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A Fresh Look at SAP's Software as a Service (SaaS) Solution

After a year of silence surrounding SAP's newest Enterprise Resource Planning (ERP) solution, SAP Business ByDesign is back. During that year, many of its competitors pounced on SAP's silence, even going so far as to initiate and spread rumors that the new product was dead. At Sapphire 2009, SAP showcased about a dozen Business ByDesign customers, some brand new and some I had met a year ago, along with a test-drive area that allowed customers and analysts to touch and feel, and take a guided tour of the product. Not being one that is easily led, this analyst went a bit off-road in the test drive. While the data might not have been real, I left convinced that the application behind it was.

A Bit of Background

By way of recap, SAP officially announced SAP Business ByDesign on September 17, 2007 with great fanfare. The market had actually been hearing about this product for months before, previously referred to by its internal code name of AIS since December 2006. But SAP had been working on the product for four years prior to these announcements. Two years ago at Sapphire 2007, this constituted a major announcement around the intent to design and develop a whole new application suite, designed specifically for companies with 50 to 500 employees. SAP later moved the target just a bit (to a minimum of 100) to better distinguish it from its sister products, SAP Business One on the low end and SAP Business All-in-One at the higher end of the mid-market.

Table 1: SAP ERP Product Portfolio Targets

Company Size	SAP Product	Typical Organizational Structure	Number of employees
Large	SAP Business Suite (including SAP ERP 6.0)	Multi-national, multi-location	>2,500
Mid-Size	SAP Business All-in-One	Multiple locations, divisions and all types of subsidiaries	500 - 2,500
Mid-Size	SAP Business ByDesign	Multiple locations, divisions and independent subsidiaries	100 - 500
Small	SAP Business One	Up to five locations and independent subsidiaries	<100

Source: SAP September, 2007

Analyst Insight

Aberdeen's Insights provide the analyst perspective of the research as drawn from an aggregated view of the research surveys, interviews, and data analysis.

Definition of Company Size

Aberdeen defines company size by annual revenues:

- √ Small: under \$50 million
- √ Mid-size: \$50 million to \$1 billion
- √ Large: over \$1 billion

SAP uses the terminology of SME (Small to Medium Size Enterprises) and defines target markets as shown in Table 1.

But then about a year ago, SAP went quiet. There were no major announcements at Sapphire 2008. Given the prior hype and fanfare, the silence seemed deafening. When asked, SAP said they were still developing the products, but were not going to accelerate their investment in rolling out SAP Business ByDesign. While even then some of their competitors pointed to this as an indication of lack of competitive success, Aberdeen believed it to be a wise decision, providing they continued to invest in the product itself. Because Business ByDesign was being built from the ground up on the SAP NetWeaver platform it served as an opportunity to develop components of re-usable code which could be incorporated as or with composite applications. By developing SAP Business ByDesign, SAP was also developing its other product lines.

Why was this a wise decision? First of all, as a result of introducing a new product along with a completely new business model, Aberdeen anticipated it would take SAP more than a year to lower its own costs of delivery. In order for this to be a successful venture, SAP must make it profitable. Secondly, there appeared to be plenty of opportunity in the geographies where they had already rolled it out. In fact the opportunity in the mid-markets of Germany and the United States alone was in excess of 60,000 companies, as SAP claimed at the time, why push beyond while the pastures where they were grazing were still green?

SAP Promised Differentiation

Given SAP does not want to cannibalize its other "SME" products, it needs to somehow differentiate SAP Business ByDesign from SAP Business One and SAP All-in-One as well as from its "enterprise" products R / 3 and SAP ERP. Several factors indeed differentiate it from its SAP siblings:

Less Complexity

SAP has reduced the complexity of the offering in comparison to its enterprise solutions (SAP R / 3 and SAP ERP). Of course in doing this, the set of features and functions currently available cannot compete head-to-head, but given its target market, perhaps it need never compete at that level. However, SAP has taken a non-traditional approach to adding functionality. While ERP solutions in the past have started with the core fundamentals first before expanding footprints to include functionality often delivered in extensions to ERP – functionality such as Customer and Supplier Relationship Management, Human Capital Management, self-service expense reporting, project planning and accounting – SAP jumped right into these extensions up front and is now steadily filling in gaps in core functionality with features such as budgeting planned for the next release.

