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Soft•letter

BUSINESS INSIGHTS FOR SOFTWARE DEVELOPERS & PUBLISHERS



*In the main, a good year for Return on Equity in the industry, but the education sector looks in need of some repairs
See pages 4-5.*

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Video Helped the Software Star

*The Internet has opened up a variety of video and interactive advertising opportunities to smaller and mid-sized software companies that formally only large companies with big marketing budgets could hope to use. No form of marketing is more compelling than an interactive, moving, talking, singing ad a person **chooses** to watch. And over the last few years, the cost of producing videos has plummeted with the introduction of new tools that simplify the process and the continuing increase in processing power and growth of storage.*

However, we've been surprised by the relative paucity of decent videos being produced by software companies. We went in search of a solid success we could highlight and found one at Centive, publishers of executive compensation software. We spoke with Bob Conlin, CMO of Centive, about the success of their "Bic Bac" video and the lessons they learned.

What was "Bic Bac?"

Bic Bac was a take off of the "JibJab" video that ran during the 2004 presidential elections. These ads featured semi-static, hinge-jawed images of Bush and Kerry saying deeply scurrilous things about each other. The Bic Bac ads take a similar approach, with a salesman and a CFO each insisting they're responsible for a company's business success. Bic Bac can be seen at www.centive.com/parodies. The JibJab parody is still up at www.jibjab.com.

How was Bic Bac produced?

The original concept and script was developed in house with the help of our PR department (and it was lot of fun doing it)! The first version ran for five minutes; we decided to cut it to three. Company employees served as the models in the video. On the day of the shoot, more than 200 pictures of each character were taken for the animation sequences. The animation was done by M Motive (www.m-motive-studios.tv). Once we'd given them the script, they came back two or three times to whiteboard the video and discuss production details.

The actual production took two iterations. The entire process, from conception to final release took about 14 weeks. The entire cost of production was under \$15K.

(continued on page three)

CD Cover Mount Placement Programs, Part I of II

by Mark Haskell, Strategic Connexions

Many publications have an accompanying CD with slots available for trial/demo ware and free lite/express versions, usually called in the industry “*cover mounts*.” But what can you achieve from these and what is it going to cost you? This article discusses expectations, ways to maximize your efforts, and how to place your software with publications at no direct cost.

The Market for Cover Mount Programs

In terms of availability, cover mount programs have decreased in popularity in the US (though there are still many opportunities for placement) because of Audit Bureau of Circulation stipulations. Under these regulations, when you bundle something of value with a publication in the US, the Bureau deems the value of that item (the full “lite” version of your software) to be more than that of the magazine itself and therefore readers are paying for the software, not the publication. Thus, sales of the publication do not count as genuine for auditing purposes. One way that magazines circumvent this problem is by running “special” issues; because they're not audited on an annual basis, they don't have the same impact on circulation figures. As for ROW, cover mount programs are stable in Western Europe and more popular in Central and Eastern Europe. The programs are seeing strong growth in China.

Types of Offers

There are numerous types of cover mount approaches; below I list common options.

Free Lite/Express versions. These programs offer a free software carrot that you hope will please users so much they'll be willing to upgrade to a paid version. A typical example of this type of program will be an express version of a desktop business application polybagged with a magazine that's assigned a retail value of \$50. If your main version costs \$200 you'll typically offer readers the main version at \$150.

Demo/Trial versions. There are less opportunities for trial version placements, but some publications do provide this opportunity. A good option for publishers who don't want to go to the expense and time of developing a lite version.

Free prize/draw giveaways. These offer readers a select number of copies of your main product. To enter, readers need to download a demo/trial copy of your main product and then register their contact details. In due course, the winners are drawn at random from the registered E-mail addresses. These programs have the advantage of encouraging more of a publication's readers to try out your flagship product. Prize draws are common alternative with publications that don't run cover mount CDs or have suitable websites for downloads.

Printed URLs. A special section within a magazine for promotional downloads. Not a very common option, but worth pursuing if you obtain covering editorial from the publication.

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We made the choice to use Flash as the underlying video format. Our research told us 97.9% of the browsers in use have Flash installed; Flash is really a universal Internet video platform. Development was done in Flex with a variety of Flash tools.

The point of using Flash was that we wanted someone to come to the site and be able to view Bic Bac immediately without having to download QuickTime or invoke Windows Media Player. Four years ago Flash would have been a tough call, but most of today's systems have enough cache memory to ensure smooth playback. Also, the Centive site is built in Flash and management was comfortable with the technology.

