

# Soft•letter

BUSINESS INSIGHTS FOR SOFTWARE DEVELOPERS & PUBLISHERS

## The Odd Couple: Desktop Software Meets SaaS

### Happy Thanksgiving



Revenue per employee numbers show an industry that should enjoy a Happy Thanksgiving!  
See pages 4-5.

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*It's likely that if you need to capture screen shots from time to time (and who hasn't?) or add narration and create a "video" version of a PowerPoint presentation, you've used SnagIT or Camtasia from TechSmith. Founded in 1987, TechSmith Corporation, located in Michigan, initially used the shareware model to grow its business to a 130 person operation that has grown 25% per annum over the last six years.*

*On the surface, TechSmith seems to be the quintessential "retail" software product, but the company recently introduced a new SaaS-based component to its product lineup. We sat down with TechSmith founder and CEO Bill Hamilton to discuss his take on the current state of the shareware approach and the intersection between desktop software and the SaaS model.*

**TechSmith is a classic shareware success. We first used SnagIT years ago, and finally got around to paying for it. We'll also be using Camtasia for some future presentation work. How is the shareware model working today?**

Sadly, I don't believe the original shareware model works anymore, at least for most markets. Much of the shareware culture has disappeared. Ten and twenty years ago, many great and useful products were developed by people whom I think of as "lifestyle entrepreneurs." One or two people would come up with an idea, put a product out there, and perhaps turn it into a mini-business. Many of the shareware successes, such as TechSmith, grew out of consulting operations; we turned our project work into products.

But today, except for some limited opportunities, I don't think this approach is very feasible. You're certainly not going to build a company offering a shareware enterprise solution. You're not going to get far trying to knock off an established leader. In most cases, to succeed you're going to have to build a real company, with marketing, sales, support and all the other components of a modern software company. You need to understand how to run a Google AdWords campaign. You're going to have to put together an executive team to succeed.

**TechSmith is in many ways the quintessential retail company and over the last several years we've noted that this segment of the industry is slowly shrinking.**

*(continued on page three)*

## Product Management and SaaS

Things are changing rapidly in the software industry, as our recent SaaS and upcoming virtualization surveys are demonstrating. SaaS in particular is having an immediate impact on the role of product managers (PMs). We recently interviewed half a dozen PMs at various SaaS-based companies, all competing in different market sectors, to get their take on how this model impacts their jobs both strategically and on a day-to-day basis. These are some of the highlights of our talks.

- SaaS products are no cure for “featureitis.” We confess we were a bit surprised by this observation. The PC press has been carrying on for years about “bloatware” despite the historical fact that feature-laden products, with almost no exceptions, dominate the market. SaaS has been touted as a great simplifier, bringing to the masses just the software that they need. However, our product managers report that the first things customers want to talk about is...more features and capabilities. In software, people seem to like their chrome thick and shiny if the price is right, regardless of whether the product is SaaS-based or licensed.
- Multi-tenanted architectures are critical to success if your business model calls for you to scale (which is the basic point of the SaaS model). Every product manager said their products were based on multi-tenanting. This is in sharp contrast to the results of last month’s survey, where only 37.6% reported they were using this approach. Last month we addressed the Boston Product Manager’s Association on the topic of SaaS and after the meeting had a PM approach and inform us they were not using multi-tenanting and suffering all the predicted problems this choice entails, including a lack of scalability.
- Marketing requirements documents (MRDs) will be slimming down while product requirements documents (PRDs) bulk up. This change will be driven by the fact that our survey revealed that as opposed to licensed software, most SaaS products see at least two major releases a year.
- Related to the above is the growing domain expertise required of product managers. A very deep understanding of an industry’s business processes and issues is important to success, according to our SaaS PMs. As one put it “I spend most of my time studying my customer’s business and less studying mine.”
- Integrate customer feedback systems directly into your SaaS system; of the six PMs we spoke with, four admitted sheepishly that they didn’t have this capability, though all thought it was invaluable. Why didn’t our PMs have access to this capability? “We just didn’t think of it at the time” all admitted.
- Expect to spend more time with sales. “Sales is a rich store of customer information, once they trust you” one our group told us.
- Beta as a marketing tool goes away. As everyone we spoke with agreed, beta programs make little sense with SaaS systems.
- Customers like a Web 2.0 look, and every SaaS publisher is under pressure to make their applications look and behave more like desktop applications. “Customers demand a Windows look. It’s what they’re used to, and clickfests aren’t competitive in the market anymore” one interviewee stated emphatically.

