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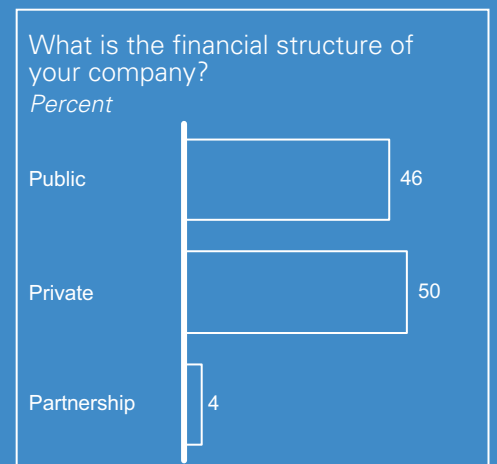
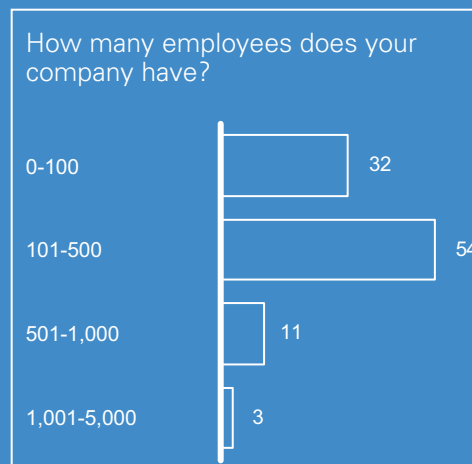
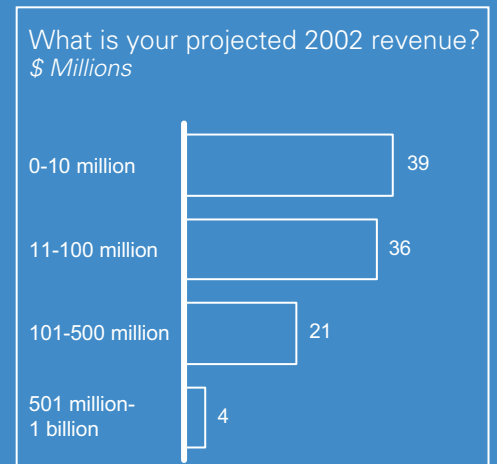
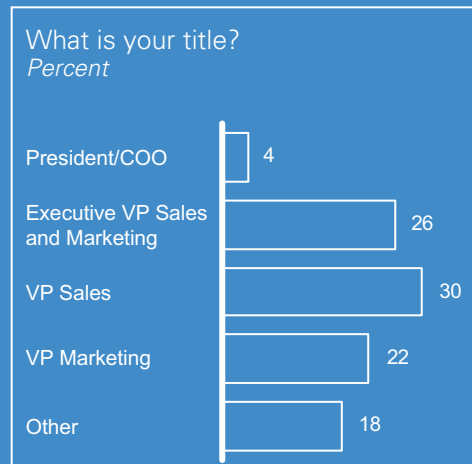
Bob Wright, **MARKETING ARTS**

The report of the 2002 SMART Enterprise Conference, and all previous Enterprise reports and conference information, are available on-line at www.sandhill.com

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the participants

The overwhelming majority of individuals attending the 2002 SMART Enterprise conference were sales and marketing vice presidents (78%). 75% of participants came from companies with less than \$100 million in sales and 86% of participants came from companies with fewer than 500 people. While this year's attendees tended to come from smaller organizations than in 2001, this year's participants were more likely to come from public companies than last year (46% this year versus 25% last year).