How did you publicize Bic Bac?

Four primary methods.

- First, we asked all our company employees (about 65 at that time) to tell everyone in their contact books about the video.
- Second, we sent it to all our analyst contacts. Actually, we didn't expect them to pass the word but they did.
- Third was a PR campaign aimed at publications in our sector. These included *Destination CRM*, *CRM Buyer*, *Selling Power*, etc.
- Fourth was the blogs. We went to all the blogs that dealt with selling and marketing; that's where word of mouth about Bic Bac took off. We received prominent mention in seven of the top 10 business-oriented blogs and traffic began to really take off.

Another important factor in driving awareness was that the Bic Bac campaign was discussed on a www.salesroundup.com podcast; this site has a strong international following and the cast drove overseas awareness of Bic Bac to an extent we hadn't anticipated.

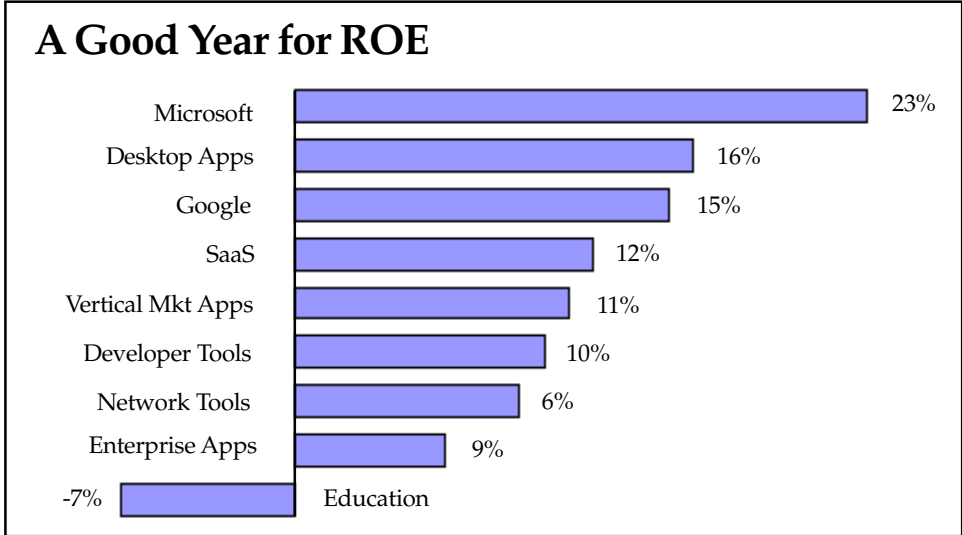
What were the results of the Bic Bac campaign?

Let me give you the actual web statistics:

- The increase in unique visitors in June 2006 (when Bic Bac was introduced) from May 2006 was 217%.
- The increase in unique visitors from July 2006 over May 2006 was 77% (this demonstrates that we continued to drive significantly higher traffic for over eight weeks).
- Web traffic has maintained a level of monthly unique visitors from September 2006 to January 2007 that is 68% higher than our average monthly unique visitors from January 2006 to May 2005. We were very pleased that Bic Bac appears to have substantially improved our baseline traffic (and corresponding sales leads and conversion to sales) on an ongoing basis. We attribute this to *(continued on page six)*

Bic Bac produced a huge amount of positive internal energy for the company. People were fighting to be involved.

—Bob Conlin
Centive



Benchmarks: Return on Equity

Return on equity (ROE) is simply a company's net income (revenues after expenses are deducted) divided by shareholders' equity in the company. The equity is calculated by adding up all the assets and deducting all the liabilities, including debt.

The resulting figure is an indicator of how efficiently management is using a company's assets, and comparing the figures is a rough guide to identifying industry leaders and leading sectors. Yahoo! Finance reports the following returns on equity for the various sectors of the software industry:

Information and Delivery Services	31.0%
Applications Software	23.5%
Business Software and Services	15.2%
Security Software and Services	14.7%
Technical and System Software	14.5%
Healthcare Information Services	7.8%
Multimedia and Graphics Software	6.6%

Soft•letter's Benchmark 50 reports enable readers to compare their own company's performance with that of peers and competitors. But note that a company heavily in debt or with a large write-down could easily have a high ROE because its equity has shrunk, and companies in financial difficulty will generate some anomalous figures: a large net loss can generate a large negative ROE (see Knova in our table on page 5), while net losses divided by negative equity (like Saavis) will generate positive values. Because the Benchmark 50 reports arrange sector results by medians, these outliers have a minimal effect on the larger picture.