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## Is desktop software dead?

It's interesting that you make that point, but you should remember that we never established a retail presence; we considered it, but decided the rewards weren't worth the risks. Looking back, I'm glad we made that decision.

And no, I don't think the desktop is dying. What I do think is happening is that companies are becoming increasingly pragmatic about solving their problems and also more highly aware of "where" problems can best be solved. This is nothing new, but it's useful to point out that over the last several years applications are using more bandwidth and CPU cycles while the demand for higher reliability continues to grow. The question facing companies selling software and companies buying it is: Where is the best place for applications to "work?" Today's desktop has a lot of power; shouldn't all those cycles be working and doing something?

**Hmmm. This seems to be in line with the Microsoft "SaaS" model; that the desktop remains the center of your computing world, but that desktop applications extend their tendrils out into the Internet and communicate via a series of services.**

I do agree that's what Microsoft wants to happen but that's not necessarily what the customer wants. Microsoft is facing some severe challenges to their business model and I'll assume they don't want to see their bread and butter applications cannibalized. But again, it comes back to where is the best place for an application to do its work? No one has completely solved the latency problems and in many cases it doesn't make sense to try. Use the desktop; there's a lot of power there. I suspect Microsoft wants you to use the desktop even when the web is where the application should be humming along.

## What impact do you think SaaS is having on the industry?

It greatly depends on the nature of the application. Web 2.0 is real, at least in terms of the presentation and UI of applications. But overtime, I think a hybrid approach will be very effective in many markets. But the first generation of many hybrids have been very proprietary; they were tied closely to the hosting section and this limited their success.

## Let's discuss Camtasia and your new service. What is it? And why did you launch it?

We launched Screencast.com because some initial attempts at partnering didn't work out. The system is aimed at business and academic professionals. Camtasia users can share and upload online video, audio, and multimedia content and retain its quality, size, and dimensions.

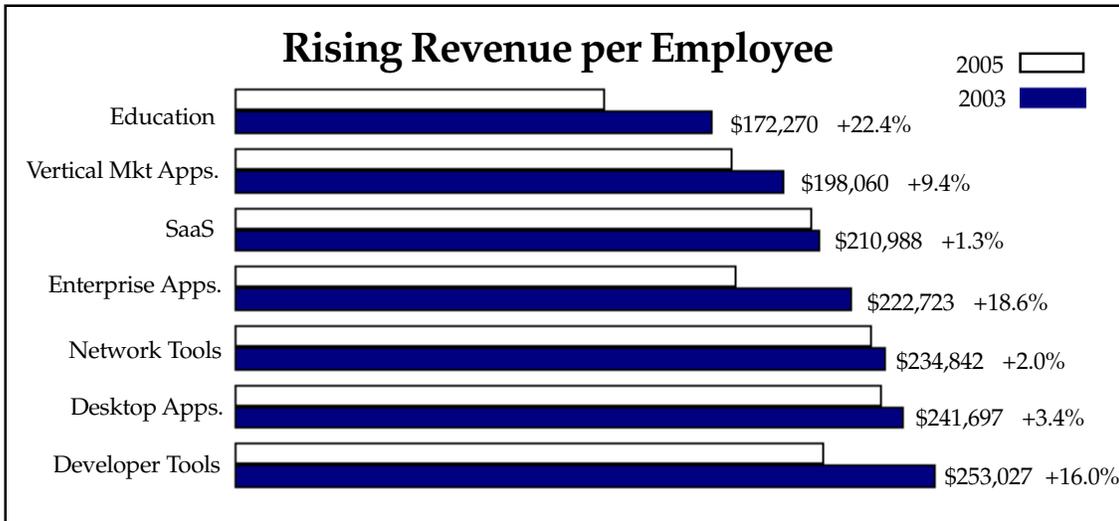
Users retain complete ownership of their content and can control access to their content; we don't want to compete with YouTube.

