

THE SOFTWARE DISTRIBUTION CHANNEL: THE REPORTS OF ITS DEATH ARE GREATLY EXAGGERATED

White Paper

For Interactive / eBusiness executives



In recent years, with the increasing use of the Internet for eCommerce, many pundits have announced the death of the distribution channel for software. But now, more than ever, this channel serves an increasingly important role for the software industry. And within just a few years it will likely change more than any other channel in businesses globally. As a result, software marketers will need to understand these changes and the underlying technology needed to support them.

INTRODUCTION

Software producers have traditionally relied on their channels for market awareness, inventory management and physical distribution services. So with the advent of the Internet, along with its support for virtual storefronts and online distribution, some industry analysts believed that the software industry would lead in the elimination of channels, in favor of going direct to end user. Our research shows the opposite. Given the increasing complexity of software sales and fulfillment, the reseller channel will dramatically change and adapt, but not die. Ecosystem participants must be prepared with corresponding technology solutions to support emerging new business models.

***Software distribution online is accelerating.
IDC estimates that by 2015 over 70% of sales & fulfillment will be online.***

SOFTWARE ECOMMERCE - NEW WORLD ORDER

Software publishers have historically used their reseller channels to service smaller-sized customers with a local presence at a lower cost versus their own direct sales model. However, Web technologies and newer affiliate-style marketing channels are changing the channel. Going forward ISV's will need to leverage online channels to reach new customers, address new markets and to address the growing complexity of software eCommerce, regardless of customer size.

Role	Old world model	New world order	Implications
Awareness, marketing (discovery)	Local or vertical channel sales professionals for marketing awareness	Customers: Both new and fragmenting markets - global and niche. Channels: Expanding quantity & type of online partners	Marketing content is distributed throughout the ecosystem including social media sites, blogs and online marketplaces.
Selling, (decision making)	Sales, designing solutions, creating relationships	Buyers self-educate & research online outside of the ISV website	Affiliates and resellers capture vertical niche buyer interests. All leverage cloud based marketing automation to move prospects through buying cycle.
Software fulfillment (logistics)	Regional inventory management, financial risk & logistics.	Goodbye to logistics as inventory moves to the cloud	New software consumption & alternative billing models including per-use, monthly user, freemium upgrade to premium
Services & support (implementation & retention)	Local or vertical channel partners.	Self-service & community based support online complemented by local, context-specific support.	Online support communities & use of social networks. Coordination needed around customer ownership. Focus on customer lifecycle management (for renewals & upgrade).

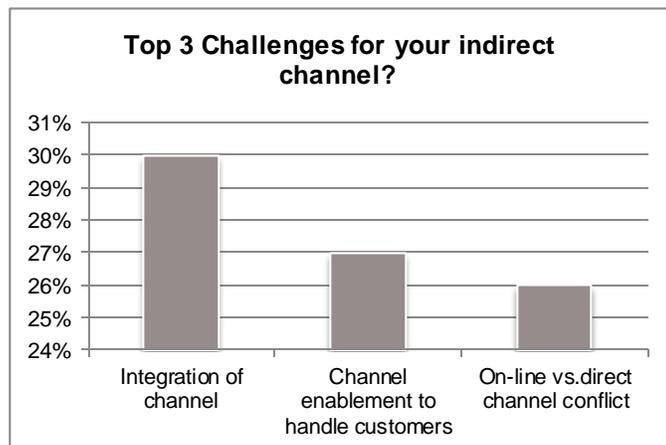
As the transition to online makes doing business more complex, not necessarily simpler, ISVs and their channel partners will need to understand how best to support these challenges in order to capitalize on them.

ISV SURVEY INSIGHTS

Revenue Architects recently surveyed a small sample of Independent Software Vendors (ISV's) to gain insight into their perspectives on their current channel challenges and their view of the future role of their reseller channels. The sample we interviewed worked with on average 100 to 500 resellers who drove 21% to 50% of their revenue.

Deeper Channel Integration and enablement reflect current challenges ...