SOA "By Design"

While its existing products are "SOA by evolution," SAP's Business ByDesign was built from the ground up on SAP NetWeaver. Although the

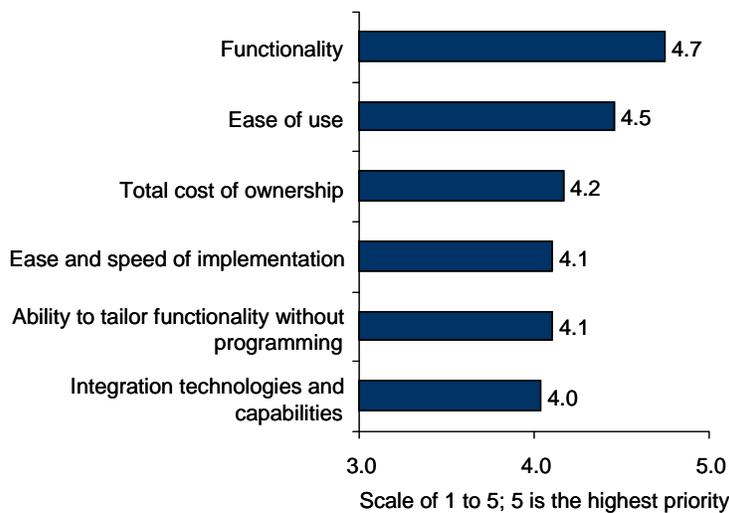
"Prior to implementing SAP Business ByDesign, we were running two different CRM systems and ERP and yet we were still managing inventory with spreadsheets. For over 30 years, BendPak built a reputation for same day delivery. Over time, many duplicate items were created in the system by our sales departments in order to process sales quickly, resulting in our logistics folks working from descriptions to deliver the correct items from inventory, and we held large inventories to be sure that we could fulfill all orders. We did not have the necessary system controls and best practices in place, however we did meet our commitments, but this came at a cost for us.

"With Business ByDesign we now have the necessary controls in place. Today, we cannot sell a product without associated inventory, so duplicates have been phased out. This initiated a huge maturation of the company and brought discipline to our sales and logistics operations. While it was a culture shock, we were able to reduce inventory between January [2009] and now by over 30%. Now our challenge is to maintain the discipline and maintain lean inventory levels. In this market liquidity is king and that was a major driver for the implementation."

~ Sina Moatamed, CTO,
BendPak, Inc.

technical advantages of Service Oriented Architecture (SOA) are clear to those with a technical bent, Aberdeen research indicates most end-users really don't see SOA as their ticket to the future. However, they do seem to value some of the benefits that SOA delivers, particularly in the context of ease of integration and providing web-based services. In its annual 2009 ERP survey, Aberdeen asked survey respondents to prioritize ERP selection criteria on a scale of 1 to 5, where 5 is the highest priority. Early findings from 575 companies show Functionality continues to be the highest priority (4.7), as it has for the past three years, but integration technologies and capabilities appeared in the top selection criteria with an average priority of 4.0 (Figure 1).

Figure 1: Top ERP Selection Criteria



Source: Aberdeen Group, May 2009

SaaS Deployment Model

SAP Business ByDesign is delivered exclusively as a service. While ERP has historically been *The Last Bastion of Resistance to Software as a Service* (July 2007), Aberdeen has been tracking the propensity, or indeed the resistance to On Demand or Software-as-a-Service (SaaS) deployment options over the past several years. Figure 2 shows little change over the past three years. However, follow-up interviews with survey respondents reveal a significant degree of confusion over these different deployment models.

