

Why Private Software Companies Grow Better in the Cloud



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In the software industry, the characteristic of vision often separates the also-rans from the winners. By “vision,” I mean visualizing a broad roadmap your company follows and adapts in pursuit of its strategic objectives. This vision covers virtually every aspect of the business—the products you deliver, the customer needs you meet and, importantly, the technologies you choose to run your financials as well as CRM, sales and order management, and more. Financial and business management choices made early in the maturation of a private software company can profoundly influence its fortunes in the years that follow. Let me offer an example.

QuickBooks is a reasonable choice for a 10-person software startup to use to manage its books. It generally supplies the functionality a company of that size needs and offers some room for expansion. But with growth, the company will need to manage more complex financial processes such as recurring subscription-based revenues, revenue forecasting and specialized pricing models. As the customer base grows, so does billing complexity. Other needs arise for sales and lead management, CRM, marketing, and support for personnel in, say, the United Kingdom and India with multi-currency consolidation and global roll-up.

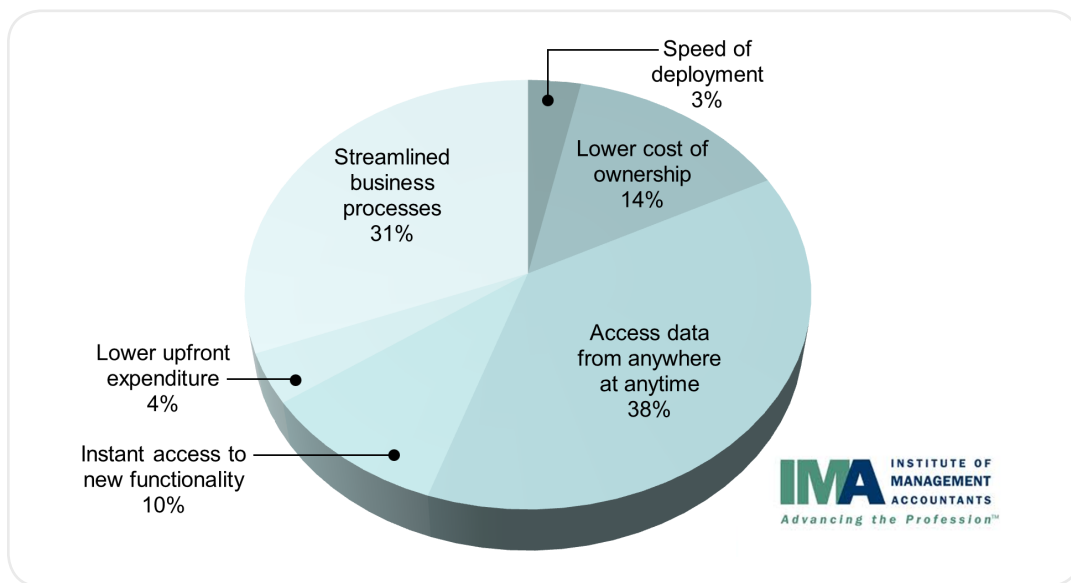
To meet each of these incremental needs, it may seem expedient to deploy standalone applications, and customize spreadsheets to email back and forth around the globe. But as growth continues, these un-integrated processes and ad-hoc applications can begin to hinder performance and sap productivity. Staffers are forced to re-key data from one system into another. The company begins to wonder if it's time to deploy, say, SAP or Oracle ERP... but can it afford the multimillion-dollar cost and an eight-month implementation of an on-premise system? Even if it does manage to get the system implemented, can a company going through a high-growth period afford to devote resources towards a static system that is painful to maintain and expensive to upgrade? In most cases, the answer will be no. The alternative to A) a hairball of unintegrated applications or B) a multimillion-dollar on-premise ERP system is simple—cloud-based business management.

Five Reasons for Private Software Companies to Consider the Cloud

Usage of cloud computing continues to grow briskly around the world. According to IDC, the Software-as-a-Service (SaaS) delivery model is set to grow six times faster than the overall software market. I suspect the growth rate for cloud solutions is even higher among software companies, given the impressive adoption we've seen of NetSuite's cloud-based ERP/financials suite among software companies. At last count, more than 750 software companies—including RightNow Technologies, LogMeIn Inc., SuccessFactors, CA Technologies and SolarWinds—use NetSuite.

Of course, NetSuite uses NetSuite. We run all of our business applications in the cloud, through a web browser—tracking a sales opportunity to sales order, through to invoicing and revenue recognition, and from management reporting and generating GAAP financial statements—on the same technical infrastructure we provide to our customers. The impact on finance and our broader organization has been profound—and a sharp contrast to software companies where I've worked that ran traditional financial applications such as Oracle Financials, SAP R/3, or Microsoft Dynamics.

Five key reasons prompt software companies to adopt cloud-based ERP/financials—1) access to data for visibility and mobility 2) better cash efficiency and lower cost 3) faster deployment and decision-making 4) ability to focus on innovation and 5) to better manage recurring revenue from contracts and subscriptions. Several of these were cited as key benefits of cloud-based financials in a recent survey of about 800 finance professionals that NetSuite conducted with the Institute of Management Accountants (IMA). Though that survey spanned multiple verticals, several of its findings (shown in the chart below) are relevant to private software companies.



Productivity Benefits Cited as Key Drivers for Cloud ERP

“The cloud enables you to grow into a distributed finance organization that can yield substantial cost benefits.”

1) Access to Data: Visibility and Mobility

Access to information is critical for private software companies. As they decide their next move, whether it's further investment, acquisition or going public, the amount of information required increases with each step. With traditional, on-premise models, data can quickly become siloed within the business, buried in spreadsheets, local databases, or applications. With a glut of applications, finance staff members can quickly find themselves with outdated information, can encounter conflicting data in different places, or will be holding out for a spreadsheet extract. With a distributed team, this can result in substantial latency in the flow of financial information throughout the finance organization and to the executive level.

