instead, all future SAP Business ByDesign-related expenses are to be funded out of SAP's normal operational business.

In explaining this shift in strategy, SAP cited a need to address problems of scalability and a desire to incorporate more functionality into the product before making a more aggressive global launch sometime during 2009. While the above explanation is certainly valid, Springboard Research believes a more likely explanation is that SAP feared a cannibalization of software license sales coupled with a short-term negative impact on operating margins as customers and prospects gravitated towards a subscription model. In fact, as part of the announcement SAP specifically highlighted the positive impact this funding decision will have on operating margin expansion for the remainder of 2008.

Despite these significant shifts in strategy and approach, we believe SAP Business ByDesign is still a core part of SAP's strategic direction and overall product/solution

portfolio. The ongoing (albeit more conservative) SAP Business ByDesign rollout (availability in India was announced on June 4, 2008), is a significant development for SAP, the SaaS market and small and medium-sized business (SMB) customers.

SAP's challenges in this space highlight the increasingly aggressive posture of traditional enterprise application vendors in the SaaS market while also illustrating the difficulties these vendors face in straddling both on-premise and SaaS business models. For SMB customers with limited in-house IT capabilities, SAP Business ByDesign offers a comprehensive hosted application suite to consider as a means to automate business processes more effectively.

This document briefly outlines the SAP Business ByDesign offering at a high level and explains Springboard's evaluation of the offering. Our perspectives of what this launch means for the SaaS marketplace are also shared, as well as some key areas we will be monitoring as the offering is sold to the market throughout 2008.

SAP BUSINESS BYDESIGN – HIGHLIGHTS

SAP Business ByDesign is a full-fledged SaaS offering targeting the SMB market. Based on SAP's estimates, it is targeting a US\$15 billion market with the Business ByDesign product on a global basis. Some of the "sweet spots" for this product according to SAP are customers with 100 to 500 employees, who have fast-growing businesses and lack integrated ERP solutions as well as those struggling to support applications in-house adequately from a technology and staffing perspective.

Key elements of the Business ByDesign offering are:

- Fully hosted SaaS enterprise application
- Comprehensive bundled offering with financial management, HR, CRM, SCM, SRM, project management, compliance management and executive management support that looks to provide role-based functionality instead of just point applications
- A dedicated website with free trials to customers
- A solution targeted at both business and technology users
- Priced at US\$149 per user a month with a minimum of 25 users, an extension to the base modules is available including manufacturing and warehouse management starting at US\$34 per month.
- A scaled-back offering of US\$54 per user a month is offered for five users, but it excludes an overwhelming majority of applications and features.

Additional details on the SAP Business ByDesign product specifications and pricing can be found at: <http://www.sap.com/solutions/sme/businessbydesign/index.epx>

PRODUCT PERSPECTIVES

Springboard believes that by any measure, this offering is a significant and comprehensive one. In addition to considerable R&D put into the product, (and despite the setbacks highlighted above), SAP has invested heavily in go-to-market elements such as marketing, education and partnering efforts to ensure the rollout is a success.

Product Strengths

We believe key product strengths are:

Comprehensive Bundle – The Business ByDesign offering is unique from other SaaS offerings we have evaluated due to the amount of applications bundled into one product. Whereas most SaaS products focus on one application area – such as CRM, the SaaS pioneer – this product provides a comprehensive suite that solves a number of business problems in one package.

Integration & Interoperability – Due to the fact that so many different applications are bundled in one offering, the interoperability between applications is reasonably straightforward, freeing organizations from handling a number of integration issues. SAP Business ByDesign is developed on the SAP NetWeaver platform, and leverages that platform’s SOA capabilities.

Free Trial & Online Tools – The option to configure and try the applications online for free before deciding to buy is a key product strength and point of value for customers. SAP leverages the web for configurations and provides an excellent website for experimentation and information. We believe this component of the offering is done elegantly and better than many other competitive SaaS offerings.

Ease of Implementation and Manageability – Although not unique to this product alone, faster implementations enabled by SaaS and eased manageability for companies struggling to maintain capable and affordable in-house IT teams are key product strengths. Similarly, ease of implementation across a number of offices is another strength often overlooked when considering SaaS applications such as Business ByDesign.

