



## **The On-Demand Services Market**

Defining the product, the marketplace and the agent earning opportunities

**By**  
**Robert Bye**  
**Executive Vice President**  
**nGenx LLC**  
**[www.ngenx.com](http://www.ngenx.com)**

## Introduction

As small and medium-sized organizations rely more and more on information technology and critical business processes, the visibility of the corporate IT function has increased dramatically. Companies increasingly want features, functionality, and security that in the past were available only to very large enterprises. Features such as remote access keep workers in touch. Collaboration, customer relationship management, and shared calendaring increase productivity and performance. But, maybe of more importance in today's corporate world is disaster recovery and business continuity which have become necessary to protect critical data and keep businesses up and running.

The desire to have IT positively impact business growth has resulted in a new IT requirement: agility—meaning the ability to quickly and easily respond to change. This need for agility is driven by any number of business situations, such as a desire to better empower users, a merger, a response to a competitive threat, or to take advantage of new opportunities.

However, IT departments are more thinly stretched than ever before. New regulations, such as the Health Insurance Portability and Accountability Act (HIPPA), electronic discovery rules and Sarbanes-Oxley are affecting how organizations must track, document, and secure their internal and external information. Not only are IT departments required to keep systems up and running, they are now also charged with compliance which requires additional education and expensive legal advice. The realities of operating a successful business have increased the need for cost-effective solutions to support applications, data, and compliance, and to allow for desired agility within IT.

Driven by lower broadband costs and the advances in workstation technology, companies have begun to adopt the on-demand outsourcing model. Software-as-a-Service (SaaS) and managed hosted services provide a cost effective solution for those organizations that want to focus on their core business rather than devote time and resources to non-core IT functions. Companies get feature-rich, real-time functionality they need without the added burden of deploying, managing and supporting expensive hardware and software in-house.

More and more businesses are relying on companies that can provide software delivery and management services through an on-demand, professionally managed environment. These services are typically housed and run from the vendor's central data center location and are delivered via the internet or private connection. On-demand services are becoming widely accepted by businesses that are comfortable with working in a web-enabled environment and that view it as a legitimate alternative to internal IT staffing and infrastructure.

**"THINKstrategies, in conjunction with Cutter Consortium, has surveyed IT and business decision-makers worldwide and found the proportion of organizations that have adopted or are considering SaaS solutions has jumped from 65% in 2005 to 74% in 2006."**

## What are On-Demand Services?

On-demand services such as SaaS are a hot topic now, but what does the term really mean? There are many varieties, and not everyone is referring to the same thing when they refer to SaaS, Managed Hosted Services, Managed Services, and ASP. This can be very confusing to both the prospective customer and the sales agent. However, there are at least three characteristics shared by on-demand services:

1. they are delivered to the end user via a broadband connection.
2. they reduce or eliminate investment in infrastructure such as servers.<sup>1</sup>
3. they reduce operational management requirements and allow IT to focus on higher value-added, more mission-critical tasks.<sup>1</sup>

