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PRAGMATIC MARKETING'S

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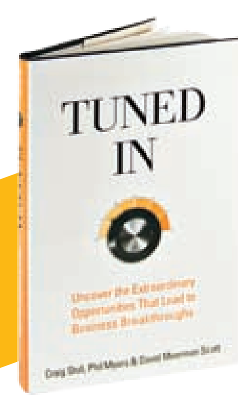

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50,000 product management and marketing professionals have learned the Pragmatic Marketing Framework, a common sense approach to finding unresolved problems, creating breakthrough experiences, and launching market resonators. Over 90% of alumni rate the training as essential or very useful to their careers.

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15 Years Later...

How a simple phrase came to define a global company

"Your opinion, although interesting, is irrelevant."

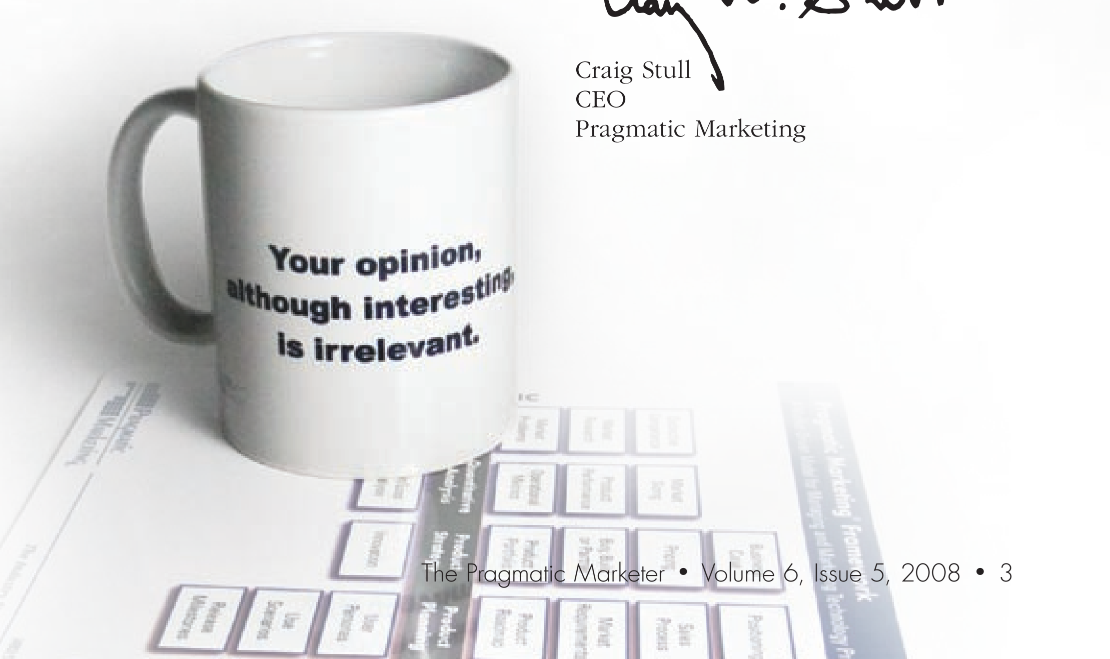
In December 1993, in a small meeting room in Herndon, VA, I unveiled to the world *the* Framework for successful product management. Okay, so there were only 12 product management students in the room but those early adopters had the right idea because they knew how critical it was, even back then, to understand that the strategic role of product manager was not based on opinions but market facts. Fifteen years and nearly 50,000 students later, Pragmatic Marketing has become the standard for defining roles and responsibilities for product management and marketing at more than 4,000 technology companies around the world.

Since then, we have added more seminars and onsite workshops, created a full-service consulting team, launched this magazine (now in its 6th year), wrote the best-selling book *Tuned In: Uncover the Extraordinary Opportunities That Lead to Business Breakthroughs* and created an online community for 45,000 visitors per month. Recognizing this growth, *Inc.* magazine named Pragmatic Marketing one of America's fastest growing private companies three times in the last eight years.

