



IDC TECHNOLOGY SPOTLIGHT

Software Monetization: Meeting Customer and Business Needs in a Changing Market

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As software use and delivery continue to evolve, so does the need for software vendors to monetize their offerings in a way that meets their own business goals and customer needs. This Technology Spotlight describes how software monetization models are changing and the ways in which software providers will need to adapt in order to support new monetization approaches. In addition, this document describes the products and services from SafeNet that help support various software monetization models, and it offers advice for software vendors looking for ways to monetize their product offerings.

Introduction

The software industry is undergoing dramatic changes that are necessitating new approaches to capturing the value of software through pricing, licensing, and packaging strategies — or monetization. Software vendors are facing the fact that it's increasingly difficult to make money as a traditional software company (i.e., through perpetual licensing). Independent software vendors (ISVs) are being pushed by the current financial climate and industry trends, such as the growing interest in pay-per-use licensing, to seriously consider alternatives. In addition, many of their customers believe that current software licensing models are not an accurate or fair gauge of software's value.

The software industry has already shifted away from a unilateral focus on the traditional, perpetual license model. According to IDC research, 16% of the top 100 software vendors worldwide derive more than 50% of their revenue from subscription licensing. Subscription revenue per ISV averages about \$181 million per year, with a median of \$13 million per year. For these ISVs, subscription revenue grew an average of 20% from 2009 to 2010. Interestingly, while much of the revenue growth will continue to be in software-as-a-service (SaaS) distribution, many ISVs are also offering on-premises software under subscription license. (Note: IDC considers SaaS a delivery model, not a way to license software.)

While subscription has crossed into the mainstream, it won't always be the preferred way to buy. Software vendors must offer a portfolio of flexible pricing options that allow customers to buy in the ways that fit their needs. At the same time, software vendors need to simplify their approach to minimize complexity. Additionally, they must investigate and adopt new ways of monetizing software in order to respond to customer needs and take advantage of new opportunities.

For example, a software provider may need to offer an enterprise license agreement to satisfy the needs of large companies, or it might experiment with new pricing models to capture revenue in the following different ways and with different types of customers:

- Pay per use
- Freemium
- Business value or outcomes-based pricing

In addition, customer experience is a key focus for many software vendors, and pricing and packaging of software plays a key role in shaping this. Therefore, pricing and packaging can no longer be an afterthought but should be part of product strategy from the very beginning and an enabler of business value.

Underlying these shifts will be the increasing importance of and reliance on license management and tracking technologies to help support new monetization models.

Maximizing Software Monetization

Software monetization models should help free customers from the complex terms and conditions required by traditional licensing that usually take away from the value that they receive from the software and cloud their experiences. Software business models must also support dynamic, elastic, mobile, global, and virtual software deployment and usage.

This isn't easy, especially given that customers want less complexity, not more. There's the back end to consider; enterprise resource planning (ERP), billing, and licensing systems are generally not good foundations for agility. While models need to be more flexible, software vendors should also be looking for ways to simplify their approach from every perspective. Ultimately, a successful software company must have a successful software licensing approach — one that is consistent and concrete, demonstrates an awareness of the customer experience, and is communicated effectively.

First and foremost, the ISV must offer a portfolio of well-defined licensing approaches. There are several examples of software publishers with great products that were beaten by competitors with good-enough products that had business models that were more transparent, more customer experience-friendly, and better at aligning customer perceptions of price and value. ISVs need to consider an approach that aligns software cost more closely with value. Usage-based monetization models could be one way to achieve this goal.

This is a challenge, considering the potential impact of new business and monetization models on a software company's culture, internal compensation systems, revenue, short- and long-term shareholder value, and so forth. In addition, the software firm likely will need to continue offering its traditional approach because not every customer will want to move to new models. Therefore, it's wise for software vendors to consider and plan for all feasible licensing scenarios and develop policies to support them. The alternative is handling emerging customer requirements on a one-off basis, but this approach does not scale and often puts a strain on internal operations.

In addition, customers should have the ability to access software product/service capabilities wherever they choose (whether on-premise or as a service) and wherever the software is provided (hosted in a private datacenter, delivered as a public cloud service, or deployed in a private cloud). "Access" is key, and furthermore, customers should be able to access software functionality on whichever device or devices they find most appropriate. IDC sees different licensing models for each delivery model (see Table 1).