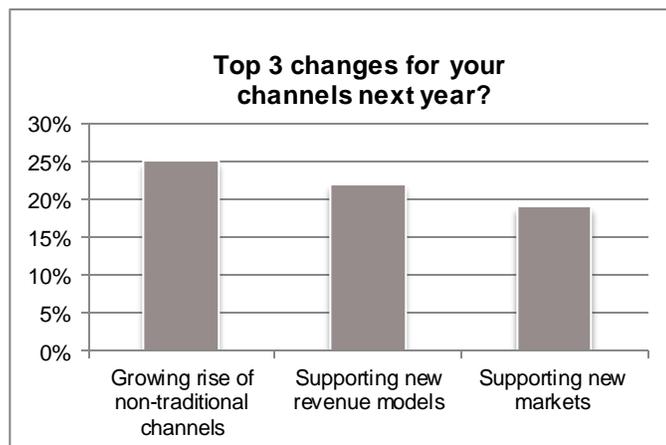
Channel integration topped the sample ISVs' list of primary challenges. Tight integration between partner systems was credited with increasing time to market, preventing lost orders and increasing ISV visibility to channel effectiveness. Also important was the drive to enable the channel to handle their customers on their behalf, not just for the initial sale, but also for support, upgrades and renewals.



Revenue Architects Survey, January 2012

... even as the rise of touch points, new models and markets top challenges for next year

For the coming year ISVs see the growing rise of non-traditional channels as their biggest hurdle. They see rapid rise of importance of affiliates, eMarketplaces and social media touchpoints, all of which provide access to specific vertical domain or niche markets. ISVs also see the need to enable their channels to support their new revenue models (e.g., subscription, in-app purchases, etc.), even as they focus on growth in alternative software consumption models and markets (e.g., international, connected devices).



Revenue Architects Survey, January, 2012

IMPLICATIONS FOR ISV'S

To navigate the changing channel environment, ISV's will need to determine how to maintain existing channel partner relationships while exploring and exploiting new channel types as well as new business model variants.

ISVs need to go beyond current channels . . .

The importance of Affiliates and eMarketplaces as channels is rapidly growing. These channels represent a compelling lead generation and new customer acquisition source. Forrester Research estimates that worldwide affiliate marketing spending is already over \$2 billion and predicts that this spending will reach \$4 billion by 2014. In addition, iSupply recently estimated that just the top 4 app-stores alone will soon account for over 5% of software applications sales. ISVs that ignore or underestimate new online channels will lose out on new business growth opportunities.

While originally focused on consumer markets, Affiliates and eMarketplaces are rapidly expanding to support business to business markets (businesses both small and large) based eCommerce. These online channels go beyond horizontal or general-purpose markets to support increasingly vertical niche industry markets and disparate geographies. Similar to consumer "in context" lead capture, such as offering an application for sale within a special interest consumer website, B2B affiliates offer goods and services within the context of a niche industry vertical or business process. Technology vendors such as Airwatch, Salesforce.com and SAP have already opened enterprise app stores. Now even enterprises such as Informatica create eMarketplaces, while Cisco and GE have open internal employee eMarketplaces to service and manage internal software purchases.

Most of these new online channel partner types offer "pay-for-performance" business terms. This means they typically offer low, or no, setup fees to join and only ask for payment upon a referral or a sale. Furthermore, finding and establishing reseller or lead referral relationships can usually be done online. Then if relationships don't bring expected results these relationships can be dissolved quickly.

... As well as deepen current ISV-channel relationships ...

While emerging online channels represent a great opportunity to expand to new markets, as well as address existing market segments, these new channels may not yet be mature, nor cost effective enough to warrant a wholesale shift in channel strategy. In addition, with resellers representing over 50% of 2011 software sales and customer propensity to shift purchasing behavior slowly, existing reseller channels will likely remain critical in the short and mid-term future. Therefore ISVs must manage their current partner relationships accordingly.

Case in point, in certain software market niches, online markets are not mature enough to engage in software digital distribution. In some segments, the progression to digital fulfillment is slower than industry experts have predicted. For instance, most government agencies and some geographic markets, like in some regions in Europe, still prefer or even mandate the delivery of the physical package, instead of a digital download.

When the environment is more favorable for digital eCommerce, as it is in the U.S. market, doing business with affiliates and eMarketplaces does not always represent cost effective customer acquisition options. Online markets sometimes come at a high commission rate (30% or more). And after paying this upfront commission fee, obtaining upgrades revenues or second year customer renewals is not a given for the ISV. Furthermore, long term marketing success is not guaranteed either. In many cases ISVs find that it is not easy to rise above the many hundreds, sometimes thousands, of titles to become top choices in their desired solution / product category.