Looking to the future, we have a number of new and exciting initiatives planned and look forward to you helping us celebrate our next 15 years.

Craig W. Stull

Craig Stull
CEO
Pragmatic Marketing



Living in an Agile World:

the Strategic Role of Product Management when Development goes Agile

By Steve Johnson and Luke Hohmann

While software development teams have been moving toward agile methods for years, many product managers are only now becoming aware of it. An agile approach applies collaborative and continuous improvement concepts to software development. It emphasizes close collaboration between development teams and customers; frequent delivery of deployable code (in sprints); face-to-face communication with customers; tight, self-organizing teams; managing backlogs of user stories to reduce requirements churn; and identification of self-improvement opportunities.

There is no single, definitive "agile method." Agile teams tune practices and processes for themselves to create a method that is unique to their environment. Broadly, agile methods function as both an organizational philosophy and a set of development methodologies.

When you adopt agile development methods, you encounter new concepts, new artifacts, new planning methods, and new roles and relationships. It seems that agile teams do everything in a new way. And, as you attempt to integrate agile into your existing systems, you'll also attempt to map these new concepts to your old, familiar concepts. Requirements are now stories; iterations are now sprints.

And a product manager is now called a *Product Owner*… right?

Wrong!

Companies adopting agile methods know that product teams need a voice representing the customer. Developers need personas, market problems, and most of all, a prioritized list of requirements. Agile methods advocate a role called ***product owner*** to support the product team with customer and market information. Since the closest equivalent to product owner in most companies is the product manager, it seems natural to equate the two.

But product owner and product manager are ***not*** the same. In fact, a product owner's responsibilities are just a small subset of product management.

What is a product owner?

The product owner is a new role, created and defined by the Scrum Alliance (www.scrumalliance.org). Product owners live full-time with development teams—elaborating users' stories, managing sprint-level backlogs, expanding specifications, and interpreting product vision.

Most product companies already have staff members with similar skills, such as a requirements analyst or business analyst (titles and job descriptions have shifted over time, but product companies have always needed to provide developers with detailed, feature-level information and UI guidance; someone with intimate customer experience is always necessary to build great software).

The product owner addresses the agile development teams' intense need for real-time input on user stories, user experience/user interface, and requirements.

Spotting fundamental flaws

Product owners can close the gap between a product manager's inbound role (that is, understanding the needs of the marketplace) and the development team's need for product direction (that is, understanding the detail of personas and their problems).

There are, however, a few fundamentally flawed assumptions built into the product owner role that experienced product managers immediately spot. These flaws become abundantly clear when the product owner role is aligned against pre-existing functions (e.g., requirements analyst), which we would not expect to drive strategy:

1. **The top determinant of a product's revenue success is whether it meets real customer needs.** Regardless of what the development team builds, a product without interested customers is a failure. It's the agile product manager's primary job to meet existing customers and potential prospects face-to-face and deeply understand what they want.

   Throughout the development process, the product manager represents customers against short-term trade-offs. If there is a product owner, he or she needs to channel the product manager throughout the day, avoiding short-term thinking that can come from living with Development every day and answering only to the technical team. *Remember: You can't understand customers without getting out of the office.*

2. **Product owners can't rank backlog based on ROI.** In fact, this task is impossible for anyone to do, since real business metrics and financial projections don't exist at the feature/backlog/item level. Researchers tell us that the only way to assign revenue at the feature level is to perform conjoint analysis on every feature. Will any company perform this type of research for each product project? Probably not.

   A broader and more rigorous backlog ranking approach, "prioritizing for profit," considers market opportunity and corporate strategic fit at the product level. Most important to this process is someone who can prioritize the issues of all stakeholders, considering the needs of buyer and user personas, key new markets, and issues of internal stakeholders in Sales, Marketing, Support, Development, and others.

   Every release must have at least one feature (story, improvement) requested by each major stakeholder group. Figuring out the features for a release is an organizational challenge, not a technical challenge. The market-driven product manager should determine what goes into the final product; a product owner cannot.