A cloud-based financial system ensures that information is readily accessible at your fingertips through a web browser, whether that data was entered at headquarters or in a U.K sales office or by a project manager working at a customer site. The cloud enables you to grow into a distributed finance organization that can yield substantial cost benefits as well as enable you to retain the best staff, especially with the continued growth of globalization. At a global or regional level, you gain a clear and timely view into how the business is performing across sales, bookings, billings and more, while role-based dashboards let key managers track KPIs critical to software companies. The cloud also lets you take advantage of shifting work patterns. Web-based, on-demand access lets employees view comprehensive information anywhere, anytime, from any device, including powerful handhelds—a decided advantage compared to traditional systems.

2) Better Cash Efficiency and Lower Cost

With cash burn management among the top priorities for a growing software company, many are justifiably wary of the substantial capital expenditure that would be required to implement an on-premise integrated financial /ERP solution. The up-front costs for software (not only application software but the operating system, database and security software needed to support the application), servers, backup and network infrastructure are large themselves. Add in ongoing expenses for IT personnel, training, maintenance and upgrades, and the total cost of ownership (TCO) can become staggering.

Cloud computing eliminates those capital expenditures, and enables you to fine-tune your subscription to your needs, from small to large. With TCO that is typically 50% less than on-premise ERP, you free vital funds to build products and the business, not manage a complex IT infrastructure. And instead of being forced to weigh your desire for new features and functions against the high costs in time and money of upgrading each time your on-premise vendor releases a new version, you can let your cloud provider implement upgrades automatically.

As of this writing, I'm running on version 2011.1 of NetSuite, a version just released in the winter of 2010. More importantly, every single NetSuite customer—from the smallest five-person shop that signed up with us in 2002 to the large customer we signed last month—is also running on version 2011.1 and benefitting from the updated GUI, enhanced workflow and hundreds of other features and functions included in that release. In my years of working at software and technology companies, I can't remember the last time I was running on the very latest version of the software, even when I was working at the vendor that made it. Even when the software was free, the internal costs in time and money of transitioning to the new version were just too high.

3) Faster Deployment and Decision-Making

Speed is of the essence for a private software company. During critical growth phases, software companies can ill afford a six- or nine-month implementation of an on-premise ERP system. Rapid implementation is high on the list of advantages that the cloud offers to private software companies. According to research by the Software and Information Industry Association (SIIA), cloud solutions are typically deployed 50% to 90% faster than on-premise ERP, and because of the ease of upgrade, your company is always on the latest system. Once deployed, cloud-based ERP/financials give managers the real-time information they need for better, faster decision-making on the fly. Smaller software companies can exploit the unique strengths they enjoy over their large counterparts—a sharp focus, greater agility and a close relationship with customers and partners.

4) Stronger Focus on Innovation

By using a cloud-based financials system, private software companies can focus on how to build processes that scale from the start. By giving the organization the ability to focus on improving business processes and delivering innovation instead of on keeping servers running, backing up data and performing upgrades, the company can truly manage for growth. From a TCO perspective, it isn't just about reducing IT spend—it's about reallocating the IT budget from maintenance to focus on helping the business.

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Some years ago, a report from Gartner found that more than 90% of a typical IT budget is spent on maintenance, and as little as 9% is left for actual business process improvement. The result can be a substantial gap between the goals of the finance organization—such as establishing clear business visibility and strengthening internal controls—and what IT can provide from the current systems. There simply isn't any budget left for innovation. Cloud delivery changes this equation because businesses are able to recoup 50% or more of their IT application operating costs by making the transition. IT can move from an operational role to a strategic role. At NetSuite, the systems team supporting finance is completely focused on business process improvement and incremental visibility, not maintenance.

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5) Improved Recurring Revenue Management

As a software company grows, so do its types of revenue streams. Whether your company is an on-premise or SaaS supplier, subscription-based recurring revenue streams are likely to become more important as your installed base grows. Among the world's 100 largest software companies, subscriptions are estimated to account for about 40% of all revenues. Without the proper financial management system in place, manually managing recurring revenue can become a tedious and error-prone process that results in revenue leakage and customer churn. In many cases, software companies leave money on the table because they cannot respond quickly enough to expiring customer relationships.

The NetSuite Software Company Edition, a verticalized version of our business management suite tailored to the needs of software companies, takes aim at this important issue. It features functionality that enables software companies (whether they're offering perpetual or term-licensed products, or both) to automatically trigger renewals based on a pre-defined window. It allows the co-termination of multiple transactions into a single contract with a single renewal. It provides flexibility in uplift and discount management to maximize both revenue and customer satisfaction across the board, or on a per-customer basis.

Preparedness for Going Public

It comes back to the vision thing. Winning in the brutally competitive software industry requires speed, precision, agility and sound financial and customer management. An integrated SaaS business platform makes that possible in a way that a hairball of standalone applications will never achieve, and over a time and cost horizon that would be impossible with an old-school on-premise ERP implementation. Vision isn't just about visualizing success—it's also about visualizing failure if the wrong choices are made.

At NetSuite, we're especially proud of how our software has helped other software companies succeed. A visit to the software industry page at the customer success stories section of our website will give you a glimpse into some of the benefits our software customers have realized using our on-demand suite. Ultimately, we help software companies prepare for an event they may have dreamt of when mapping the vision for their company out on the back of a napkin at a coffee shop during their start-up days—bringing the company public. And when they do, the NetSuite Software Company Edition gives them the sophisticated financial management, revenue recognition capabilities, compliance support and other features they need to excel as a listed company.