Even some of those Aberdeen knows are running SaaS ERP (because the vendor they use only offers this option) claim they are unwilling to consider it, indicating either they are confusing SaaS with a hosted model or when the ERP solution is accessed via a web-based connection, it is not clear to the end-user exactly what deployment model is used. This leads Aberdeen to conclude that while the SaaS model may not be a significant factor in attracting prospects; neither will it prove to be a deterrent.

SaaS versus Hosted

SaaS: The software itself is not licensed or owned by the end-user, it is provided as a service.

Hosted: Licensed applications are hosted by an outside third-party. This may be in a separate instance on a separate piece of hardware (dedicated to your company), or in a separate *virtual* instance (dedicated to your company) where the application is housed on hardware shared by multiple companies.

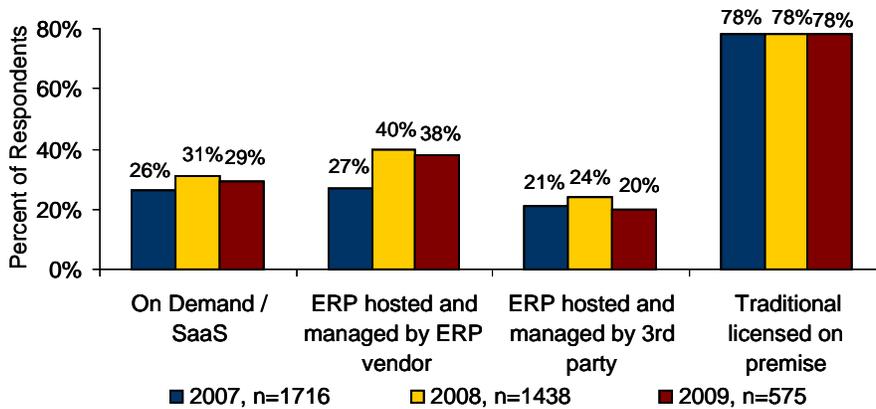
Preconfigured on a hardware appliance:

Licensed software is pre-configured and pre-installed on the hardware. Pre-configuration may be industry-specific and include best practices templates for workflows and role definitions.

Traditional license on premise:

Software is not bought and sold; instead it is licensed for use. It may be licensed to be used on a particular computer or by other criteria such as number of users.

Figure 2: Deployment Models



Source: Aberdeen Group, May 2009

Priced to Sell

Another significant factor in differentiating SAP Business ByDesign from other SAP ERP products is its price. The minimum configuration of a Business ByDesign installation is 25 users, which is in fact more users than most of its current clients initially deploy. In addition SAP offers "efficiency users" (casual users which may have limited access to self-service types of applications such as expense reporting or tracking time against projects). But for a list price of about \$45,000, even if fewer users are needed immediately, the price point is quite affordable and allows for some growth with no added expense.

Of those companies that **are** willing to consider SaaS, the factor that is most compelling is the anticipation that up-front costs are lower (Figure 3). While "software license price" did not make it onto the list of top selection criteria (a priority of 3.8 out of 5.0), the software license is only one part of the whole in terms of up-front costs. These typically include implementation and training services, and if installed on premise, may include hardware, operating system and perhaps middleware costs. Although SAP is targeting SMEs, early findings from Aberdeen's annual 2009 ERP survey indicates it is not just small or mid-size companies that might be attracted to this model. Indeed most of the appeal of a SaaS solution revolves around cost or the decision to bring Information Technology (IT) resources in house...or not.

Table 2: What Makes SaaS Attractive?

	Large	Midsize	Small
Lower up-front costs	88%	77%	68%
Difficulty in attracting and retaining IT talent	58%	62%	66%
Limited IT resources and no interest in building IT staff	67%	42%	54%
Reduces the cost and effort of upgrades	38%	48%	46%

"When we were spun off in December 2007, we were using a legacy ERP from our original company. We were facing an increasing monthly rental fee to continue to use it. We set a 'drop dead' date to get off by May 1, 2008. We actually went live May 12th, just 14 weeks after the first exploratory phone call. Part of our decision was based on my previous three ERP implementations. We needed someone we could trust. I knew R / 3 so I knew I could trust SAP, but I was scared by the massiveness of that product and we had no local IT staff.