## Traditional Software Model

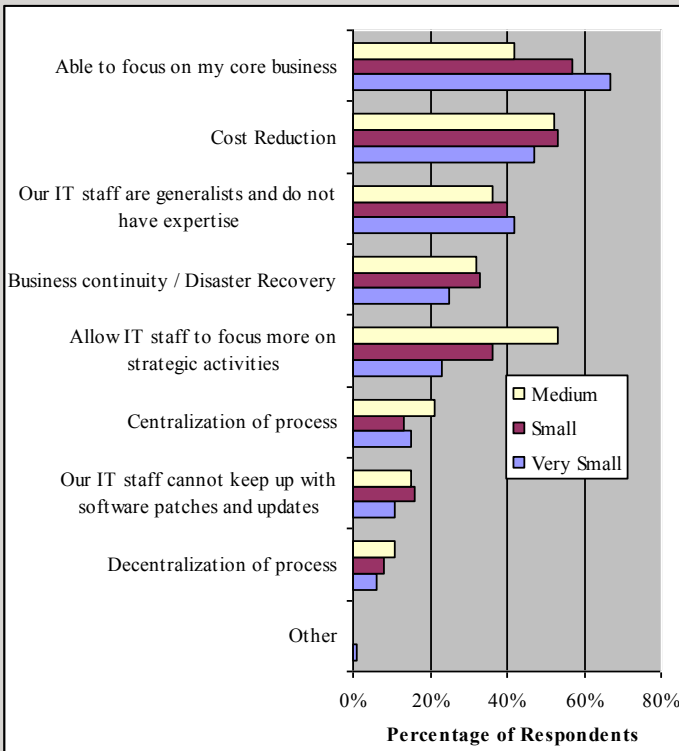
In order to understand on-demand services, it is useful to remember how software has traditionally been delivered. There are large upfront licensing costs and annual maintenance agreements for support which are typically 15-20% of the original cost of the software. Companies must deploy servers and other hardware to support the software, and it is likely that only one piece of software can reside on each server, so capacity is

1. "The Cost and Benefits of SaaS vs. On-Premises Deployment," Gartner, September 28, 2007.



wasted. All of the on-going maintenance and management of the application are provided by the customer. The customer must then also provide all of the physical and logical security, backups, disaster recovery, and regulatory compliance.

### Reallocation/Direction of Resources Biggest Reason US SMBs Use Managed/ Outsourced Services



Source: Yankee Group Anywhere Enterprise—Small and Medium: 2007 US Managed IT and Communications Services Survey

### Software as a Service (SaaS)

The key component to a SaaS offering is that it is based on a monthly recurring subscription. Customers normally subscribe on a pay-as-you-go basis which allows them to scale up or down by adding or deleting users as business demands dictate. The monthly fee includes all of the server and data center infrastructure necessary to operate the software. In addition, the SaaS vendor is responsible for data backups, application maintenance, and 24 x 7 customer support that ordinarily would be the customer's responsibility.

SaaS applications are typically written specifically for the web using .NET or Java. However, some vendors such as Microsoft allow their applications to be sold on

a monthly subscription basis which is convenient for the user even though the software itself is not web-enabled. In those instances, the service provider must use other technologies such as terminal services and application virtualization to enable the software to be delivered over the internet. Because the SaaS applications are web-enabled, they can be accessed remotely from any PC, over any broadband connection.

### Managed Hosted Services

Managed hosted services are similar to SaaS because applications are web-enabled and can be accessed remotely just like in a SaaS model. In the managed hosted services environment, the vendor is responsible for the end user's server, applications management, data backup, security, disaster recovery, and customer support. However, the model is different because these are typical software applications that are not written specifically for the web. The customer owns their own software licenses, and the vendor is simply managing the IT function for the customer.

The customer still retains many of the same benefits as in the SaaS model. There is no need to invest in servers or maintain them. Services can be activated quickly, and the business does not need to worry about whether an additional server will be required to add a user or an application. Also, in the event of a downturn in business, the customer can delete users and save costs without stranding hardware assets. Remote access, disaster recovery, business continuation and data backup are all included in the monthly fee as well.

This model is important because very few software applications are currently available in the SaaS model. Although the prospects for SaaS are enormous, the fact is that many software companies are content with the current business model. There are new software vendors offering their applications in a SaaS environment, but customers are not yet willing to switch from software applications they know and trust to unfamiliar upstart companies.

**According to Gartner Inc.,  
75% of all IT budgets go to  
maintain software applica-  
tions and the hardware to  
support them.<sup>2</sup>**

2. Gartner, Inc. is the world's leading information technology research and advisory company. Statistic taken from the book "The End of Software," by Timothy Chau (2005).