Screencast.com doesn't resize or

*(continued on page six)*

**"I think Web 2.0 has gotten people to think more about what a hosted online application should look like and what it should do."**

—Bill Hamilton  
TechSmith



### Benchmarks: Revenue per Employee

The addition of Google to the Benchmark 50 is turning up some interesting results. While revenue-per-employee is positively related to the size of the firm (see the table below), Google manages to stand things on their head. Microsoft, the largest firm, manages \$623.7k per employee, but Google with scarcely 14% of Microsoft's revenue and 8% of the employees, manages nearly twice as much revenue for each employee: \$1.081m.

In all sectors of the Benchmark 50 the news is good: revenue per employee has increased across the board. The chart above shows the 2003 and 2005 revenue per employee for each sector, with dollar values for 2005 and % increase. The 2003 dollar values may be found in the Benchmark 50 table opposite.

We believe that the current wave of prosperity has caused customer companies to spend more on IT infrastructure and on software development. Of particular interest are the large improvements of three of the sectors, Developer Tools, Enterprise Apps, and Education.

Developer Tools and Enterprise Applications are obviously benefiting from the extensive IT infrastructure upgrades, and we believe the improvement in the Education sector of the Benchmark 50 is a result of the mergers of the past couple of years. In the case of each merger we have substituted the new company in our listings.

Finally, there is a slight positive relationship in the data between size of the enterprise and revenue per employee:

Firm Size	Revenue/Employee
Under \$25m	\$197,342
\$26—\$100m	\$182,391
\$100—\$200m	\$202,732
\$200—\$300m	\$218,018
\$300m—\$1b	\$233,787
Above \$1b	\$261,985