TABLE 1		
Software Delivery Model and Corresponding Licensing Approach		
Delivery Model	Description	Corresponding Licensing Approach
Hosted application management	Hosted application management (aka ASP), involving a one-to-many service model, is captured within IDC's application outsourcing services program. Hosted application management refers to services where a customer's packaged applications are hosted and managed out of a vendor-managed datacenter.	The packaged application is almost always sold in the traditional sense for a one-time license and recurring maintenance fee. The hosting contract is separate from the license contract.
Software as a service (SaaS)	Software as a service is a service delivery model made up of a utility computing environment in which unrelated customers share a common application and infrastructure that is managed by an ISV or a third-party service provider, and code, or intellectual property (IP), of the service is typically owned by the SaaS ISV. The model provides access to and consumption of software and application functionality built specifically for network delivery and which is hosted, provisioned, and accessed by users over the Internet.	SaaS applications are priced via a subscription model. A single price includes the right to access the software for as long as the customer continues to pay, as well as access to any future updates to the application. The metrics for SaaS offerings are typically user based, but usage-based metrics could also work well in this environment due in part to ease of metering/tracking (compared with on-premise).
Public cloud	According to IDC's definition, public cloud services centering on access to software are synonymous with software as a service.	Cloud applications are also priced via subscription, and public cloud services are generally user based in reality, although a key tenet of cloud is metered usage-based pricing.
Private cloud	Private clouds are designed for and access restricted to a single enterprise (or extended enterprise) and are an internal, shared resource where the IT organization acts as the service provider for its own constituents.	This implies pay-per-usage metrics, although very few software applications are priced in this way today. CIOs of large companies tell IDC that they tend to strike one-off deals with key vendors — including database and operating systems — to come up with models that work in a private cloud environment. Key considerations for software publishers developing approaches are management tools to support licensing policy, policy that supports chargebacks, and the CIOs' desire to reduce costs first and foremost with cloud.
Mobile access	Mobile applications provide a critical front-end application for mobile workers based on the role of workers and the subsegment of data that those workers require from an existing back-end application residing within the enterprise or accessed via a hosted environment.	An emerging area, perpetual models that include a right to mobile access, as well as subscription models where mobile is included or priced as an add-on, can be found in practice. Licensing for mobile access is more challenging for those vendors that typically count the number of devices versus the number of individuals that access the system.
Source: IDC		

As the distribution ecosystem for software changes from physical delivery to a digital download model, ease of implementation and speed to deployment are paramount. Barriers to adoption in the form of inefficient distribution channels or services requirements have serious negative consequences for subscription renewals and trial conversions. A key success characteristic for software providers therefore must be tied into an efficient payment ecosystem.

Software publishers must determine what presence they wish to have in which ecosystems and must develop policies that support the requirements of customers. Policies must include price transparency, bundled right to use and update/upgrades, mobility, ease of management via portal/console, ease of procurement, global license portability, and licenses tied to users, not machines.

The Importance of the Customer Experience in Software Monetization

In the software industry today, ISVs are educating their customers about excelling in the new era of the "empowered customer," with customer experience becoming a key driver of business value. ISVs are also focused on the experiences of their own customers. While pricing and licensing is only one element that influences the experiences of customers as they progress on their journey with the ISV, it is an important one that is encountered virtually every step of the way.

IDC expects that trends in the software industry that are necessitating changes in the ways that software is monetized will put further strains on the software pricing and licensing infrastructures of ISVs and negatively impact the customer experience. The goal of any ISV that is focused on customer experience should be to create a flow that is planned and architected in a manner that makes the interactions throughout the customer's journey as easy, quick, transparent, positive, and full featured as possible.

IDC believes that two key aspects of pricing and licensing impact the customer experience:

- The elements of the pricing and licensing policy itself, such as:
 - How simple/flexible and transparent are the pricing and licensing?
 - How easy is it for prospects or customers to interpret the licensing policy and its impact on how they deploy, use, and manage the software?
 - Does the underlying entitlement management system support the pricing model?
 - Does the billing system support the pricing model?
 - Can the customer easily maintain and demonstrate compliance?
- The effectiveness of the pricing and licensing policy in capturing and reflecting the value that the software provides, such as:
 - Does the customer perceive the price as fair?
 - Does the cost of the software (up-front and over time) align with the customer's expectations of what it should be?

Benefits and Challenges of Software Licensing Monetization

More methods to monetize software increase the predictability of software revenue and make it easier to demonstrate future health. Customers, for example, like the low up-front cost of the subscription model as well as the enhanced ability to build a relationship with the software provider. In addition, many customers could never have afforded the software products if they were licensed under the traditional perpetual model.

Because subscriptions typically renew annually, the software provider must also demonstrate ongoing value and build a relationship with the customer. However, for this strategy to be successful, quality of technology is of paramount importance because if clients don't see returns in a rapid fashion, they likely will decide not to adopt the technology on a longer-term basis. Customers like this aspect of subscription licensing because they believe it results in a better customer experience, but most software vendors' businesses are based on a model of selling the value of the software at a single point in time.

Usage-based monetization models have advantages but also come with challenges. If usage has not been tracked in the past, it's very difficult to move to this kind of an approach for the following reasons:

- If the ISV doesn't know what customers are using, how could it possibly determine if a model that charges for use is advantageous?
- How could the ISV develop an appropriate pricing scheme if usage is unknown?
- Why would customers accept an approach where they can't use any historic basis for predicting future costs?
- How can usage be audited (to support a usage-based pricing scheme) if there is no mechanism for tracking it?

On-premise customers typically don't want to provide usage data to software publishers, but they are very receptive to using tools that provide insight into their own usage as long as the tools don't automatically report data back to the vendor. In the case of SaaS or public cloud applications, usage tracking is implied and more widespread; however, ISVs must be clear with customers up front about what data is being tracked and how it is being used.