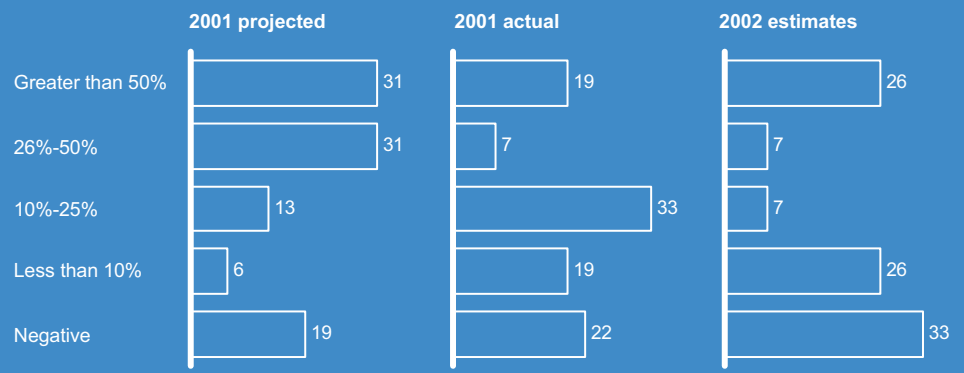


demanding customers growing even tougher

The enterprise software industry in 2002, like all sectors within high-tech, continues to be deeply affected by the overall economic climate. The rebound anticipated by analysts in 2002 has failed to materialize as growth has slowed from 35% in 1998 to 5-10% this year. Analysts have pushed back their expectations for economic recovery to 2003 or even 2004, when growth rates are expected to hit 12-14%.

Faced with these challenging times, understanding and adapting to customers needs and buying behaviors are of paramount importance. Customers at the conference highlighted three specific trends behind this general picture - all having grown in importance since last year: 1) Customers are continuing to shrink their IT spend; 2) C-level executives, particularly the CFO, have increasing influence and control over IT decisions; and 3) a continued emphasis on purchasing consolidation favors a few large players.

2001 Participant Growth Rates Fell Short of Projections; 2002 Participant Outlooks Positive Despite Contradictory Facts
Percent



Source: Sirius

CUSTOMER SPEND ON IT PROJECTS IS SHRINKING

Enterprise software purchases remain under pressure as organizations curtail the "excesses of the past." Customers have taken inventory of the assets and systems they have on hand today and are turning their attention to capturing the value from these investments. "Networks are running at only 20-40% utilization today," said keynote speaker Ed Zander, who further commented, "only 5-10% of IT spending will

be allocated towards pursuing 'new' projects."

Moreover, winning these new project dollars means beating out six other internal and external competitors: other potential IT projects, in-house initiatives, shelf software acquired during past 3 years, vendors from adjacent product categories, vendors in your own category, and indecision. Today's biggest competitor today may well be indecision. A CEO of a software company shared that "26 out of the past 30 proposals we have pursued resulted in 'no decision'." Customers that are making purchases are funding investments from hard asset consolidation savings and demanding extremely quick returns (e.g. two-three quarters to payback).

C-LEVEL EXECUTIVES TAKING CONTROL OF IT DECISIONS

The economic downturn, and resulting pressure on budgets, continues to force a change in enterprise IT decision making. Decision making power has shifted away from IT departments towards a risk averse set of C-level executives - oftentimes the CFO, CEO, and their boards. Not only are these C-level executives becoming increasingly "tech savvy", but they are also enforcing a new set of productivity and economic demands for investments. Whereas IT professionals in the past were not held responsible for demonstrating near-term returns, this group of decision makers emphasizes the requirement for a business and cost rationale in all decision making. Also, with more vendors chasing fewer deals, gaining access to C-level executives directly is difficult; their agendas are so packed that one panelist revealed that he has gone so far as to task two assistants with filtering email requests from salespeople requesting meetings.

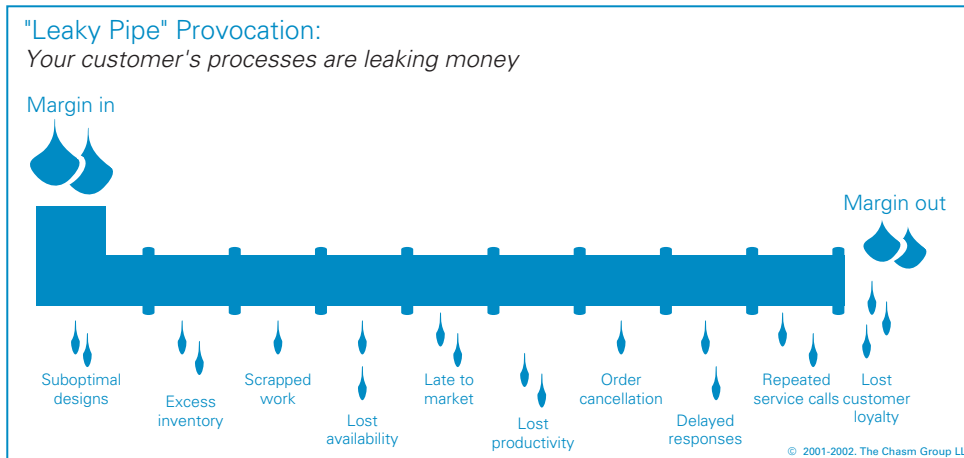
This shift in decision-making power requires a fundamental change in how sales and marketing professionals approach the customer. It is critical to present a concrete business case, not just a technology case. As one sales expert stated: "Don't talk to the monkey when the organ grinder is in the room." And gaining access to and influencing C-level executives is now a "must have" rather than a "nice to have."