## The Benchmark 50: Revenue per Employee

	Revenue (000)			Revenue/Employee			Avg. '03-'05
	2003	2004	2005	2003	2004	2005	
<b>Microsoft</b>	<b>\$36,835,000</b>	<b>\$39,788,000</b>	<b>\$44,282,000</b>	<b>\$646,228</b>	<b>\$652,262</b>	<b>\$623,690</b>	<b>\$640,727</b>
<b>Google</b>	n/a	<b>\$3,189,233</b>	<b>\$6,138,560</b>	n/a	<b>\$1,055,688</b>	<b>\$1,080,732</b>	<b>\$1,068,210</b>
<b>Desktop Applications</b>				<b>\$233,423</b>	<b>\$240,351</b>	<b>\$241,697</b>	<b>\$238,490</b>
Adobe	\$1,294,749	\$1,666,581	\$1,966,321	\$369,190	\$530,420	\$342,923	\$414,178
Symantec	\$1,870,129	\$2,582,849	\$4,143,392	\$352,855	\$397,361	\$258,962	\$336,393
Nuance Commo. (Scansoft)	\$135,339	n/a	\$232,388	\$286,735	n/a	\$208,982	\$247,859
Cyberlink	n/a	\$65,141	\$74,926	n/a	\$224,624	\$241,697	\$233,160
Bitstream	\$9,726	\$11,632	\$15,653	\$180,111	\$211,491	\$252,468	\$214,690
Smith Micro	\$7,216	\$13,316	\$20,258	\$131,200	\$256,077	\$222,615	\$203,297
Intuit	\$1,179,101	\$1,242,693	\$1,351,636	\$175,985	\$177,528	\$180,218	\$177,910
<b>Vertical Market Applications</b>				<b>\$179,527</b>	<b>\$199,455</b>	<b>\$198,060</b>	<b>\$192,348</b>
Autodesk	\$951,600	\$1,233,800	\$1,523,200	\$272,431	\$354,846	\$316,476	\$314,584
Ansys	\$113,535	\$134,539	\$158,036	\$186,123	\$244,616	\$263,393	\$231,378
Moldflow	\$65,558	\$64,418	\$65,558	\$225,285	\$202,572	\$198,060	\$208,639
Advent	\$137,159	\$149,990	\$168,701	\$179,527	\$199,455	\$229,213	\$202,732
Kronos	\$397,355	\$450,694	\$518,658	\$165,565	\$180,278	\$178,848	\$174,897
MapInfo	\$106,255	\$124,673	\$149,424	\$150,078	\$155,841	\$165,475	\$157,131
Dendrite	\$321,107	\$399,197	\$437,240	\$127,221	\$156,609	\$156,549	\$146,793
<b>Enterprise Applications</b>				<b>\$181,268</b>	<b>\$192,338</b>	<b>\$222,723</b>	<b>\$198,776</b>
Witness Systems	\$108,037	\$141,335	\$185,371	\$217,378	\$291,412	\$299,468	\$269,420
Pegasystems	\$99,313	\$96,461	\$102,007	\$235,339	\$237,589	\$222,723	\$231,883
Business Objects	\$560,825	\$925,631	\$1,077,151	\$142,922	\$241,427	\$243,810	\$209,386
Knova Software (ServiceWare)	\$11,511	\$12,502	\$23,595	\$225,714	\$117,945	\$248,368	\$197,342
SPSS	\$208,367	\$224,074	\$236,063	\$166,427	\$192,338	\$209,090	\$189,285
Concur Technologies	\$56,737	\$56,550	\$71,831	\$181,268	\$161,571	\$181,851	\$174,897
Manhattan Associates	\$196,814	\$214,919	\$246,404	\$176,199	\$153,514	\$154,003	\$161,238
<b>SaaS</b>				<b>\$208,316</b>	<b>\$198,688</b>	<b>\$210,988</b>	<b>\$205,997</b>
Savvis	\$252,871	\$616,823	\$667,012	\$254,654	\$331,982	\$314,036	\$300,224
Digital Insight	\$154,362	\$188,891	\$213,971	\$208,316	\$248,214	\$267,464	\$241,331
salesforce.com	\$96,023	\$176,375	\$309,857	n/a	\$229,954	\$237,620	\$233,787
WebSideStory	n/a	\$22,602	\$39,452	n/a	\$167,422	\$184,355	\$175,889
RightNowTechnologies	\$35,879	\$61,764	\$87,148	NA	\$153,261	\$164,430	\$158,845
WebEx Communications	\$189,341	\$249,133	\$308,422	\$152,571	\$136,436	\$147,500	\$145,503
<b>Network Tools</b>				<b>\$230,038</b>	<b>\$222,087</b>	<b>\$234,842</b>	<b>\$228,989</b>
iPass	\$136,078	\$166,319	\$169,273	\$412,358	\$413,729	\$416,929	\$414,338
Citrix Systems	\$588,625	\$741,157	\$908,722	\$312,268	\$279,050	\$286,573	\$292,630
McAfee (Network Associates)	\$987,299	\$910,542	\$987,299	\$266,838	\$308,658	\$300,091	\$291,862
NetManage	\$50,663	\$47,666	\$43,434	\$214,674	\$211,849	\$212,912	\$213,145
Novell	\$1,105,496	\$1,165,917	\$1,197,696	\$192,797	\$194,320	\$234,842	\$207,320
Altiris	\$99,339	\$166,565	\$187,640	\$165,565	\$222,087	\$213,713	\$200,455
Tumbleweed	\$30,595	\$43,438	\$50,001	\$230,038	\$160,881	\$156,253	\$182,391
<b>Developer Tools</b>				<b>\$212,585</b>	<b>\$221,002</b>	<b>\$253,027</b>	<b>\$228,872</b>
BEA Systems	\$1,012,492	\$1,080,094	\$1,199,845	\$324,309	\$322,128	\$309,398	\$318,611
Progress Software	\$309,060	\$362,662	\$405,376	\$222,185	\$233,674	\$254,473	\$236,778
Pervasive Software	\$49,608	\$48,352	\$45,580	\$202,482	\$192,637	\$276,242	\$223,787
Borland Software	\$295,236	\$309,548	\$276,743	\$217,405	\$227,442	\$218,080	\$220,975
Sybase	\$778,062	\$788,536	\$818,695	\$212,585	\$221,002	\$220,376	\$217,988
Red Hat	\$124,737	\$196,446	\$278,330	\$183,167	\$208,985	\$253,027	\$215,060
Raining Data	\$22,297	\$21,483	\$20,294	\$157,021	\$150,231	\$152,586	\$153,279
<b>Education</b>				<b>\$133,609</b>	<b>\$145,522</b>	<b>\$172,270</b>	<b>\$150,467</b>
Scientific Learning	\$29,916	\$30,976	\$40,139	\$230,123	\$193,600	\$232,017	\$218,580
Apollo Group	\$1,339,517	\$1,798,423	\$2,251,472	\$166,690	\$171,491	\$199,210	\$179,130
Plato Learning	\$82,192	\$141,801	\$121,804	\$109,589	\$180,179	\$203,686	\$164,485
American Education Corp.	n/a	\$10,187	\$9,819	n/a	\$145,522	\$172,270	\$158,896
Saba Software	\$34,471	\$42,210	\$71,147	\$133,609	\$126,377	\$137,882	\$132,623
Renaissance Learning	\$127,632	\$111,724	\$116,283	\$129,182	\$118,603	\$121,635	\$123,140
SumTotalSystems	\$29,487	\$55,204	\$74,970	n/a	\$123,499	\$119,379	\$121,439
<b>All companies (median)</b>				<b>\$177,629</b>	<b>\$211,645</b>	<b>\$216,036</b>	<b>\$201,770</b>