Considering SafeNet's Software Monetization Solutions

SafeNet has taken advantage of its expertise in authentication, security, and software license management to now offer a broad range of software monetization solutions for software vendors. With more than a 25,000 reported customers, SafeNet has continually broadened its portfolio to offer products and services for the entire software monetization life cycle — from copy and intellectual property protection to product catalog management and end-user experience management. The company offers solutions for any type of software, including on-premises, embedded, and cloud-based, and supports the complete range of ISV business models from direct sales and channel distribution to SaaS.

SafeNet's software monetization solutions are based on the Sentinel family of products and services. Solutions include software packaging, control, management, and usage tracking features to help software publishers address the full spectrum of software monetization challenges from IP protection and piracy prevention, effective and customer-friendly operational processes, and business intelligence. SafeNet also offers a full range of software monetization consulting and implementation services.

All license enforcement solutions in the Sentinel portfolio include the company's Cross-Locking feature — a mechanism by which software publishers are able to apply software protection "on the fly" to meet the needs of every unique customer, every time. Sentinel LDK, Sentinel HASP, and Sentinel RMS currently support a choice between hardware- and software-based protection keys. The company's cloud-based solution, Sentinel Cloud, supports a choice between software- and cloud-based license protection mechanisms. The company's Sentinel LDK out-of-the-box licensing security solution focuses on security and ease of use. The Sentinel RMS software license enforcement toolkit focuses on enabling software publishers with the maximum level of customization in their licensing implementation. Sentinel RMS can focus on security, visibility, or flexibility, or any combination of the three.

All of the company's license enforcement solutions rely on Sentinel EMS for entitlement generation, tracking, and management. Sentinel EMS is a Web-based solution that provides software publishers with a centralized tool for all license and entitlement management functions, a simple interface to back-office systems, and a variety of advanced data collection and reporting functions. While Sentinel EMS is fully integrated with Sentinel LDK and Sentinel RMS, it is a licensing system-agnostic solution, enabling ISVs to provide central management of disparate licensing systems and offer a single, consistent interface for managing their software licenses.

Through Sentinel EMS, all of SafeNet's solutions can be fully integrated with a software publisher's back-office systems — such as CRM, ERP and billing — to automate business processes. The company offers many out-of-the-box connectors for such integrations and has an experienced professional services organization to handle custom requirements.

Sentinel Cloud is reported to be the industry's only software licensing and entitlement management solution deployed in the cloud for cloud service. This service enables SaaS providers to package, deliver, and manage any cloud-based application delivered to a PC, laptop, mobile device, or other device. The cloud service also provides software publishers with detailed visibility into the usage of their application, providing invaluable insight into not only who is using which aspects of their offerings but also when and how often.

Challenges

As the face of software monetization changes, SafeNet will need to keep up with changing market requirements while continuing to support customers that are not ready to embrace new software business models. To respond quickly and efficiently to new opportunities, SafeNet will need to continue adding strong partners to expand its presence with ISVs that are shifting to cloud models. In addition, the company must continue to incorporate functionality into its product and service catalog that supports the dynamic needs of cloud-oriented ISVs, including usage tracking and management.

Perhaps most important, ISVs and their customers are concerned about data security and protecting valuable customer information, including the necessary usage data to manage software licenses. It's imperative that SafeNet continue to leverage its more than 25 years in cryptography and security to ensure secure data collection and ownership.

Further, as more ISVs and customers embrace new monetization models, competition for products to support this will grow. In particular, companies that serve needs in adjacent markets, such as billing providers, "platform" providers, and traditional asset management firms, may expand their scope to include software licensing and entitlement management. SafeNet must continually look for ways to demonstrate technological advantage and its successes to gain continued recognition and share.

Conclusion

In the on-premises software world, it has been acceptable to take some time to configure a solution. In the cloud, this must all happen immediately. In addition, customers' experiences with cloud approaches influence customers' expectations for on-premise software. With the dramatic growth of new monetization models such as subscription licensing and electronic distribution approaches, the ability to offer appropriate monetization will become a critical component of any ISV's business model.

Software vendors face the difficult challenge of giving customers increased flexibility in the ways that they buy and use their software without adding complexity to their models. Good support tools can mitigate complexity, but software vendors should be careful to use tools that are transparent to their customers.

Software vendors that are looking to take advantage of a variety of ways to monetize their offerings should consider the following:

- While cost is important, customers also need a way to flexibly and rapidly deploy new software resources to meet changing business needs.
- Selecting resource utilization metrics that truly reflect software business value and are easy to track and report is critical; working with customers is a great way to find out what makes sense and build a relationship.
- Technology to track resource utilization information should be rock solid and easy to use so that vendors can provide complete and detailed billing summaries.
- Offering a new pricing model will be difficult for the vendor, but the model should be easy for the customer to adopt.
- Because customer preferences vary, vendors should offer a portfolio of licensing and delivery approaches.

The bottom line is that software vendors must succeed in a world where customers are dictating how they want their solutions delivered and priced. ISVs that ignore this will be in trouble. To the extent that SafeNet can address the challenges described in this paper, the company has a significant opportunity for success with ISVs that need software monetization products and services.

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