3. **Real revenue is driven by pricing and packaging.** Product managers typically own pricing; product owners rarely do. And unless you have a seasoned product manager driving software pricing and packaging, you' be leaving revenue on the table.

4. **Creating successful benefits and feature descriptions that truly sell products requires a detailed understanding of the technology and a detailed appreciation of the customers' problem.** This takes lots of practice, hands-on field experience, and a clear view from both sides. In our experience, internally promoted technical staff members almost never get this right. Marketing materials created under this approach are often feature-heavy, too technical, and fail to motivate the exchange of money.

In cases where large projects (products) are divided into multiple teams, it makes good sense to have a product owner (or requirements analyst or business analyst) assigned to each team—just as we would have a development manager and program manager (scrum master) and QA manager assigned to each team. The point of integration for these teams, though, is a single product manager. When the executives demand "one throat to choke," it's the product manager who is responsible for overall success of the result. ➔

Failure modes

Over the short term, we can easily see product owners operating without close alignment with a product manager. Over the course of a release—or a half-dozen sprints—we repeatedly see a few failure modes:

- **Trading off company-wide strategic product fit in favor of product-level features.** Good product managers look across the product line for ways to make the overall collection more valuable. Hermetically-sealed product teams tend toward local optimization: what's best for my release plan—without regard to portfolio-level needs. Yet Sales and Marketing are constantly trying to cross-sell existing products into the current customer base. Without some strategic thinking sneaking into every sprint-level prioritization, the company loses many chances to make money through product bundling, cross-selling, integrated features, and old-fashioned customer opportunities.
- **Assuming a few showcase customers represent the broader market.** Experienced product managers know that one customer is not a market—unless you are a custom development shop or internal IT group. It's easiest to believe that three customers previewing your

Do I *Really* Need a Product Owner? *By Rich Mironov*

Many agile development teams think they need a product owner for every project, but product owners address only a small portion of the agile product management challenge. The product owner role has been created by the agile development community to focus on the hour-by-hour demands of an agile team—even though software product companies typically have a product manager and other existing resources to meet those needs.

A product manager's focus is creating products that are delivered to a market full of customers, not one-time projects delivered to a single customer. And if we have agile product managers assigned to the product, do we *ever* need a product owner?

A thoughtful answer needs context, and must be based on the structure and talents of the team. Agile development is scaling beyond single co-located teams and now includes revenue-driven product organizations. So let's consider four situations:

1. **Single, co-located agile team. One agile product manager can handle all of the demands from a product team that sits together.** In fact, one agile product manager should be able to manage two product teams in the same building—even factoring in travel, customer visits, and demands from Marketing/Sales. We routinely (and confidently) allocate 50% of an experienced agile product manager to each development team. When everyone sits together, there's no need for a product owner (or requirements analyst or business analyst) on the team to supplement the agile product manager.
2. **Large, co-located projects with multiple development teams. As products and projects grow, Development has to create additional agile teams.** This approach is sometimes called the "scrum of scrums" approach, where one backlog is split among three or more groups, each of which has a development manager, project manager (scrum master), QA group, etc. The experience level of the agile product manager matters here, as well as scale, team cohesiveness, and whether the groups have radically different technical challenges. It's critically important that one person (the agile product manager) continues to be fully responsible for the resulting product and its revenue success, but it may be time to provide some help.

   Most product companies already have a range of resources and talents to apply, so they might have a junior product manager needing hands-on agile experience under the guidance of a seasoned agile product manager; business analysts and requirements analysts with intimate knowledge of the specific customer requirements; field sales engineers on loan for individual product releases; or someone formally designated as a product owner. In all cases, the product manager is delegating specific authority and is responsible for overall execution, coordination, priorities, and customer satisfaction. The product owner (by any name) is assigned to remove roadblocks, research questions, elaborate, clarify, motivate, and assist—but also to raise issues of substance with the agile product manager. So, product owners are optional for complex, co-located projects. Product managers need to ask for help if they need it, and executives should provide it.
3. **Geographically distributed development teams.** When Development is split across time zones and continents, one product manager can't possibly provide the face-to-face daily input and leadership that agile development demands. Even if the sub-projects are part of one product's overall architecture—and one agile product manager's overall vision—you need leadership on the ground in each location to keep the work of agile moving. This usually includes a development manager, a project manager (scrum master), test/QA manager, and a product owner. Here, the company should provide some formal agile training to resources such as business analysts, since they'll be without much in-person guidance from their agile product manager.