Note: "Years" may not correspond to company fiscal years; figures are from public filings and other sources.

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reformat the user's content, whether the content comes from Camtasia Studio which is seamlessly integrated with Screencast, or if a user wants to upload a stand-alone video. Also, the system keeps track of a wide array of different statistics on who sees your content, for how long, etc.

To refer back to my previous point, we've made a deliberate decision to decouple Camtasia from Screencast.com. In other words, we're going to support other video services. That might mean scripting via a browser link, an API, whatever makes sense. We'll also integrate with Skype and Flickr. We believe a hybrid desktop/SaaS offering only makes sense if the SaaS part avoids locking in our customers to a proprietary service.

**"If your SaaS application doesn't grow up quickly, you're going to serve as a prototype for another application."**

—Bill Hamilton  
TechSmith

### **What are your business expectations for Screencast.com?**

We believe that Screencast.com is going to drive more sales of Camtasia Studio. Right now, we have no revenue expectations for Screencast.com. The cost per month is very low: \$6.95 per month. Long term, we think growth will be explosive, but we want to have an early conversation with our customers.

### **What are these conversations centered on?**

New features and capabilities for Screencast.com.

**This seems to be a theme running through many of our conversations on SaaS. A lot of press coverage focuses on bloatware and fat products, but it seems SaaS users also like their products to have lots of chrome.**

Well, we've been selling software a long time and people like new capabilities and features in our products. In software, products with the most features usually win; people have demonstrated they'll pay for more bling. Nothing we're seeing with Screencast.com contradicts this.

### **What are your long term expectations for Screencast.com? Number of users, percent of users will sign up, etc.**

We think that at the end of six to eight months we'll sign up 20k users. In two years we think we'll hit 200k customers. Over time, we forecast 20% to 30% of Camtasia customers will also sign up for Screencast.com.

### **Do you anticipate that Screencast.com will replace capabilities currently found in Camtasia?**

We think so, where it makes sense. For instance, conversion between file formats might be best done online because that's where much of your content will be stored. On the other hand, extensive video editing is probably best kept on the desktop. But as these issues are sorted out, I think hybrids will represent a significant jump forward in application power and usability.

Bill Hamilton, president, TechSmith, 2405 Woodlake Drive, Okemos, Mich. 48864; 517/381-2684. E-mail: w.hamilton@techsmith.com.

## Why All the Focus on EBITDA?

By Dang Nguyen, Corum Group

When preparing a private software company for an exit strategy, the first question that may arise is, "What is my company worth?" There are no simple answers to this question but being prepared, using the appropriate valuation metrics, and understanding accounting standards can make the difference in getting a fair market value for your company or leaving money on the table.

One of the most popular methods used by analysts in valuing a company is the price-to-earnings (PE) ratio, which is a multiple of net income. The PE method is typically a good measure for publicly traded companies with a long history of profitable earnings. Different industries historically have different PE ratios; tech companies usually sell at an average of 40 PE. However, using a net income multiple to derive a value for a privately held young and fast-growing software firm can have significant price ramifications. The record of private companies frequently doesn't reflect the true cost of business. For example, earnings may be artificially low because the owners have been charging the company rent on a facility they own, taking royalties out of the company, or paying themselves large salaries and bonuses. As a result, financial statements must be recast.

To get a better measure of how much money a company is generating from operation and to derive a better valuation, owners should focus on EBITDA (Earnings Before Interests, Taxes, Depreciation, and Amortization). Interest expense is the result of financing decisions and buyers typically do not assume the debt as part of the acquisition. Taxes are also not under consideration, since any investment that the buyer makes that yields a positive return, will be taxed at their corporate tax rate. Depreciation and Amortization are an accounting requirement and not a cash related activity that should be included in valuation.

