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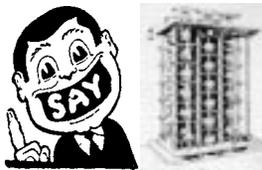
Soft•letter

BUSINESS INSIGHTS FOR SOFTWARE DEVELOPERS & PUBLISHERS

Forget the Crystal Ball: Try These Approaches to Understanding What Your Customers Will Want

by Nicole Bernheimer, Amoebic, Inc

In the rapidly changing technology landscape, determining exactly who will be buying your product feels like aiming at a moving target. Technology companies must try to anticipate, often years in advance, what their customers will want and the best ideas can require even longer development cycles. But identifying customer needs before your competition does can make the difference between not just product success or failure, but that of your company as well.



Our requirements manager reveals RMs make more money reporting to marketing than development See pages 4-5.

While many software companies rely on market reports and research to plot product development, the reality is that these will not give you an edge over your competition—this information is widely available to anyone willing to pay. Your true advantage often comes from obtaining information and insights not published, correctly interpreting their meaning, and then extrapolating usage several years down the line. There are several proven and achievable ways to help you achieve this goal.

Usability studies. Design is becoming more and more recognized as an important sales driver. Usability studies can be one of the best and most cost effective ways to improve a product's success, and it's hard to put too much emphasis on ease of use for the consumer.

Technology companies often rely on internal product development teams to improve usability, even though the people most familiar with a product frequently have the hardest time understanding a new customer's experience. Companies wishing to improve usability can outsource these studies or develop internal design teams dedicated to delving into a product's ease of use.

Usability studies can also help you focus your product development efforts and avoid overbuilding. David Horowitz, vice president of Netomat, a software company that has built a platform for web, phone, and PC convergence in New York, found initially that his developers had created a top heavy product in early development efforts. "We exceeded our customers' needs. The product was too complicated for customers to use. We brought in a usability expert, gathered all the data, and boiled it down to one strong value proposition." Netomat was over-engineered and as a result, the basic value proposition of the service

(continued on page three)

Publisher & Managing Editor
Merrill R. Chapman
rickchapman@softletter.com
860/663-0552

Editor
Donald K. Rosenberg
don@softletter.com
919/687-4172

Editor Emeritus
Jeffrey Tarter
jtarter@softletter.com
617/668-0028

Editorial office
Soft•letter
34 Sugar Hill Rd.
Killingworth, Conn.
06419
860/663-0552

Subscription office
United Communications
Group
11300 Rockville Pike
#1100
Rockville, Md. 20852
301/287-2718
866/313-0973
customer@softletter.com

www.softletter.com

Harsh Shelves: The Retail Realm Becomes Grimmer, Part I of II

by Merrill R. (Rick) Chapman

As we've reported on in the past, the world of retail shelfware is a tough neighborhood getting even tougher as different economic trends in the industry converge. Online sales, WebOS, SaaS, etc. have everyone counting the days till space currently dedicated to software is occupied by MP3 players or moist towelettes. We have to agree that long-term trends look bad, but after speaking to several retail publishers, we've been forced to concede that cellophane-clad cardboard and jewel cases are not ready for the graveyard. Yet. In the meantime, here's what you need to know if you're going to pursue a shelfware strategy.

- The traditional "big box" retail packages (typically 9.5" * 8") is completely moribund among resellers except for holdout CompUSA and we anticipate they're shortly jumping on the bandwagon. All packaging should conform to the mini-box (7.5" * 5.5") form factor. The good news is that you can anticipate a no-flap, five color box will cost between 30% to 45% less over the big box, depending on volume. But anticipate higher shrinkage costs; mini-boxes are easier to steal and losses from theft will be carried over to your bottom line.
- Reseller shelf space is undergoing another shrinkage. As of May of this year, Wal-Mart has reduced the number of titles dedicated to software (non-games) from 341 to 243, a 30% drop. This also represents a loss of approximately 100K linear feet of display space in the chain as a whole. Other resellers, such as Office Depot, are also reducing titles and display space.
- Be prepared to spend more money on high-quality package design. One publisher we spoke with felt that Stomp Software's bright orange boxes helped the package stand out in a sea of less vibrant colors and designs.
- Anticipate new MDF overhead. OfficeDepot has just raised its mandatory MDF charges from 15% to 18 (if you're not selling to the reseller directly, the distributor will collect these funds from you on a "pass through" basis). You should note that you will receive no extra marketing services for these expenditures; this is simply a margin grab. If you are selling through a distributor, plan on handing over 5% mandatory MDF to them as well. In the aggregate, current obligatory MDF costs for your product will range between 20% to 25%. Don't make the mistake of comparing your deals with Microsoft, Symantec, or a similar heavyweight; they can drive deals you can't.
- All channel sales are strictly consignment and your invoices will ship with zero dollar amounts (or maybe a penny; some invoicing systems can't handle zero SKUs). In most cases, you'll receive a monthly sell-through statement and you can expect to be paid in 45 days.
- If financially feasible, regard your retail efforts as branding and advertising; treat any actual revenue derived from the channel as found money.