   Plane flights are too slow, phone calls too impersonal, and hour-by-hour task assignment changes posted to the walls of the War Room too complicated to manage at a product represent the entire market. Product managers have had this awareness beaten into their heads after thousands of dissimilar customer meetings and presentations. First-time product owners tend to be naïve (or hopeful) that the input they get is both true and universal.

- **Adding new features without pricing them.** Product owners worry about completing the sprint; product managers worry about making money. Every new feature is an opportunity to re-bundle, re-price, or encourage customers to upgrade in order to capture more revenue.
- **Starving the product architecture in favor of customer-visible features.** Product managers and product owners alike often neglect the architectural element—forgetting to incorporate system improvements into the backlog. To ensure that system internals, architecture, "technical debt," and other technical issues are kept in the priority, we add the architecture itself as a stakeholder. That is how you keep the architecture healthy—both now and four releases from now.
- **Wandering from the roadmap.** Development teams (and their product owners) concentrate on the next release, but often lose sight of the 12- to 18-month roadmap and goals that achieve business results.

➔

distance. Having someone in each office responsible for keeping the team clear on user stories/backlogs seems essential. As above, this quickly spins out of control unless the product owner (or equivalent) is tightly aligned with the remote agile product manager, and quickly escalates issues to that person. So, a product owner seems necessary for each remotely located development team.

4. **My product manager isn't doing a good job and doesn't know agile development.** Ask most agile development managers in private, and this is what they *really* worry about. They are way ahead of their (non-agile) product managers and are used to slow, second-hand, poor-quality customer input. Hiring a product owner is one way of protecting the team from bad product management. The thinking goes, "We still won't have good market inputs or truly customer-driven backlogs, but at least we'll manage our sprints well, and our developer-side collaboration will deliver something usable."

   This situation is all about trust, skills, team-building, and managers being brave enough to say what they think. It should not be about creating another new title in order to cover for a failing product manager.

   Coming back to our core beliefs as "agilists" (we value individuals and interactions over processes and tools; we value collaboration over contract negotiation), the leaders of Development and Product Management need to step up with honest discussions such as:

   - "Our product managers don't have any agile training. Let's get them all to class this month so we can stop complaining about it."
   - "We need more of a kick-start, especially since project timelines are at risk. Let's bring in an outside agile product manager for two or three iterations who can show us how it's done while getting everything back on track."
   - "We all know that product manager X was barely competent doing waterfall, and is hopeless under agile. Let's replace him instead of spreading the load."
   - "Development doesn't understand why product managers can't be here at Headquarters every single day. Let's give the development team a half-day tutorial on what (else) product managers do, and why sitting at their desks every single day leads to inevitable strategic failure."
   - "Iteration Planning is always on Mondays and Retrospectives are always on Fridays. Can the agile product managers schedule more of their customer travel and sales briefings mid-week?"
   - "Developers want to hear even more of what customers really say. If we promise not to say anything, can we sit in on your next few conference calls?"

   Product management veterans have seen similar reactions from other functional groups faced with weak product management teams. Marketing suddenly creates product marketing managers for select products rather than identifying the one product manager who's unable to get his or her features/benefits straight. Finance invents a "pricing czar" to fill in for product managers who stumble through the pricing and packaging process without leadership or strategy. Developers freely interpret vague requirements and hope they build marketable software.