"We had a quick ROI due to our rapid deployment. I wanted something pragmatic but expandable. I liked the prescriptive approach to implementation. The scope of our implementation includes Customer and Supplier Relationship Management, Financials, Supply Chain Management, HR and production. Next we'll be looking for more profit and cost analysis, budgeting and building models to better predict profitability."

~ George Bilkey, President, Tam Ceramics, SAP Business ByDesign customer for over a year

	Large	Midsize	Small
Not emotionally attached to having it in-house	25%	49%	46%
Strategy choice to focus internal resources elsewhere	50%	36%	39%
Lower total cost of ownership	25%	33%	34%

n = 498

Source: Aberdeen Group, May 2009

Typically a SaaS deployment will indeed require less upfront costs, but often the true advantage will be the way the costs are accounted for. With no hardware purchase required, and no up-front licensing fee, a SaaS implementation can be viewed as an operating expense versus a capital expense. No one begins an ERP implementation thinking, "Why not? I can always walk away from it if it doesn't work out." That may be sound logic for other software categories, but not for the solution which provides the transactional and operational system of record for your business.

Most reservations about the SaaS deployment model center around concerns over security or the very nature of ERP itself. Fifty-one percent (51%) of those unwilling to consider SaaS cited security concerns and 49% expressed the sentiment that ERP is too basic and strategic to the business to relinquish control. Yet both of these concerns escalated with the growing size of the company and therefore should not provide SAP with a reason not to succeed in smaller companies.

Case in Point

Take for example the case of OneVision Solutions, founded in 2004 and specializing in the sale and implementation of advanced videoconferencing solutions and services. As many companies today look to reduce travel costs, visual and audio communications provide a lower cost alternative for collaboration. With 35 employees, the company is growing even in a down economy. In fact, the search for an ERP solution was spurred by double digit growth year-over-year since its inception. Prior to its implementation of SAP Business ByDesign the small company had been using QuickBooks to manage their business and were quickly outgrowing a desktop solution.

"We knew how much revenue we had, but we had little or no visibility as to where our profit was coming from," said Brent Walters, CFO. "If for example we wanted to know how much business we had done in healthcare in the Northeast region, we had no single source of data to turn to. We had many different offline spreadsheets. We had manual processes and hard copy files. In processing orders and servicing customers, these hard copy files could transfer from desk to desk up to eight times.

"We needed to be able to add new geographic regions, attack new market segments and change our corporate structure as needed. We needed to look at gross profit from many different angles. We wanted to eliminate the need for offline spreadsheets. We still have some, more as backup, but we

"We chose Business ByDesign because it offered the functionality we needed at a price we could afford. We didn't start the process by looking for Software as a Service. We were looking for project accounting and the ability to run a project-based business. But I love the fact that it is SaaS because I don't want to add one single IT person. My only concern up front was around security, but SAP quickly alleviated my fears. We expect every employee to use the system. Some will be 'efficiency users,' only using self-service applications to record their time and expenses against a project."

~ Patti Charlton, CFO, ResearchPoint

"ERP is a long term commitment. It is not something you can casually move in and out of a company. We needed to make sure the solution had a solid roadmap that would meet our long term goals."

~ Sina Moatamed, CTO, BendPak, Inc.

are continuing to move away from them. We have eliminated manual processes and those hard copy file swaps. We are still bringing sales onto the system, but now we have a 360-degree view of our company."

Costs were a major factor in the decision by OneVision Solutions. In final stages of the evaluation the cost comparison was made between SAP Business ByDesign and an on-premise solution (also targeted at the small to medium-size businesses).