The logical question that arises from the grim tidings above is: Why would any software company in its right mind bother with a retail strategy? The answer is that despite the ugly realities above, some companies still see value in retail and are still launching products into the stores. In the next issue, we discuss why and how.

was not clear. For some it was a way to take and send pictures via the web and the phone, for others it would be a way to do phone messaging, for others it was a means to create and send photo albums. The application had a host of different uses and its core usefulness was confusing to many. What was needed was a stronger and clearer value proposition to bring to the market.

The initial part of Netomat's process was to conduct focus groups and E-mail surveys directed at friends and family (a favorite tactic of small startups who wish to save precious cash). Next, they commissioned a structured usability study to redesign the interface for phone and web. They found that it was particularly important to focus on the phone application interface as they had less experience in this area. Their testing included designing wire frames and testing these one-on-one with their clients.

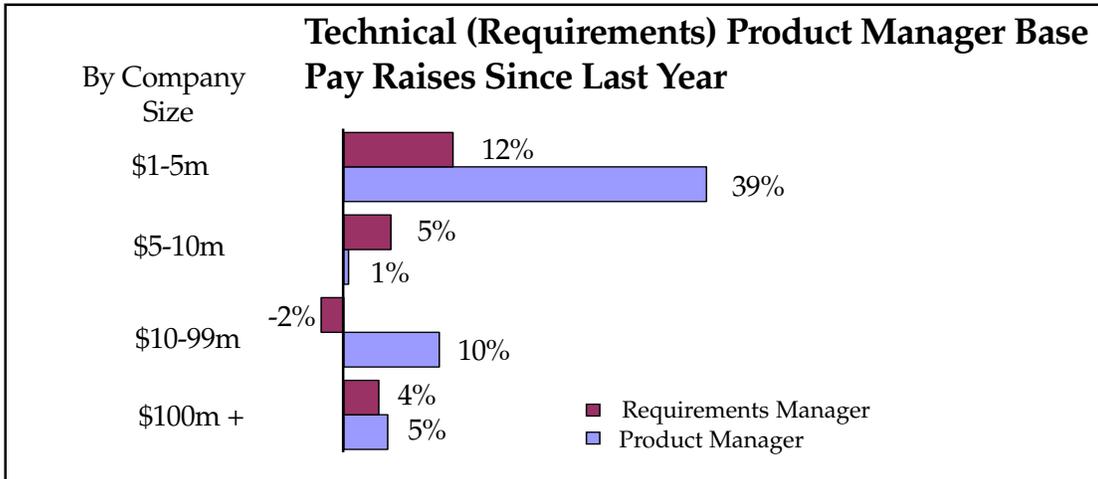
Horowitz says, "we found that ultimately, the main thing our users wanted to do, secondarily to talking on the phone, was to get information. We narrowed our product down to this very strong value proposition, which included managing RSS feeds, updates, and managing our newsreader functions. We left social networking (initially thought to be an important function) in but not in the product's primary workflow. Usability testing was crucial to validating or disproving our assumptions and refining key application tasks."

Develop a strong customer feedback pipeline. One of the most proven ways to elevate product success is sometimes surprisingly overlooked—developing an ongoing, organized communication with existing customers. Companies that make the effort to keep in touch with customers not only find out sooner about problems that can adversely affect sales but also uncover their customer's wishes for future product functionality. David Dreifus, corporate direct of technology and market strategy at Agere Systems, believes that one of the key factors contributing to his company's increasing product sales is their "extremely deep customer relationships. You have to be 'intimate' with your customers. To really predict what they will buy, identify the value you offer not just to your customer, but to their customers as well. Discover what is going to make the people who buy your product successful in **their** jobs and career advancement."