Thus tables of ROE performance are primarily useful for the broader picture: is a company's ROE in line with or superior to its sector rivals? More importantly, is it improving over time? A startup like Salesforce.com or RightNow can begin with a negative equity and turn it positive, thus putting its ROE figures into the black.

The Benchmark 50: Return on Equity

	Revenues (000)			Return on Equity			Avg. '04-'06
	2004	2005	2006	2004	2005	2006	
Microsoft	\$36,835,000	\$39,788,000	\$44,282,000	11%	25%	31%	23%
Google	n/a	\$3,189,233	\$6,138,560	n/a	14%	16%	15%
Desktop Applications				16%	19%	12%	16%
Adobe	\$1,666,581	\$1,966,321	\$2,575,300	32%	32%	10%	25%
Intuit	\$1,802,224	\$2,037,703	\$2,342,303	17%	23%	24%	21%
Cyberlink	\$48,966	\$65,141	\$74,926	20%	19%	19%	19%
Symantec	\$1,870,129	\$2,582,849	\$4,143,392	15%	14%	1%	10%
Smith Micro	\$7,216	\$13,316	\$20,258	-16%	31%	12%	9%
Nuance Commo. (Scansoft)	n/a	\$232,388	\$388,510	n/a	-1%	-4%	-3%
Bitstream	\$9,726	\$11,632	\$15,653	-24%	-13%	18%	-7%
Vertical Market Applications				12%	13%	8%	11%
Autodesk	\$951,600	\$1,233,800	\$1,523,200	19%	34%	42%	32%
Ansys	\$113,535	\$134,539	\$158,036	17%	20%	20%	19%
Kronos	\$450,694	\$518,658	\$578,203	17%	16%	11%	14%
Dendrite	\$321,107	\$399,197	\$437,240	12%	13%	8%	11%
MapInfo	\$124,673	\$149,424	\$165,495	4%	7%	6%	5%
Moldflow	\$65,558	\$64,418	\$48,673	4%	8%	1%	4%
Advent	\$137,159	\$149,990	\$168,701	-33%	-6%	6%	-11%
Enterprise Applications				7%	5%	6%	6%
Concur Technologies	\$56,550	\$71,831	\$97,145	7%	17%	29%	18%
Manhattan Associates	\$196,814	\$214,919	\$246,404	9%	9%	9%	9%
SPSS	\$208,367	\$224,074	\$236,063	8%	4%	10%	7%
Pegasystems	\$99,313	\$96,461	\$102,007	12%	5%	3%	6%
Business Objects	\$560,825	\$925,631	\$1,077,151	2%	3%	6%	4%
Witness Systems	\$108,037	\$141,335	\$185,371	-41%	13%	-2%	-10%
Knova Software (ServiceWare)	\$11,511	\$12,502	\$23,595	-2778%	-16%	-21%	-938%
SaaS				12%	9%	16%	12%
Savvis	\$252,871	\$616,823	\$667,012	10144%	233%	52%	3476%
WebEx Commo.	\$189,341	\$249,133	\$308,422	36%	19%	17%	24%
RightNowTechnologies	\$35,879	\$61,764	\$87,148	9%	11%	17%	12%
Digital Insight	\$154,362	\$188,891	\$213,971	15%	5%	8%	9%
WebSideStory	\$16,360	\$22,602	\$39,452	5%	6%	14%	8%
Salesforce.com	\$96,023	\$176,375	\$309,857	-8%	5%	15%	4%
Network Tools				8%	8%	10%	9%
Citrix Systems	\$588,625	\$741,157	\$908,722	18%	14%	14%	15%
McAfee (Network Associates)	\$936,336	\$910,542	\$987,299	8%	19%	10%	12%
iPass	\$136,078	\$166,319	\$169,273	8%	9%	6%	8%
Altiris	\$99,339	\$166,565	\$187,640	8%	8%	1%	6%
Novell	\$1,105,496	\$1,165,917	\$1,197,696	-17%	6%	27%	5%
NetManage	\$50,663	\$47,666	\$43,434	-21%	8%	21%	3%
Tumbleweed	\$30,595	\$43,438	\$50,001	-28%	-12%	-6%	-16%
Developer Tools				9%	9%	12%	10%
Raining Data	\$22,297	\$21,483	\$20,294	-17%	-9%	-16%	-14%
BEA Systems	\$1,012,492	\$1,080,094	\$1,199,845	12%	13%	13%	13%
Progress Software	\$309,060	\$362,662	\$405,376	11%	11%	12%	11%
Sybase	\$778,062	\$788,536	\$818,695	12%	9%	12%	11%
Red Hat	\$124,737	\$196,446	\$278,330	3%	13%	17%	11%
Pervasive Software	\$49,608	\$48,352	\$45,580	9%	5%	5%	6%
Borland Software	\$295,236	\$309,548	\$276,743	-11%	3%	-10%	-6%
Education				-1%	-6%	-14%	-7%
Renaissance Learning	\$127,632	\$111,724	\$116,283	24%	27%	26%	26%
Apollo Group	\$1,339,517	\$1,798,423	\$2,251,472	24%	29%	63%	39%
American Education Corp.	\$8,599	\$10,187	\$9,819	3%	-6%	-19%	-7%
Plato Learning	\$141,801	\$121,804	\$90,719	-1%	-21%	-20%	-14%
SumTotalSystems	\$29,487	\$55,204	\$74,970	-33%	-23%	-14%	-24%
Saba Software	\$34,471	\$42,210	\$71,147	-194%	-16%	-13%	-75%
Scientific Learning	\$29,916	\$30,976	\$40,139	-25%	9%	-305%	-107%
All companies (median)				11%	11%	12%	11%