CONTINUED EMPHASIS ON PURCHASING CONSOLIDATION FAVORS A FEW LARGE PLAYERS

Frustration with unfulfilled promises in the past has created a customer set that is simultaneously consolidating purchases into the hands of a few, trusted organizations and flexing their market power with

smaller organizations "because they can." The main beneficiaries of this shift have been trusted professionals and partners in the IT arena, such as the system integrators.

A Fortune 500 company's IT vice-president described a useful frame of reference regarding how purchasing organizations think of IT vendors. He said that there are three tiers of vendors, where even the key standards players (e.g., SAP, Siebel) are constantly on their toes. The top tier includes major system integrators and key standards players who account for 80% of the IT spend. This top tier is kept honest by constant competition from secondary providers who capture 15% of spend; the balance of the spend is tied up in win-lose ventures where the customer extracts tremendous effort and expense from small vendors looking to get a foothold in a Fortune 500 company's portfolio. Given such scenarios, the competition for IT spend - and the scrutiny of real benefits - has never been greater.



Effective selling approaches must adapt to this shift by incorporating a deep understanding of prospective customers' businesses. An Enterprise 2002 Conference speaker advised vendors "You've got to understand my business, how I make my money, and what my problems are." This, in turn, will require the sales force to actively listen to the customer - a skill many salespeople have lost. One sales expert went so far as to comment that "The opposite of talking for a salesperson is waiting to talk. To succeed today, you need to listen to identify the problem that needs to be solved."

Participants offered several tips on how to do this successfully. Conducting an upfront diagnostic, ideally with some nominal fees attached, is critical. The goal of these diagnostics should be to determine how the proposed effort will deliver sufficient economic returns to breakeven within two-three quarters. One sales executive counseled participants to "look for the line item in the budget that will be affected by your software." Primary process owners and key influencers should be viewed as partners throughout the diagnostic phase - to both build commitment and shared understanding of the potential benefits. A successful diagnostic will ensure that these influencers present the economic rationale to the C-level decision makers.

2. DEFINE A COMPELLING, SIMPLE, CUSTOMER-CENTRIC VALUE PROPOSITION

This year's conference reinforced and elevated the importance of the value-based selling theme highlighted last year - with a new emphasis on connecting with customers' pain spots. Virtually all panelists, speakers, and participants articulated this theme in one way or another - and surfaced four critical qualities that a compelling value proposition must deliver:

- **Directly address a core business issue.** Access to decision makers today requires addressing a core issue which is a source of both business and emotional pain for the top-level executive. "You need to have a power sponsor with an emotional, almost embarrassing, problem you can solve".
- **Define your offering in terms of a business category and unique position.** The need to "identify yourself within a category that matters" was emphasized numerous times by presenters and panelists. Overwhelmed with a tremendous number of vendor choices today, decision makers bucket vendors into categories or market containers. The best vendors today will do this work for the customer - explicitly communicating in which category they compete, their position relative to the competition, and their unique sources of competitive advantage.
- **Deliver real returns in the near term.** As a CEO and Chairman of a software firm commented, "the days of over-promising and under-delivering are over." Customers are demanding quick and measurable economic benefits from all IT investments - with some considering only those investments that break even within a matter of months.
- **Communicate simply.** Time is almost as precious as investment dollars today - and vendors find themselves with only the elevator ride to the lobby to make their case. In the little time that is available, sales must deliver a message that resonates with the business executive and CFO, not just an IT executive. Practically, this requires that all vendors heed the advice given by an early-stage software vendor to "streamline and simplify communications down to a point where your case can be made in 30 seconds or less and simple enough that it can easily be retold." Messages ridden with technical terminology will be quickly forgotten; those that focus on business issues will be remembered.

3. SHIFT THE CUSTOMER ENTRY STRATEGY TOWARDS A "LAND AND EXPAND" MODEL

Given the large amounts of underutilized IT in place today, the customer appetite for business- changing applications is at an all-time low. As one panelist commented, "Today you need to go for singles, not home runs." Customers are focusing on smaller projects and upgrades rather than major new spending initiatives.