Good ways to maintain and strengthen customer relationships include interactive online customer pages, focus groups, targeted surveys, and customer interviews about new product features. Many technology companies have started providing blogs to provide relevant, up-to-date product information, and develop a sense of community, particularly among developers. Blogs can spur reciprocation of information and participation by your customers. A Pew survey from 2005 reports that 16% of US adults (32 million) are blog readers (a 58% increase from 2004). Companies are taking advantage of this medium to improve customer relations and promote interaction. *(continued on page six)*

"Good product usability can really pay off. In *Cost Justifying Usability*, the authors report that by some estimates, revenues of a usability-enhanced system were 60% higher than projected, with customers citing usability as a main factor in buying a new system."

—Nicole Bernheimer
Amoebic



Benchmarks: Requirements Manager Compensation

In the March 15th issue, Softletter looked at compensation for product managers on the marketing side of the house; this time we look at the technical product managers (often called “Requirements Managers”) who are generally found on the development side. Virtually all companies polled had both types.

For Requirements Managers (RMs), Base Pay is essentially static, with increases coming from Variable Pay. Compared with (marketing) Product Managers, Requirements Managers see smaller pay increases and less likelihood of bonuses (74% of Product Managers receive them, and only 38% of Requirements Managers). The best raises tend to be in the smaller companies.

The two types tend to stick to their own side of the house: a Product Manager is nearly twice as likely to report to marketing as to development, while Requirements Managers are more than twice as likely to report to development. About 18% of either group report to “Other.” The above figures are generalizations that respondents made about their companies; the people actually described in our two polls broke down as follows:

Product Managers reporting to Marketing:	63%
Product Managers reporting to Development:	24%
Product Managers cross-reporting to both:	13%
Requirements Managers reporting to Marketing:	22%
Requirements Managers reporting to Development:	55%
Requirements Managers cross-reporting to both:	23%

The static pay position of Requirements Managers is related to their being on the development side of the house. Not only does the chart at the top of the page point this out, but the association of Variable Pay with marketing, not development, shows us that 90% of Requirements Managers who report to marketing receive bonuses, while only 54% of those reporting to development receive them. And to add to all the other difficulties of being a cross-report, Requirements Managers who report to both marketing and development have only a 43% chance of receiving Variable Pay.

A final point is that we interpret the “n/ms” entered for firms under \$1M to reflect the belief of smaller companies that dedicated RMs are a luxury they cannot afford.

Overall Requirements Mgr. Compensation*	Median	Top 25%	Bottom 25%	Raise
Base Pay—current	\$85,000	\$105,000	\$72,800	0%
Base Pay—last year	\$85,000	\$103,000	\$72,000	
Variable Pay—current	\$6,500	\$18,000	0	27%
Variable Pay—last year	\$5,100	\$15,000	0	
Total Pay—current	\$96,000	\$124,720	\$80,000	2%
Total Pay—last year	\$94,500	\$117,000	\$78,000	

* Number of respondents = 91 for "current," 74 for "last year."

Requirements Mgr. Pay by Company Size*	Base Pay	Variable	Total	Raise
Under \$1 million—current	n/m	n/m	n/m	n/m
Under \$1 million—last year	n/m	n/m	n/m	
\$1-\$5 million—current	\$80,000	\$6,000	\$82,500	12%
\$1-\$5 million—last year	\$71,500	\$6,000	\$80,000	
\$5-\$10 million—current	\$82,000	\$7,500	\$88,000	5%
\$5-\$10 million—last year	\$78,000	\$5,000	\$81,000	
\$10-\$99 million—current	\$82,000	\$2,600	\$94,500	-2%
\$10-\$99 million—last year	\$84,000	\$5,000	\$89,000	
\$100+ million—current	\$108,400	\$9,777	\$117,827	4%
\$100+ million—last year	\$104,500	\$9,650	\$114,250	

* Number of respondents = 7 for Under \$1 million, 16 for \$1-\$5 million, 17 for \$5-\$10 million, 30 for \$10-\$99 million, and 20 for \$100+ million. Values are medians. n/m = Sample size too small for accurate comparisons.