Source: Company 10-K filings for most recent fiscal years. "Years" may not correspond to company fiscal years.

the higher company awareness generated by the video.

- Finally, the Bic Bac page had almost 15,000 unique visits from June 2006 to September 2006.

Bic Bac was also a tremendous morale booster internally. We first introduced the video at our monthly company meeting and the staff loved it! People were laughing, asking to play parts of it again, and feeling great about themselves. We ended up playing it four times for the group. After it was released, I had engineers swinging by my office to check up on the latest web stats and find out how many people were talking about the video.

If you decide to create video, take a deep breath and accept it's a brand awareness exercise.

—Bob Conlin
Centive

What lessons can a software company looking to launch their own video campaign learn from Bic Bac?

- Make sure your video focuses on customer problems and doesn't talk about your company; people won't sit through a three-minute paean to your firm. I believe that most of the video failures produced by software companies occur because they run on about their company. We believe in keeping the piece short; our new videos, which are takeoffs on the current Mac/PC ads, are 30 seconds.
- Also, remember that you can't require someone to register to watch a video; they won't. You have to realize that you're not going to be able to generate a one-to-one correlation between viewing and lead generation and sales. By tracking web statistics, you can generate an indirect one, however. But videos like Bic Bac are powerful company and brand awareness builders.
- We like the use of the parody format because it protects you from many copyright issues; under US law, you have a great deal of protection from copyright issues with parodies.
- Also, **do not** try to be original! Leverage an existing idea or campaign that already has substantial "word of mouth" (or eyeball) presence in the market. It's expensive to be truly original and I suspect most companies don't have the budget for it.
- Be funny. And it's not easy to be funny; this ties back to the previous point.
- Involve as many people internally as possible in producing the video; don't "over professionalize" the project. This will save you money and also generate internal energy and support for the video.
- You can be a little more daring in a video than in a typical corporate piece. If most corporate collaterals are "G" rated, a video can sometimes move into "PG" territory. But stay away from "M" and "R"; those are dangerous places.

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SaaS In The M&A Arena

By Ward Corum, Corum Group

The software industry model getting the most attention today is without doubt Software as a Service (SaaS). Let's examine some of the underlying features of SaaS that make it a winner for both users and ISV's, and as a result, make it attractive for investors and acquirers.

SaaS is a model that involves the delivery of software solutions in a form different from the traditional, on-premise client-server solution that has dominated enterprise computing. With SaaS, a third party hosts the application and end users access applications over the web. With high speed secure networks, end users enjoy high performance and reliability, while outsourcing the management of hardware, networks, application updates, backups, database administration, etc. The net result to end user organizations is lower cost and easier deployments. The hosting organization (ISV or a third party) can offer these services more efficiently with economies of scale. The ISV reduces support costs, as the applications are running on servers under their control, without multiple hardware and software versions that must be supported and maintained with the on-premise model.