In some cases, existing channel partners are adapting their business models to become more like their online channel partner variants. As existing channels no longer differentiate based on inventory management and logistical efficiency, they will increasingly focus on services like marketing and branding. Or they may launch their own app-stores and eMarketplaces. This will blur the lines between today's online and physical partners of today (see sidebar below – Globell a New Age Distributor?).

Over time existing offline distribution channels will consolidate; some will change to offer new marketing or consultative services while reducing their physical inventory services and some will go away. Given the immaturity and uncertainty of existing channel evolution, ISVs will very much need to maintain their existing channel relationships for the foreseeable future.

... As well as constantly experiment

Given the accelerating shifts in the software industry towards online and SaaS delivery and subsequent changes in the role of the channel, ISVs need to constantly experiment to find new markets, let alone keep up in their current markets. During this period of transition, ISVs need to try new products, bundles, and prices and supporting business models, all while looking to optimize their channel mix.

New online channels support experimentation. Online affiliates and eMarketplaces usually offer a pay-for-performance pricing model, quick setups, as well as outsource management services making it easy for ISVs to test the effectiveness of these channels. If any given relationship doesn't deliver expected results, ISVs can dismantle online relationships just as fast. Therefore the penalty of an unprofitable relationship is low. As ISV competitors get strategic advantages from leveraging these channels, the cost of doing nothing (thus letting new leads and new customers flow to their competitors) is high.

As existing channels begin to transition to look more like online channel, ISV's can begin to capture share by helping them make that transition. With existing software and SaaS channel partners are embracing digital distribution and offering more marketing and business process services while reducing their physical inventory services, ISVs should work with existing channels to pursue the same benefits that new online channels are promising.

Shift to Customer Lifecycle Management

Channels will shift from transaction-orientation to managing of customers over time. The nature of software, being delivered as a service, with no physical good, is only accelerating this trend of engaging end-users and customers online. This means that ISVs and their channel partners will rely on online systems to help them transition from transactional systems to customer lifecycle engagement systems. As a result, ISVs will continually seek to have their channel partners to act on their behalf for after-the-sales functions. These services will include proactive renewal and upgrade marketing. Then upgrade transaction management including right and entitlement on behalf of the ISV. Followed by ongoing support. All executed online. As functions move online, so too will real-time dashboard analytics that provide visibility on partner performance and channel effectiveness. Over time, ISVs that engage and experiment with online management of both existing and digital marketing partner will gain competitive advantage.

Globell a new age distributor?

During our interview process we spoke to Globell Inc., a distributor that was founded in 1996 as a reseller of tools, utilities and other PC software. Most notably it was a reseller of the digital file compression tool WinZip. Globell initially focused primarily on the German-speaking markets in Europe including Germany, Austria and Switzerland.

Globell steadily grew its business by expanding geographically and then added additional brands. Then in early 2011 Globell launched *Software-Choice* to add marketing and branding offerings for its ISV customers. *Software-Choice* includes an online portal, social media integration, and support services for ISVs and their customers.

Now Globell has repositioned away from being a traditional distributor, moving towards being a global brand company. So while their ISV partners sometimes have the underlying technology solutions and the ability to go direct to the end user with their own online presence they often prefer to do so with Globell and their brand marketing services.

Revenue Architects sees Globell's transition to a brand management company as a model for the changing nature of distributors. As distributors and resellers no longer differentiate based on inventory and logistics efficiencies, they will need to offer value added services like marketing, branding and market management consultation.

A FRAMEWORK FOR TECHNOLOGY SOLUTIONS

ISVs and their channel partners should think differently about eCommerce solutions for the software industry. First generation eCommerce solutions were born to support consumer retailing web sites and not necessarily designed to handle the complexities of software sales and distribution. Vendor solutions for the software trade need to support both deep multi-channel management capability and support software specific eCommerce functionality as the software reseller channels evolve.

Multi-Channel Access and Management

Solution vendors must facilitate ISVs, and their partners, to grow and manage channel participants over time, including:

- **Dynamic Partnering:** vendor solutions must support rapid partner identification, self-service onboarding, terms negotiation, and partner succession on an as needed or real-time basis.
- **Multi-channel visibility and control:** an ideal platform should provide partner performance analytics and allow for ongoing management of the relationship over time, including the software upgrade and renewal process.
- **Consistency of customer experience across channels:** regardless of vertical market, location or offline/online fulfillment, a software eCommerce solution must enable ISVs to seamlessly maintain the product mix consistency (price, terms, brand, packaging) across all selling channels.