Requirements Mgr. Pay by Development Stage*	Base Pay	Variable	Total	Raise
No significant customer revenue—current	n/m	n/m	n/m	n/m
No significant customer revenue—last year	n/m	n/m	n/m	
Privately owned, privately funded—current	\$80,000	\$7,000	\$88,000	7%
Privately owned, privately funded—last year	\$75,000	\$5,100	\$80,100	
Privately owned, venture funded—current	\$90,000	\$0	\$94,000	2%
Privately owned, venture funded—last year	\$88,000	\$1,750	\$93,205	
Public—current	\$108,000	\$7,925	\$117,300	4%
Public—last year	\$103,500	\$8,000	\$113,000	

* Number of respondents = 1 for No significant customer revenue, 49 for Privately owned, privately funded, 17 for Privately owned, venture funded, and 23 for Public. Values are medians. n/m = Sample size too small for accurate comparisons.

Fostering relationships with technology leaders and advanced users can help a company identify important features. But it also has the added benefit of placing your product in the hands of people who can expose and inform others about it. By developing relationships with them during the formation of your product, you can plant seeds for future sales.

—Nicole Bernheimer
Amoebic

Develop relations with industry insiders. To help understand a future buyer's needs, it pays to find visionary and informed potential customers with insight into what's possible. Gregg Reed, chief operating officer for Mediavision, a near-real-time broadcast monitoring company, swears by using alternative sources to divine future trends. These include developing strategic relationships with Internet user groups, universities, and industry insiders. This is particularly useful for Mediavision because the company is developing a replacement for traditional media broadcast monitoring companies that leverages the Internet. Because it is a new technology, there can be a substantial learning curve for customers to overcome and new business models to adjust to.

Reed finds that customers of conventional monitoring companies "don't necessarily know what is possible" with this new technology. Consequently, Reed seeks out thought leaders and advanced users in the industry to hone product features and pricing. "We work closely with people on the leading edge. We go after the early adopters." In order to find these people, he treats the process like an investigation, constantly searching for them. In addition to engaging with Internet user groups, he attends industry meetings, and identifies thought leaders in the media business, universities, non-profit organizations, and media watch groups.

These relationships have led to substantial tweaking of both product features and Mediavision's business model. Through one relationship with an important non-profit, the company was able to roll out a "single user" subscription service, and test drive it with organization members while getting valuable feedback on pricing and features. Interaction with customer's also helped Mediavision determine what subscribers would and wouldn't pay for. Reed says about the experience, "We learned what is important and what isn't. One feature we evaluated was online searching [of media broadcasts]. Could we charge for that? If so, then how do we charge?

The answer was that we couldn't. If we'd tried, we'd not have had many users. We saved much development time and effort with this discovery.

In another case, the company found an organization that many college professors belonged to "a nonprofit, public interest group that is dedicated to global media issues and that offers news, reports, commentary from an international network of media related organizations and publications, original content, and discussion forums." After developing a relationship, Mediavision was able to refine their ideas on how to sell their system to college students while the professors started offering use of the product in their classrooms. In addition to valuable product feedback, the relationship brought Mediavision a small revenue stream and gave the students exposure and training on a technology relevant to their career prospects.

Nicole Bernheimer, founder, Amoebic, 535 W. 23rd St., New York, N.Y. 10011; 917/650-0167. E-mail: nicole@amoebic.net. Website: www.amoebic.net.

How Applications Cross the Chasm to Valuations, Part I of II

By Marshall Warwaruk

Crossing the Chasm by Geoffrey A. Moore describes the lifecycle that technology companies follow in their transition from an early market dominated by a few enthusiasts and visionary customers to a mainstream market dominated by a large block of companies who are predominantly pragmatists in orientation, followed by conservatives, skeptics and laggards. The Chasm is also an excellent framework for identifying value drivers and compatible valuation models in trying to determine the market value of companies as they progress through this lifecycle.

In the "Early Market Stage," technology companies have barely established a market presence and lack any significant revenue stream, so traditional measurements and multiples of annual sales and profit margin are very poor metrics for determining value. Innovative technology, defensible patents and product differentiation are some of the major attributes sought by buyers, with a key advantage being "first-to-market."