As a manager managing your business, a lot of focus is placed on the bottom line. From a valuation perspective, the bottom line of a private software firm doesn't always tell the whole story. More focus should be placed on EBITDA to derive a more accurate picture of the operating performance and a fair valuation of the company.

Dang Nguyen, senior financial analyst, Corum Group, 10500 NE Eighth St., Bellevue, Wash. 98004; 425/455-8281. E-mail: dangn@corumgroup.com.

Company/Description	Acquired by	Price/Terms	Revenues	Multiple
<b>Open Solutions (Open)</b> • Financial services	Carlyle Group/ Providence Equity Partners	\$1,300,000,000 <i>Terms: Cash and debt</i>	\$282,800,000	<b>4.60</b>
<b>FormScope Group</b> • Document and transaction automation	Bottomline Technologies	\$22,000,000 <i>Terms: Cash and stock</i>	\$9,000,000	<b>2.44</b>
<b>Industrial Logic</b> • Network management software	DataPath	\$21,000,000 <i>Terms: Cash</i>	\$12,000,000	<b>1.75</b>
<b>MetaSolv</b> • Operations support system	Oracle (ORCL)	\$219,200,000 <i>Terms: Cash</i>	\$92,030,000	<b>2.38</b>

## Recommended Reading

*The Real Story of Informix Software and Phil White* by Steve Martin, Sand Hill Publishing.

Before HP chairman Patricia Dunn's recent indictment for illegal bugging activities (and CEO Mark Hurd's amazing attack of amnesia about the aforementioned), Sanjay Kumar's accounting fraud conviction, the recent options scandal that have engulfed McAfee CEO George Samenuk and CNet CEO Shelby Bonnies and may tar other industry figures such as Steve Jobs, there was Phil White of Informix, who ended up pleading guilty to securities accounting fraud in 2004. He only served 60 days at a Club Fed with a salad bar and exercise room, but nonetheless convicted felons tend to have a hard time landing "C" level jobs in high-tech.

"The Real Story" is the chronicle of the rise and fall of Informix, once a database power that competed head on with Oracle, SyBase, and other DBMS heavyweights. It's a fascinating look at the competitive, sales, and marketing events and activities that drove White to make a series of decisions that led to the company's collapse and his own eventual imprisonment.

High-tech executives tend to suffer from what Tom Wolfe described as "Master of the Universe" syndrome, a belief that they are immune from the normal rules and vicissitudes that apply to others. But in the post-Enron era, people like Eliot Spitzer are quite eager to send high flyers and big billionaires (like Dennis Koslowski) to the slammer. Read "The Real Story" to learn about how you can avoid a similar fate. Interesting reading for any software company executive and highly recommended.

### REPORTER REBECCA ARONAUER ON SALES TRAINING

**EFFECTIVENESS:** "Last year companies spent an estimated \$51.1 billion on formal training. One year later, has that investment paid off? Maybe not, according to a recent study by ES Research Group, a sales training and consulting research firm in West Tisbury, Mass. The report revealed that 90 percent of sales training programs result in only a 90-to-120-day boost in sales productivity. Less than 20 percent of companies enjoy sales productivity gains after one year." (Quoted on [http://www.managesmarter.com/msg/content\\_display/publications/e3ilMzAQHc3EHKG45CWungqdQ%3D%3D](http://www.managesmarter.com/msg/content_display/publications/e3ilMzAQHc3EHKG45CWungqdQ%3D%3D), 11/06/2006)

### NY TIMES REPORTER MIGUEL HELFT ON VENTURE CAPITAL:

"In the last couple of years, hundreds of other Internet start-up companies in Silicon Valley and elsewhere have followed a similar trajectory. Unlike most companies formed during the first Internet boom, which were built on costly technology and marketing budgets, many of the current crop of Internet start-ups have gone from zero to 60 on a shoestring." (Quoted in the *New York Times*, 11/07/2006)

**GOOGLE CEO ERIC SCHMIDT ON GOOGLE "OFFICE":** "The sum of that is a different way of managing information and we don't position it as an office suite. We position it as something you'd use everyday in everyday life." (Quoted on [http://news.yahoo.com/s/zd/20061109/tc\\_zd/193717](http://news.yahoo.com/s/zd/20061109/tc_zd/193717), 11/09/2006)

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