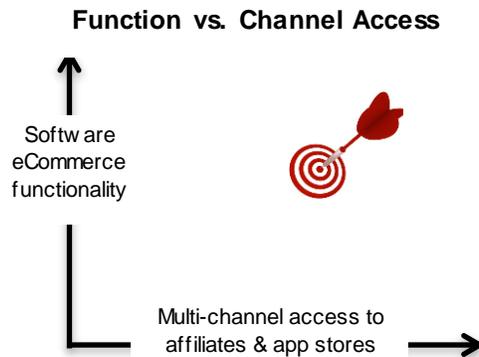
Software eCommerce support

Since first generation eCommerce software vendors' origins lie in support of consumer retail eCommerce, which has traditionally been transactional focused, they often lack support for critical services needed for the software industry. Software eCommerce vendors need to support processes beyond the transaction to become engagement based and thus, able to support the following:

- **Software lifecycle management:** software eCommerce must support the full software lifecycle for both the Electronic Software Download (ESD) and the SaaS delivered solutions. This includes channel support for software key distribution, subscription activation, as well as lead marketing to promote additional purchases, including extending additional seats, or add-on solutions, as well as renewals and upgrades (for example freemium to fee based).
- **Subscription billing model:** technology vendors must provide support for a variety of software industry unique revenue models, including support for Software as a Service delivery (SaaS) and periodic re-occurring billing. In addition, vendors need to support other billing models including; metered-use, user-based, and freemium to premium upgrades.
- **Global / Localized:** technology vendors not only need to support the global scale of selling worldwide, but to support local buying preferences, processes, and regulations – whether selling direct online, or indirect via partners.

The Software eCommerce Sweet Spot . . .

To meet ISV and channel partner future needs, commerce service providers and platform vendors will be best served by offering both robust software eCommerce functionality with integrated channel management capabilities, including access to a robust network of online partners. By combining these two elements channel partners gain time to market advantage. They can create, change and disengage partners rapidly. And they can maintain this consistency and control while gaining visibility, analytics and actionable insight across their global partner network.



Source: Revenue Architects, January 2012

Notable vendors to watch:

Revenue Architects has identified a group of vendors that go beyond support for horizontal eRetailing to offer advanced functionality for software eCommerce. Most of these vendors offer some form of pay-for-performance model whereby they charge for their offering upon successful use of their platform (for example a payment to the vendor is only due for a lead received, or a month's of usage, or a customer serviced):

Vendor	Advantages . . .	Challenges . . .
Asknet	<i>Long history in software eCommerce functionality</i>	<i>Deemphasizing their U.S. market coverage focus</i>
Avangate	<i>Highly configurable multi-channel channel & eCommerce functionality</i>	<i>Focus to date has been outside of the U.S. market</i>
Cleverbridge	<i>Feature rich & flexible eCommerce platform</i>	<i>Limited multi-channel capabilities & affiliate network</i>
Digital River	<i>Longest history in software eCommerce platform marketplace</i>	<i>Traditionally focused on the enterprise (high-end) segment of the market</i>
Hybris	<i>Depth in multi channel management functionality</i>	<i>Limited support of software eCommerce specific functionality & affiliates</i>
Zuora	<i>Depth in subscription management functionality</i>	<i>Limited multi-channel management & affiliate network support</i>

SUMMARY - WHAT ARE YOU WAITING FOR?

Vendors: We expect vendors to continue to build out their software eCommerce platform capabilities and continue to sign-up more affiliates and eMarketplaces. Vendors that provide value both to ISVs, as a robust eCommerce enabler and that also provide rich multi-channel friendly services including access to affiliates and app-stores will be the long-term winners.

Channels: We believe that software eCommerce channels are alive, but not necessarily well. Only distributors and resellers that transition from physical goods distribution to broad eCommerce enablement, with marketing, collaboration, integration with online channels and support to manage the entire software and SaaS lifecycle will be the winners.

ISVs: We recommend that ISVs avoid standing on the sidelines and adopt a “launch-and-learn” approach. Since most of the technology vendors offer a pay-for-performance model, ISVs can afford to engage with vendors with minimal outlays, and experiment on what solution approach works for them, then optimize over time.



Headquartered in Boston Massachusetts, with offices in San Francisco California, Revenue Architects is a research and professional services firm focused on marketing and sales performance. The firm focuses end-to-end across the value chain of sales and marketing to bring insights for sales and marketing excellence.

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