Placing a justifiable value on such companies is a larger and more difficult task than measuring later stage entities. In examining a model for acquiring companies in this stage of the lifecycle, buyers often look at related development costs to replicate the technology, while considering a premium for a reduction in "time-to-market." While it is not uncommon to see multiples varying from two to 10 times development costs used to determine value, buyers still defend and justify the acquisition cost based on their ability to capture market share and generate significant incremental revenues from the newly acquired products/technology. Acquiring companies in this stage of the lifecycle represents the most risk as the technology and business model are still largely an unknown and unproven commodity.

In the "Mainstream Market," which is dominated by pragmatists, the value drivers are more readily identifiable, presumably operating in hypergrowth mode, and providing initially projected returns back to the investor community. For the most part, value is driven by proven market acceptance, brand name recognition, market demand, size of the customer base, strength of the distribution channel, and domain expertise (in addition to growth in annual sales, EBITDA and earnings).

Marshall Warwaruk, regional director SW, Corum Group, 10500 NE Eighth St., Bellevue, Wash. 98004; 425/455-8281. E-mail: marshallw@corumgroup.com.

Company/Description	Acquired by	Price/Terms	Revenues	Multiple
Qpass • Software that processes digital content sales	Amdocs (DOX)	\$275,000,000 Terms: All cash	\$42,000,000	6.55
PassMark Security • Online anti-fraud and authentication	RSA Security (RSAS)	\$48,200,000 Terms: Cash and stock	\$7,000,000	6.89
Mathsoft Engineering & Education • Mathematical software	Parametric Technology (PMTC)	\$63,300,000 Terms: Cash	\$20,000,000	3.17
NetIQ Corporation (NTIQ) • Embedded knowledge and tools	AttachmateWRQ	\$495,000,000 Terms: Cash	\$194,520,000	2.54

Requirements Development Resources

- **Clear Specs** (www.clearspecs.com): Site offers series of reports and polls on current requirements management (RM) and development; also discusses an interesting methodology for requirements development.
- **Managing Requirements** (www.jiludwig.com): Site run by consultant firm Ludwig consulting that offers free templates, links, and information on requirements management.
- **Serlio** (www.serlio.com): Company offers Case Complete, a well-regarded tool for creating use cases.
- **Sticky Minds** (www.stickyminds.com): Software site dedicated to QA, RM and related disciplines. The organization is the sponsor of the STAR conferences, must attends for RM specialists.
- **TRUReq** (www.truereq.com): Site offers TRUReq requirements management software; free for two users.

ORACLE CHAIRMAN LARRY ELLISON ON DISTRIBUTING LINUX: "I'd like to have a complete stack. We're missing an operating system. You could argue that it makes a lot of sense for us to look at distributing and supporting Linux." (Quoted in *The Financial Times*, 04/17/2006)

IP ATTORNEY IAN BALLON ON APPLE'S SUIT AGAINST THREE "RUMOR BLOGS": "The First Amendment cannot trump a property right. The law is certainly on Apple's side on this issue." (Quoted in *The San Jose Mercury News*, 04/17/2006)

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United Communications Group, 11300 Rockville Pike, #1100, Rockville, Md. 20852-3030;
tel 301/287-2718
866/313-0973
customer@softletter.com

www.softletter.com

CALIFORNIA DISTRICT JUDGE FRANKLIN ELIA ON APPLE'S BLOG SUIT: "All you want here is the name of a snitch, so you're saying you have the right to invade the privacy of the e-mail system and to trump the First Amendment ... just to find out who in your organization is giving out inappropriate information?" (Quoted on <http://www.macnewsworld.com/story/50078.html>, 04/21/2006)

FORT PITT CAPITAL GROUP EQUITY ANALYST KIM CAUGHEY ON MICROSOFT'S BATTLE WITH THE EU: "I would have to say that I don't know how much it really affects the day-to-day operations, but it is a big deal for the company. They need to prove they can get along in other economies than the United States." (Quoted on <http://www.eweek.com/article2/0,1895,1952271,00.asp?kc=ewnwsMMDDYYdtx1k0000599>, 04/21/2006)

ESCAPIST COLUMNIST ALLEN VARNEY ON WAL-MART: "If Wal-Mart tells a top-end publisher it won't carry a certain game, the publisher kills that game. In short, every triple-A game sold at retail in North America is managed start to finish, top to bottom, with the publisher's gaze fixed squarely on Wal-Mart, and no other." (Quoted on <http://www.escapistmagazine.com/issue/40/11>, 04/14/2006)