Product Weaknesses

Although we perceive the product to be a strong one, areas we believe could be improved are provided below:

Lack of Modularity – While offering a comprehensive application bundle has its strengths, it is a double-edged sword. For users unready for such a comprehensive bundle of applications, the offering can appear daunting to implement and leverage. Without the ability to buy standalone application components, SMBs looking to implement one application for a business requirement – which is where we have seen most business executives adopt SaaS without IT department involvement – may turn to other SaaS offerings.

Pricing – Although a competitive price point on a per application basis, US\$149 per user per month for Business ByDesign with a minimum of 25 users amounts to a minimum of US\$44,700 for any organization. For much of the price-sensitive SMB market, this will be a difficult price point for reaching a mainstream market in our view. As such, we see this price point having more success in the upper mid market.

Usability and Interface – We believe that the usability and visual elements are improved compared to traditional SAP on-premise applications, but still behind SaaS vendors that have built applications from the ground-up and honed them over the past 3-5 years with the SaaS delivery model in mind.

MARKET IMPLICATIONS

As our previous forecasts and market reviews have shown, the SaaS market is experiencing a rapid phase of growth and gaining acceptance quickly. Our forecasts expect SaaS applications to continue gaining share at the expense of on-premise software over the next five years at a minimum.

SAP's Business ByDesign release is a further validation of the SaaS market's potential and viability. SAP dipped its toe into the SaaS waters tentatively in the past, but has realized it must take the SaaS opportunity more seriously, which it has done with SAP Business ByDesign. This launch will only serve to further boost the SaaS market as one of the world's strongest software companies invests millions of dollars in SaaS product R&D, channel development and market education.

We are particularly interested in observing Business ByDesign over the next 2 years in the following areas:

Channel Development – One key hurdle we see for the SaaS market reaching the next level is the development of the channel. Lack of a volume channel to sell SaaS offerings will negatively impact overall market growth. SAP is working closely with partners to develop the market for SAP Business ByDesign, and organizations should closely monitor the company’s ability to balance on-premise and SaaS channel programs in the future. If the model is successful, this can be a key strength for SAP versus net-native SaaS providers.

Financial and Business Model Impact – Traditional software providers like SAP have been reluctant to fully embrace SaaS in the past because it raises a number of difficult questions regarding the evolution of their existing business models and profit sources. In fact, we believe that managing this difficult evolution lies at the heart of SAP’s decision to execute a more conservative, controlled rollout of SAP Business ByDesign. Organizations should continue to monitor SAP’s financial results as this will provide valuable insights into how aggressively traditional software companies can transition to SaaS business models and in particular, how strategic SAP Business ByDesign will be to the company’s overall business model.

SAP’s SaaS Commitment – Transitioning – however little or slowly – to a SaaS delivery model is no small undertaking and we do not anticipate groundbreaking success for this rollout immediately. As such, we will be watching SAP’s commitment to developing robust SaaS offerings over the long term.

Application Modularity – We believe if SAP decoupled some components of the Business ByDesign suite and allowed users to buy singular components the rollout would generate quicker growth (integration and end-to-end tradeoffs notwithstanding). Monitoring this willingness will provide important indications in the longer term.

CONCLUSION

SAP’s Business ByDesign offering is a serious and competitive SaaS product. Nonetheless, we expect the company to struggle as it transitions from on-premise to SaaS models. Recent announcements highlight the very significant growing pains associated with this evolution from a traditional on-premise software licensing model to a mixed model that includes off-premise, subscription-based offerings. SAP’s inconsistency in terms of its

global, SaaS-related strategy will also aid competitors seeking to cast doubt on the company's strategic commitment to the SaaS market. Nonetheless, SAP is still in a position to succeed in this space and organizations in China and India considering SaaS solutions should include SAP Business ByDesign in any product/vendor evaluation process.

SAP Business ByDesign is a solid first step in a journey that will take time to bear fruit and generate substantial revenues. Although a strong offering with good long-term potential, we believe product modularity, pricing and usability are areas that can be improved.

In the final analysis, despite some obvious setbacks, we believe the SAP Business ByDesign launch is good for SAP, the SaaS market and end-users. Adding greater choice and competitiveness to the SaaS marketplace will make SaaS applications better and more affordable in the long run and help drive new enhancements and innovations, which will continue to propel the global SaaS market forward.

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