A "land and expand" philosophy lends itself well to this environment. It requires that vendors prove they can deliver true economic results, on time, against a smaller first initiative in order to build credibility. Proliferating and institutionalizing this first success across an organization is a necessary precursor to being considered for larger efforts down the road.

A VP of Marketing for a major technology company described how this model was utilized by one of its vendors during a recent CRM implementation. The 12-week breakeven and 300% return on investment on hard asset costs realized during a short-term commitment turned into a longer-term commitment. Key to this transition was the credibility built during the initial trial period and the proactive stance that the vendor took in offering to track and calculate the ROI on the investments made.

Succeeding with this "land and expand" model will require that vendors strike the right balance between addressing a core business issue that resonates with C-level executive and breaking that issue into small, low-risk modules of implementation. Large monolithic architectures will need to be parsed and re-designed to support this approach and to reflect how the customer is consuming IT today.

4. ELEVATE THE IMPORTANCE OF CLIENT REFERENCES AND INVOLVEMENT

Over 80% of last year's conference participants viewed customer references as the most effective customer acquisition tool. The need for these references has grown even greater this past year - "reference customers are an invaluable asset in future negotiations." Despite this shared belief, only 17% of participants rated client feedback as an organizational strength, and client feedback was the largest marketing budget decrease in 2002.

The chief marketing officer from a major B2B e-commerce player provided participants with a powerful case example of how to attain and leverage client references. Recognizing that the top question vendors must answer to secure a deal today is "who else has implemented this system successfully?" his organization chose to invest in creating a database of implementation results across its client portfolio. To demonstrate credible results to prospective customers, the database is administered and managed by a third party. This database has enabled the organization to not only provide would-be clients with visibility into the expected impact of its products - but has also enabled it to proactively intervene where implementation is failing to deliver the promised impact.

The investment and attention dedicated to the issue of client references described above should be remembered as organizations prepare their 2003 budgets. Strong references do not just happen; they require investment and attention. As one presenter said, "you can't take a low cost commodity approach to your best customers and partners." Companies must actively work with their accounts to benchmark performance prior to implementation and to ensure that their software is successfully implemented and delivers the promised benefits. Again, a managing director from a leading VC urged vendors to "train your customers to articulate the

value they received in your terms and your metrics." In today's ROI-driven sales environment, the ability to cite true value creation requires both ensuring and documenting implementation success.

5. FOCUS ON LEAD GENERATION WITH A RIGOROUS LEAD PRIORITIZATION PROCESS

The time and energy dedicated to won versus lost deals today does not differ dramatically for many software enterprises. Yet, "chasing an un-closable deal is a major error in today's down market." Consistent focus on opportunities - not just at the end of the quarter - smoothes demand and lets companies escape the end-of-the-quarter phenomenon, in which 60% or more of revenue closes in the last 2 or 3 weeks of the quarter.

Last year's advice was repeated again this year: pipeline reviews need to be disciplined, executed weekly, and focused on moving opportunities through the sales process. Senior management must be involved in the reviews and, in the case of start-ups, sometimes even the board must get involved. The nature of resources deployed to any given meeting must be explicitly tied to the status or level of meeting being conducted. Marketing must ensure sales efforts are focused on the best opportunities and sales must be willing to focus their efforts and to abandon low potential sales. Collectively, these actions will ensure that limited resources are not being wasted on the "un-closable" deals.

6. RIGHT-SIZE, TRAIN, AND TURNOVER SALES PERSONNEL TO ADDRESS SKILL GAPS

The core sales and marketing skill requirements have changed fundamentally from gathering purchase orders to hunting for new business. Against this backdrop, 56% of conference participants worried that their lead-generation skills are below average. While in today's environment you "have to pick up the phone and call a stranger," a sales expert worried that today's sales force is comprised of "too many bird dogs that are getting old and prefer to chomp on the bones on the porch rather than get out and hunt."

Organizations must begin by first rationalizing their sales force to an appropriate size. One software executive emphatically declared that organizations must: "Rationalize sales - [you] can't sell your way out of a recession." All organizations must take stock of their talent, and turnover those who are coasting on the heels of star performers.