The managed hosted provider can integrate many SaaS applications including email, collaboration, and customer relationship management with the customer's existing line of business applications to provide a comprehensive IT solution, whereas the typical SaaS vendor offers only one type of application such as customer relationship management. In addition, most SaaS applications do not allow for customization, whereas the managed hosted model allows customers to use the application in the manner in which they are accustomed. In today's SMB marketplace, the ideal provider will offer a combination of SaaS and managed hosted services to meet the existing needs of the customer rather than attempting to change the way the customer does business.

### **Managed Hosted Services vs. ASP**

Some people reading this paper will automatically assume that managed hosted services are the same as the ASP, or applications service provider, model. The ASP model was popular in the 1990s but made headlines when many of these companies failed spectacularly in the dot com bust. ASPs relied upon expensive direct connections to the customer, and software applications were housed on independent servers. Broadband speeds at the time were very slow and access was not ubiquitous as it is today, so the service was often frustratingly slow or could not be accessed at all. It was a very expensive single-tenant model that did not provide value to the customer.

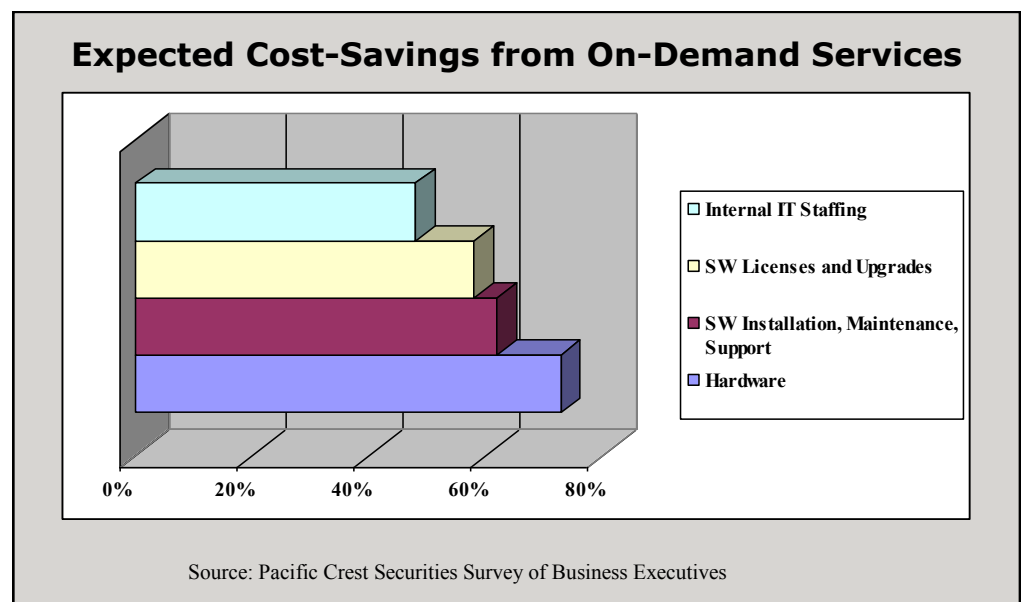
Today's managed hosted services rely upon recently developed virtualization technology. Application virtualization eliminates software conflicts and allows multiple applications to reside on a single server. This allows for more efficient utilization of processing power. It also provides scalability because when growth occurs, the vendor simply adds another server to the farm.

Virtualization also means that very few packets are actually traversing the internet allowing for better performance. Because the application is virtualized, the provider only needs to run a single instance of the application. This means that updates or maintenance can

be performed once, and all users get the update the next time they log onto the system. For the customer, this equates to zero downtime and no interruptions during maintenance or upgrades.

Encryption and other technologies allow applications to be delivered over the public internet without a private connection or VPN. The service may be used in conjunction with these private connections, but it is not necessary. This significantly reduces the cost for the end user customer and increases the market for potential customers.

These technological innovations overcome the limitations of the ASP model. In addition, the customer receives tangible benefits that make the service attractive. Data is stored off-site, so the customer should always investigate the financial stability of the managed hosted services vendor as well as contractual rights to customer data.