"The estimate for the up-front investment in the on-premise solution was \$150,000, primarily for implementation services, but also including hardware and software," according to Walters. "The projected up-front cost of SAP Business ByDesign was less than \$100,000, entirely for implementation services and allowed us to add up to 25 users, whereas the other proposal would have limited us to eight users. So while the up-front costs were lower we also compared the ongoing costs per year. For [the on-premise] solution, we anticipated annual maintenance costs of \$10,000 per year, but we also knew we would have to invest in a data base administrator / programmer. We conservatively projected that cost to be \$75,000 per year. We compared that to the \$45,000 per year subscription cost for Business ByDesign, with no IT staff required. So, on an ongoing basis we would save on the order of \$35,000 to \$45,000 a year. But the advantage of not having consultants living in our offices or an IT department...priceless."

Another advantage, according to Walters, is the ability to configure and adapt the solution to their own needs. While Walter referred to these adaptations as "customizations," they are not. In a true multi-tenant deployment model, where multi-tenant refers to multiple companies sharing a common set of code, customizations typically are not supported, and SAP is no exception in this. The fact that OneVision Solutions and other customers perceive it has a "customized" solution is a tribute to the configurability or tailor-ability of the software.

Walters does caution, however, "Business ByDesign is not the cure-all and we still have some 'work-around' issues and some spreadsheets. No software gets you 100% there."

Key Takeaways

The needs of small and mid-size companies will vary quite significantly depending on industry, structure and leadership. In these uncertain economic times, even small companies that are growing may be reluctant to take that next step beyond desktop accounting software, manual processes, and spreadsheets. SAP's goal of reducing complexity attempts to address these concerns, but of course each prospect or customer must draw their own conclusions about the level of complexity that is both required and is acceptable.

For companies that have already made the jump to an ERP solution and have found they are not able to make full use of their extended solution due to complexities beyond their current needs, and are willing and able to walk

Checklist

Questions for small to mid-size companies to consider when considering an ERP solution:

- ✓ Does the solution meet your current functional needs?
- ✓ What level of complexity does it bring to your business?
- ✓ Is the solution built on a modern, expandable technology infrastructure?
- ✓ How far is this solution likely to take you in your journey of growth? Consider both current and planned functionality as well as the solution provider's track record of delivering on promises.
- ✓ How strong is the vendor's community in terms of reference-able customers and partners?
- ✓ What is the financial strength of the vendor?

away from the time, expense, and effort already invested in another solution, SAP Business ByDesign may provide an alternative and is certainly worth taking a "test drive."

In both cases, as the company continues to grow, the functionality may or may not suffice depending on the needs of the company and SAP's ability to continue to expand the solution footprint. SAP Business ByDesign is still a "young" and relatively immature product, but has the potential of growing with the company, with existing functionality and that planned by SAP.

Today the installed base of SAP Business ByDesign consists entirely of "Charter Clients," early adopters that SAP takes great care to nurture and assist. Some of those clients came on board expressly for that reason. Obviously when SAP starts to scale the volume, this level of individual attention to each customer will no longer be feasible. In the meantime customers welcome SAP's active participation and feel it gives them a true voice in the development of the product. As such, they are in turn taking on some responsibility to their future fellow customers and SAP Business ByDesign users.

As always, the financial strength behind the product is important. With an established client base numbers in excess of 60,000 today coupled with its reputation in the ERP industry as a giant and a leader, this element of the decision should cause no concern to prospective buyers. As a public company, its financial strength is easily monitored.

For more information on this or other research topics, please visit www.aberdeen.com.

Related Research	
<i>The 2008 ERP in Manufacturing Benchmark Report</i> ; June 2008 <i>SAP Takes Aim on the Mid-Market with Business ByDesign</i> ; September 2007 <i>The Total Cost of ERP Ownership in Small Companies</i> ; August 2008	<i>The Total Cost of ERP Ownership in Mid-Size Companies</i> ; July 2008 <i>Measuring the ROI of ERP in SMB: Keeping ERP Projects Alive When You Need Them the Most</i> ; December 2007
Author: Cindy Jutras, Vice President & Research Fellow, cindy.jutras@aberdeen.com	

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