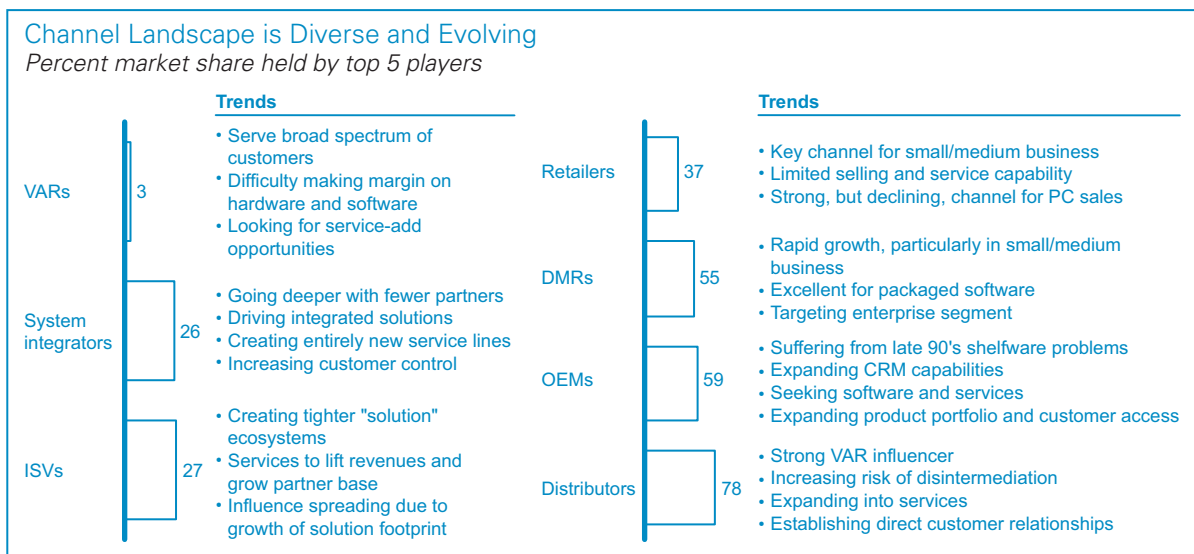
Once this rationalization has taken place, companies must retool for this challenging environment. For those salespeople that remain, creative and aggressive training programs will need to be pursued to build the hunting and value driven sales skills required. For some, this will be a natural transition. Others may need a

more dramatic course of action, such as the program one panelist described whereby all salespeople spend one day a week telemarketing to rebuild their listening and hunting skills. Secondly, compensation plans must be retooled to ensure co-operation across the sales force rather than competition for the same deal. Finally, those organizations that choose to capitalize on international growth opportunities must remember one panelist's advice: "[international] rules of engagement differ dramatically from the US. Rules and behaviors that work at home can not be imposed abroad - invest in the right people and local expertise."

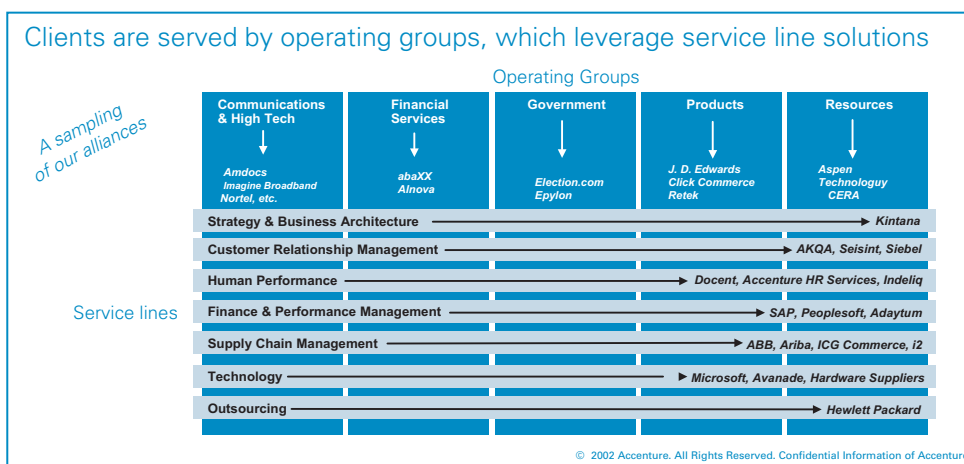
7. ELEVATE THE IMPORTANCE OF PARTNERSHIPS

The importance of partnerships continues to grow, as customers renew their focus on preferred partners and purchasing consolidation. For organizations with sales under \$100 million, over 40% of enterprise sales are derived through channel partners today. Furthermore, according to an industry leading SI, "enterprises with dedicated alliance management functions achieved a 25% higher long-term success rate ... and generated almost four times the market wealth."