### **Managed Services**

At times, companies will want to dip their toes into on-demand services. Managed services offer an incomplete solution when compared to both managed hosted services and SaaS. Managed services providers offer only virus protection, spam filtering, remote data backup, and remote access. These services take some of the IT burden away from the network administrator, but don't offer many of the benefits of a full solution. The company must still devote expensive IT resources

to managing and updating applications as well as maintaining the server network. However, many of the headaches and drudgery of IT are alleviated.

Many customers choose this option because they are afraid to allow their servers out of their sight. They don't understand that their data is more at risk when their server is sitting on-site in a closet than when it is housed securely in a state-of-the-art data center and managed by professionals. Many IT professionals are protective of their territory and won't allow servers to be managed remotely. However, as customers experience the benefits of on-demand services, the demand for these services will increase.

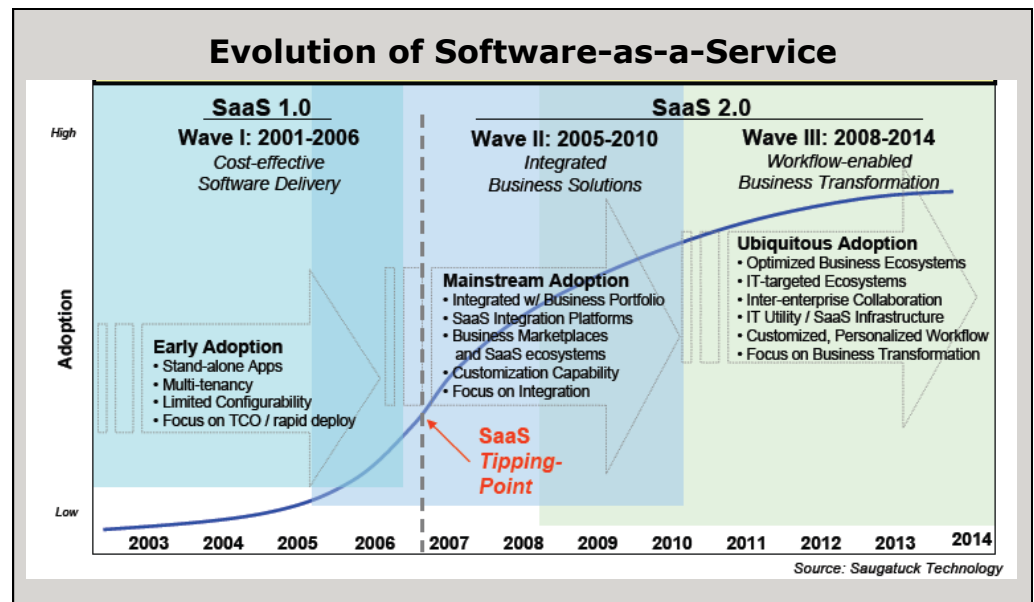
There will always be companies that choose to in-source their IT and keep servers on-site. Therefore, there is a demand for desktop-level managed services. In addition, managed services can serve as the gateway to managed hosted services and SaaS deployments. Once companies become comfortable with the managed services model, they may be more willing to outsource some or all of their IT function the next time an upgrade is needed.

### Market Opportunity

According to Saugatuck Technology, a leading analyst of the SaaS market, "The focus of SaaS will shift over time from cost-effective delivery of stand-alone application services (Wave I), to integrated business services enabled by web services APIs and ESBs (Wave II), to work-flow and collaboration-enabled business transformation." What does this mean? Industry analysts are forecasting that:

- By 2010, at least 65 percent of businesses will have deployed at least one SaaS application, with more than 75 percent US Market penetration.
- By 2010, SaaS will be interwoven into the fabric of enterprise architecture, with large organizations acquiring SaaS solutions as part of their broader business services portfolio.

- SaaS usages within mid-size and large enterprises will more than double by 2010, averaging more than 7 SaaS solutions in production.
- Through 2010, spending on SaaS will increase annually by 25 % or more.
- More than 30 percent of all new business software will be delivered as SaaS by 2012.



