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The Software Industry's Other Transition

By Paul Holland, General Partner, Foundation Capital

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Recently, a new breed of software companies has emerged that help customers grow the top line. By associating their value proposition with increase in revenues, they've been able to appeal to the strategic interests of senior executives and consequently their average selling prices far exceed that of the typical industry average. Technology companies today are hard at work to help their customers make more money vs. simply slashing IT expenditures.

I chose a challenging time to launch my career in venture capital. It was three weeks after 9-11, and the nation was reeling. Businesses of all types were trying to figure out what to do next, let alone the country as a whole.

The software industry was already deep in a post-bubble hangover. E-commerce companies had come and gone despite bold predictions to reshape the future of all commerce. Young software companies hoping to attract VC funding and get off the ground - I would say 95% - were focused on providing solutions for cost cutting or compliance. Less than 5% were looking at other business models.

Fast forward to today. Over the last few quarters I - and many of my venture colleagues - have observed a correction that seems long overdue; namely, the emergence of a new breed of software companies that provide solutions to help its customers grow the top line.

For example, we invested in a company that tells its prospective customers "you will pay us hundreds of thousands or millions of dollars, but in return we will help you make tens or perhaps even hundreds of millions in additional revenue per year." By associating their value proposition with increase in revenues, they've been able to build a business that appeals to the strategic interests of senior executives and consequently their average selling prices far exceed that of the typical industry average.

Turbo Charging the Top Line

Edge Dynamics is one of our portfolio companies currently focused on the life sciences space that provides its customers with revenue improvements through better channel control. In addition to improving the topline, they also help their customers address critical issues of regulatory compliance and patient safety.

Edge is delivering a powerful value proposition to its customers which today include many of the leading pharmaceutical manufacturers, such as Bristol-Myers Squibb, King Pharmaceuticals, Purdue Pharma, and Sankyo Pharma, to name a few.

Building Software Companies... One Leader at a Time.

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By helping these companies more effectively manage and enforce their pay-for-performance channel agreements as well as reduce speculative buying, Edge is able to deliver revenue increase of 1% or more to their customers. Considering the fact that the top 20 pharma companies range from \$5B+ to \$50B+ in revenues and even the SME segment consists of companies with a minimum of \$100M in revenues, this can significantly enhance financial performance. In the case of one top-10 pharma manufacturer who is using the Edge solution to address critical issues ranging from channel control to regulatory compliance and patient safety, they've been able to quantify financial benefits of using Edge to the tune of \$1 million per business day.

Edge Dynamics is focused on Channel Commerce Management in Life Sciences today, but the company has a powerful business policy management engine that can easily extend to other industries as well in the future, including Consumer Goods.

Further, Edge Dynamics is one of the new breed of companies that is emerging with a hybrid business model that delivers technology to customers in multiple deployment options - software that can be available both on premise and on demand.

No More Sour Grapes

Another investment of ours, Novazone, helps its customers - in industries ranging from produce, food processing and poultry to pharmaceuticals, bottled water and manufacturing - increase revenues by using ozone-based solutions to improve the freshness and safety of food, water and other processes naturally without the use of chemicals.

The company incorporates an array of patented ozone technologies into complete, automated systems that are reliable and cost-effective. Novazone has more than 250 customers in 15 countries including Coca-Cola, Pepsi Cola, Arrowhead, Sun Pacific, Orchard View Farms, Paramount Farms, Safeway, Colgate-Palmolive, Procter & Gamble, and Wyeth Pharmaceuticals.

In recent months, Novazone has doubled down on the food industry, a \$3.3 billion market, where orders quadrupled in just two months. The benefits are real. For example, spoilage is a big issue for Chilean grape producers shipping their produce overseas to Europe. By adding Novazone ozone-based purification technology to each shipping container, spoilage is slashed from 20% to almost nothing, which adds \$5,000 of value to a \$25,000 shipment.

Don't Aggravate Customers - Sell Them More

In a third example, shortly after the bubble, companies handling front line customer support via outsourced agents and automated voice systems found themselves in a death spiral. Reduced demand drove down the volume of transactions, which further eroded economies of scale in the customer support function. To correct this problem, companies looked to "fix" the cost side of the equation rather than strive for revenue increases. They replaced talented US based outsourced agents with lower quality offshore talent and additionally drove for higher automation to eliminate agents all together. The result was a dramatic decrease in customer satisfaction for the companies and a rapidly eroding market for agent outsourcers and speech IVR vendors.

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In 2003, partly out of desperation to find alternative uses for agent talent and to justify speech IVR investments, a select number of companies switched their message from cost reduction to revenue generation and up selling. Agents were trained on appropriate up sell messages, "I can consolidate your accounts and offer you a lower monthly APR if you sign up for our Platinum Card. Are you interested?" CRM systems were dusted off and put to good use in scoring potential callers and matching them with likely offers and IVRs were modified to pull callers out of the call flow and get them to agents who were idle and had proven track records of successful up-selling. One notable example, LiveOps, utilizes highly skilled home-based agents to upsell new products and services to inbound callers of customer services.

Successful up selling has significantly reduced call center budget requirements and, in a few cases, has turned these cost centers into revenue centers.

Final Thoughts

These are just a few examples where technology companies are hard at work to help their customers make more money vs. simply slashing IT expenditures to the bone. The challenge is in finding new value propositions - significant business needs that, with the help of technology, can be addressed. It is my hope that, in Silicon Valley and beyond, we will see more new companies take this approach.

Paul Holland is a General Partner with Foundation Capital. His primary focus is to help software start-ups go from zero to \$100M in revenue. He helped take two venture-funded software start-ups, Kana Communications (KANA), and Pure Software (RATL), public. Paul currently serves on the board of directors for Edge Dynamics, Ketera, TuVox, Conformia, Codefast, Bella Pictures, Mendocino Software, and Simply Hired; and previously for Talking Blocks (recently acquired by Hewlett-Packard) and RouteScience (recently acquired by Avaya). For article feedback, contact Paul at pholland@foundationcap.com