The partner landscape is diverse and evolving, as channels adapt to keep up with the market. Choosing the right partner requires a deep understanding of the key trends impacting each channel and careful selection of which channel best fits with your customers' and organization's needs. While issues vary by channel, four trends cut across the landscape: growing tension between direct and indirect, financial distress of many smaller channel players, increasing concentration within channels, and an increasing need for partners to deliver distinctive services/vertical capabilities.



Becoming part of an organization's core architecture or system of record is critical for long-term success. Increasingly, organizations are turning to system integrators to re-architect their systems. SI's, in turn, rely upon a managed alliance process to deliver the best business results to a client. Taking advantage of this highly leveraged partnership model, however, requires navigating a complex organizational map. An industry leading SI, for example, divides its solution space along both operating group and service lines specializations, creating 35 potential white spaces within which vendors can partner. Vendors must identify upfront how and where their capabilities will plug into the broader system integrator's portfolio of solutions.



With over 50% of alliances failing, participants offered 5 tips on how to ensure that your partnership will be among the alliances that succeed:

- **Know thy partner, know thyself.** Many companies develop and launch channel strategies without truly understanding the needs and capabilities of the partners with which they work, or how best to use these channel partners to complement their own internal capabilities. The best companies invest in understanding both their partner's and their own motivations, including capabilities, segments served, and capacity available to support products.
- **Say what you'll do, do what you say.** Many companies are surprisingly unclear about their overall channel strategy. Companies are often unable to provide the channel with a clear sense of the rules of engagement and how the company and the partners are expected to work together. To avoid this, it's critical that companies take the time to articulate a clear channel strategy and their expectations, including the role of the channel versus the role of the field sales force, and then stick to the strategy for more than just a few months or a year.

- **Focus.** Often times companies try to be all things to all partners, with programs and support available to all and with a belief that more partners is better than fewer for reaching the maximum breadth of customers. However, the best companies focus their channel programs and resources against the subset of partners who can really make a difference. They are willing to close off options to avoid diluting the impact of too many channel investments.
- **Spend money to make money.** Many companies assume that if their product is available to the channel, it will be embraced and sold. However, most channel partners are selling multiple products, have a defined set of skills, and are trying to optimize around profitability. To truly capture the attention and commitment of the channel requires investment to build both mind share and capabilities. This always requires putting in place a dedicated, continuous relationship management team. It may mean looking for ways of promoting oneself to partners through tailored marketing efforts that drive new demand into the partner or through rep-level incentives that encourage partner sales reps to focus more of their energies on your product. In addition, it may require investing time and energy into tailoring products to fit a partner's solution space and consider offering exclusive rights. To put it simply, there is no free lunch.
- **Monitor.** Unlike a couple of years ago, a press release doesn't equal a partnership; partnerships must be made real through rigorous and objective goal setting and monitoring. It's important to track the progress made against goals rigorously and objectively, to understand which partners are truly making a difference and which ones are not. It's equally important to ensure that the metrics used are appropriately tailored to the type of alliance being pursued.

outlook for the future

Despite the challenges of the current environment, an underlying optimism about the prospects for the software business and its professionals cut across the 2 days of conversations in Half Moon Bay. Three final takeaways emerged:

Technology is the right business for the long run. All participants concurred that the technology sector will remain the growth engine for the economy in the future. Great companies get stronger during tough economic times by establishing a foothold for the future. Great new companies also get started during down economies - the bar is higher, but those that succeed are destined to be extremely competitive when the outlook improves.

IP will be the primary driver of future value creation. While the overall economic conditions call for prudent spending, dramatic reductions in intellectual property investments are ill advised. When the economic tide turns, those organizations with superior IP will rise to the top. "If you've got a good idea, you need to go for it, even today."

Casting an eye forward to the future, a VC panelist believes that survivors will flourish in an environment of reduced competition. "The R&D cost-cutting measures which public companies are undertaking today will come full circle ... and those that focus on building a niche today will flourish in the next growth period."

Prepare yourself for the next challenge ahead. Increasingly, companies will be asking their sales and marketing professionals to broaden their responsibilities to both overcome current challenges and to prepare for leadership roles in the future. In embarking on this path, participants should take to heart the lessons learned by conference speakers. Ed Zander perhaps summed it up best in his advice to conference participants: keep it simple but prioritize every day, quarter, and year. As you think about the year ahead, be sure to constantly reprioritize, to emphasize ongoing communication, and to act with passion and confidence.