In terms of target markets, much has been written about the small and medium-sized business opportunity for on-demand services, with IDC<sup>3</sup> projecting:

"This is the year for small and medium-sized businesses (SMB) to come online... SMB IT spending will increase at twice the growth rate of large corporate spending, and in the process demand lower cost and simplicity of use."

Driving this adoption is the emergence of on-demand services that allow small companies to leverage the IT expertise and economies of scale of much larger organizations, without making oversized investments in IT infrastructure and staff. According to a recent survey by Pacific Crest Securities<sup>4</sup>, 90% of businesses expect substantial cost savings due to implementing on-demand services.

### Target Customers

One of the unique attributes of offering on-demand services is the vast market opportunity. Every company in the modern world uses some type of IT-related service, whether it's a single PC or a fully integrated LAN or even a WAN network. There are so many opportuni-

3. IDC is the premier global provider of market intelligence, advisory services, and events for the information technology, telecommunications, and consumer technology markets.

ties to attract new customers for on-demand services that most sales agents are at a loss to know how to determine the best customers to target. They feel overwhelmed at the prospect of discussing IT solutions with potential customers not knowing if it is a “fit.” While the data does not support adoption by any particular industry or market segment, there are several characteristics that potential customers have in common. Agents can realize the greatest opportunities for marketing on-demand solutions with small and medium-sized (20-500 users) businesses with one or more of the following characteristics. The target organization:

1. Currently has a limited in-house IT staff and/or is currently outsourcing its IT functions.
2. Has multiple locations making onsite IT staff inefficient and costly.
3. Has multiple locations that require centralization of software applications and databases.
4. Is operating outdated technology.
5. Requires more IT help to handle routine tasks such as applying security patches, maintaining virus updates, and changing passwords.
6. Is a new company that is looking at its initial technology options.
7. Is seeking to replace or purchase additional server hardware.
8. Is rapidly growing and needs to scale without waiting for new servers to be installed.
9. May face staff reductions or increases due to cyclical nature of business, the economy or company success.

### **What Are the Benefits of Selling On-Demand Services?**

- On-demand services rely upon broadband for their delivery. As the customer relies more and more on its SaaS/managed hosted services provider, it will need to expand the size of its data connection, resulting in increased sales of data circuits.
- Sales agents get a consultative sales opportunity. Instead of simply pushing a commodity, the sales agent can add value and garner stronger loyalty from a client.
- The convergence of voice and data will continue. Sales agents who embrace on-demand data ser-

vices will survive and prosper. However, even today, pure-play voice agents are at risk of losing opportunities to savvy agents as voice becomes just another data product and part of the larger data services bundle.

- On-demand services are very “sticky.” Factors such as local number portability increase churn and drive down prices. However, once a customer moves his data to a remote server, it is very cumbersome and expensive to purchase a new server and hire the necessary IT staff in order to move the service in-house. When combined with voice services, you almost have to put a fork in your customer’s eye to get them to leave your service.
- Margins for on-demand services are good so providers can afford to pay decent commissions. Both up front SPIFFs and residual commissions are common. Also, many vendors *evergreen* commissions and continue to pay as long as the customer stays on the service.
- Once you have an on-demand customer, you can continue to add additional services in the future. VoIP, IPTV, VoD, and all other packet-based technologies are a possibility.

**Robert Bye is Executive Vice President of nGenX Corporation. nGenX is a nationwide provider of SaaS and managed hosted services, and is a Microsoft Gold Certified Partner. Robert previously served as Vice President and General Counsel for Cinergy Communications, an affiliate of nGenX, where he was recognized as a national expert on communications regulation, VoIP and technology issues. As a leader with more than 15 years of industry experience, Robert has appeared numerous times before the FCC and many public utility commissions to promote competition and limited regulation. Robert received his Bachelor of Arts from Texas Tech University and graduated Cum Laude from Washburn University School of Law.**