SaaS can be priced many ways, but is typically identified with a subscription model, monthly fees per user, and no initial license fee. This minimizes the customer's capital commitment and can shorten the sales cycle, an attractive feature for any ISV. Lower up front costs may allow the ISV to establish a foothold at a department level, and later expand more broadly in an enterprise. There is still a need for implementation services, data conversion, and training that drives further revenue.

So, what do investors think of a model that is high in recurring revenue, and highly profitable at scale? The best example of this is Salesforce.com, the industry poster child trading at 10x+ trailing revenues, three or four times the valuation of traditional public CRM/ERP companies. From an M&A viewpoint we are just beginning to see transactions involving "pure play" SaaS companies. With only limited data from 30 recent transactions, deals were valued from 3.75 to 7.0 times revenue. This reflects a significant premium for SaaS companies compared to traditional vertical market solutions where transaction values are often in the 1.75 to 2.25x revenue range.

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Company/Description	Acquired by	Price/Terms	Revenues	Multiple
Altiris (ATRS) • Systems management software	Symantec (SYMC)	\$830,000,000 Terms: Cash	\$214,600,000	3.87
SpectralLink (SLNK) • Workplace wireless telephony	Polycom (PLCM)	\$220,000,000 Terms: Cash	\$144,800,000	1.52
SQM Sverige AB • Swiss IT services company	TechTeam Global (TEAM)	\$5,500,000 Terms: Cash	\$11,500,000	.48
Witness Systems (WITS) • Workforce optimization	Verint (Comverse) (VRNT)	\$950,000,000 Terms: Cash	\$204,300,000	4.65

CORUM

Free Phone Conferencing Resources

- **ConFreeCall** (www.confrecall.com): Service offers free conferencing for up to 500 conferees with unlimited duration. Offers plug-ins for Yahoo and MSN chat programs. International access numbers (not free).
- **Free Conferencing** (www.liveofficefreeconferencing.com): Service offers free conferencing service; you pay costs of dial-in. If you use a bulk plan, VOIP, or dial in from a cell, cost is nothing. Supports up to 25 people for up to six hours.
- **High Speed Conferencing** (www.highspeedconferencing.com): Conferencing system designed for Skype users. Up to 500 users can participate in a conference. Supports cell phone dial-in and international dial-in access.
- **Powwownow** (www.powwownow.com): Free phone conferencing system with basic capabilities. Requires users dial in at predetermined time and use a PIN. Users we've spoken to say the system is reliable (a frequent issue with these services). Supports Skype and international dial-in (not free).

STANFORD PROFESSOR PAUL M. ROMER ON THE VALUE OF PERSONAL CONTACTS: "Face-to-face is still very important for exchange of ideas, and nowhere is this exchange more valuable than in Silicon Valley." (Quoted in *The New York Times*, 02/11/2007)

BILL GATES ON WINDOWS VISTA SECURITY: "Maybe we shouldn't have showed so publicly the stuff we were doing, because we knew how long the new security base was going to take us to get done. Nowadays security guys break the Mac every single day [so your Mac] can be taken over totally. I dare anybody to do that once a month on a Windows machine." (Quoted on <http://www.msnbc.msn.com/id/16959622/site/newsweek/> 02/12/2006, 02/12/2007)

SECURITY SPECIALIST AND BLOGGER JOANNA RUTKOWSKA ON WEAKNESSES IN WINDOWS VISTA UAC: "We all remember all those Microsoft's statements about how serious Microsoft is about security in Vista and how all those new cool security features like UAC or Protected Mode IE will improve the world's security. And now we hear what? That this flagship security technology (UAC) is in fact... not a security technology!" Quoted on (<http://theinvisiblethings.blogspot.com/2007/02/vista-security-model-big-joke.html>), 02/12/2007)

BLOGGER JOHN POSPISIL ON WINDOWS LICENSE RESTRICTIONS AND VIRTUALIZATION: "The end-user license agreement for the cheaper versions of Vista (Home Basic and Home Premium) explicitly forbids the use of those versions on virtual machines (i.e. Macs pretending to be PCs):

'You may not use the software installed on the licensed device within a virtual (or otherwise emulated) hardware system,' the end user license agreement states." Quoted on <http://tech.blorge.com/Structure:%20/2007/02/07/microsoft-slugs-mac-users-with-vista-tax/>, 02/07/2007)

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