   Said another way, product management is a very tough job, and we need to do it well. Creating product owners to cover our personal shortcomings or lack of agile training is treating the wrong disease. Let's make sure we're doing our best agile product management instead of meekly letting Development redefine our responsibilities. If we're short of trained, capable agile product managers, let's get busy recruiting and mentoring and training them to fill the real need.

So, do we really need a product owner?

Sometimes—in the right context and with distributed development teams that need real-time, local help. Never staff up a revenue-driven product without an agile product manager, but don't assume that every agile team needs a product owner.

Product management is outwardly focused

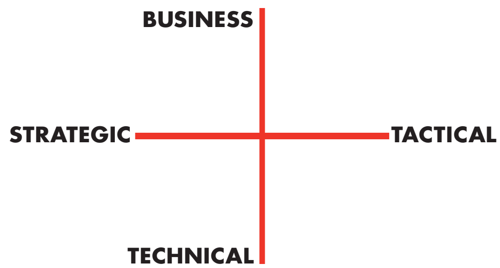
Developers and engineers tend to see product managers as internal technical resources, to be used as much for project management as product management. For some companies, agile development methods seem to have made the product management role even more internally focused—with product managers getting pulled into deeper tactical, technical activities.

But spending so much time with internal technical teams means less time spent outside the company in the market. As Pragmatic Marketing-trained product managers know, you don't learn anything about the market while sitting at your desk.

But there's more to product management than supporting Development. Product managers also work with Sales, Marketing, Support, and other departments. Most of all, astute product managers work closely with the company's senior executives.

The activity spectrum of product management

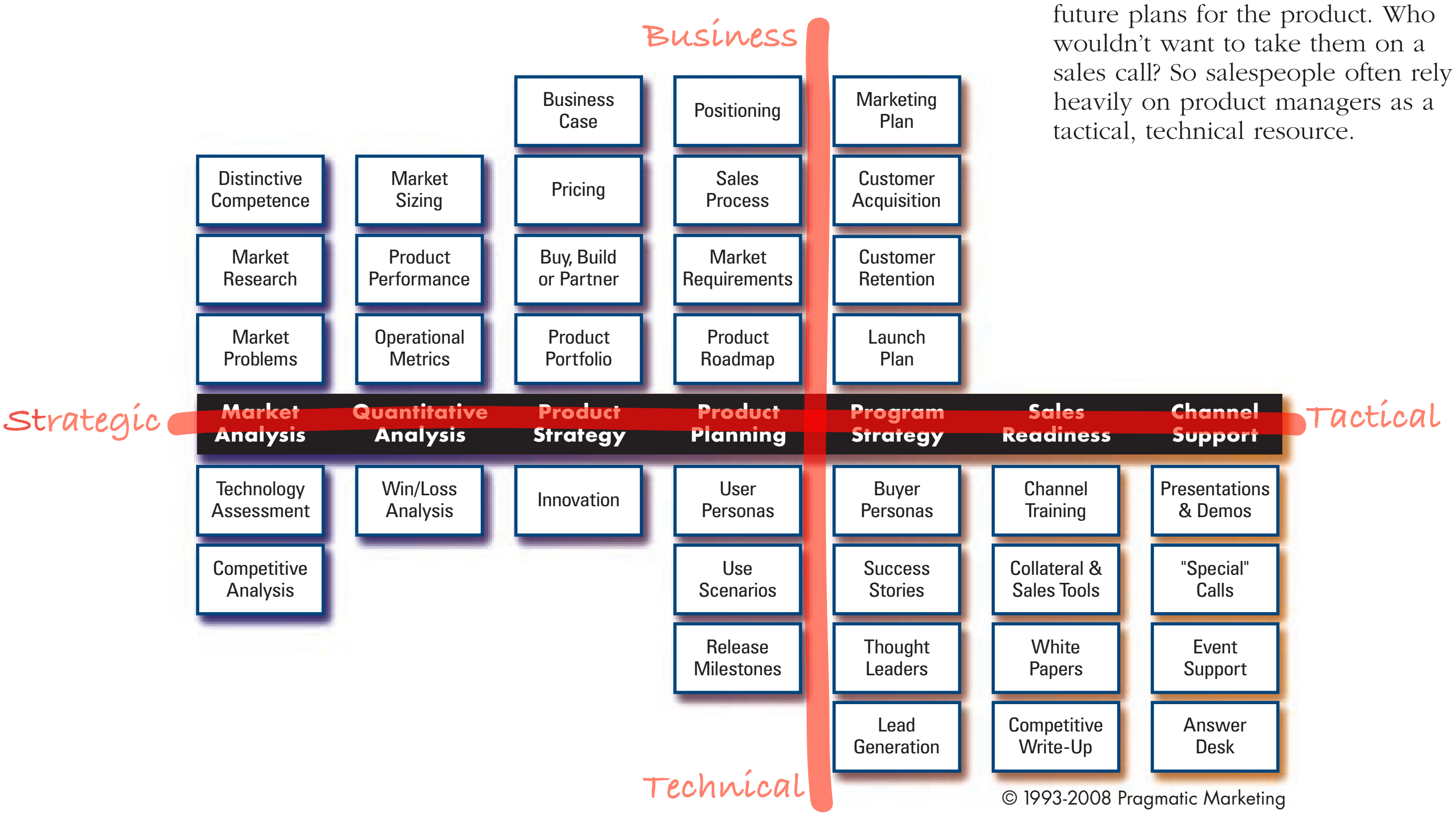
The activities of product management span the range from strategic to tactical. Some product management activities are focused on the business of the product, while others are centered more on the technical aspects of the product. Applying this concept to a grid looks like the accompanying quadrant diagram:



With this grid in mind, there are four ways that people within the organization typically look at product managers:

- **How Development sees product managers: Technical/Strategic.** Developers and other technical colleagues tend to see product managers (and therefore, the product owner role) as a strategic, technical resource. A developer's view of product management might include market requirements, technology assessment, definition of user personas, and other technical artifacts. In many cases, the team realizes that the product manager is a market encyclopedia and so, product teams want a customer expert to be available all day, every day.

- **How Sales sees product managers: Technical/Tactical.** Have you ever known a sales person who didn't see everyone in the company an available resource for selling? Product managers are the preferred source for great product demos—they can explain the internals of existing features and they know the future plans for the product. Who wouldn't want to take them on a sales call? So salespeople often rely heavily on product managers as a tactical, technical resource.



- **How Marketing sees product managers: Business/Tactical.** In most vendor organizations, the Marketing department is staffed with experts in *promotion* rather than experts in *technology*. And this makes sense. But without some technical abilities, these promotions experts can't do a very good job of positioning and messaging. And technical product managers and product owners are usually terrible at it too. That's why so many companies recruit product managers (or product marketing managers) into the marketing department. Marketing people rely on product management for tactical, business-oriented information in support of their promotional, go-to-market plans.
- **How the executive team sees product managers: Business/Strategic.** Executive management relies on product management as a strategic resource—the source for strategy and business thinking at the product level. The executive team wants to see business plans and product roadmaps.

Rather than defining one role, product management actually span four disciplines.

Mapping product management activities

Product management is often ill defined and poorly understood in technology companies; yet the role can be one that propels the company to the next level of performance. Rather than running the business like a hobby, effective product managers focus on both the business and the technical aspects of product management.

The Pragmatic Marketing Framework describes the activities, artifacts, and practices for defining technology products and delivering them to market. From market analysis to channel support, product management entails activities ranging from strategic to tactical and from less technical to quite technical. These activities align loosely with the expectations of the four groups: Development, Sales, Marketing, and corporate executives.

The most common organizational format is for one product manager to perform all of the activities of the entire framework. It's a big job, but a satisfying one. It is the president of the product (or perhaps a better metaphor is the parent of the product). In any case, it's also what the "agilists" call a "single, wringable neck." A single voice of priority.

With one product manager, everyone knows where to go for the definitive answer. But… as your business grows larger, the demands on this single person grow greater and greater, and soon exceed the number of hours available in a day.

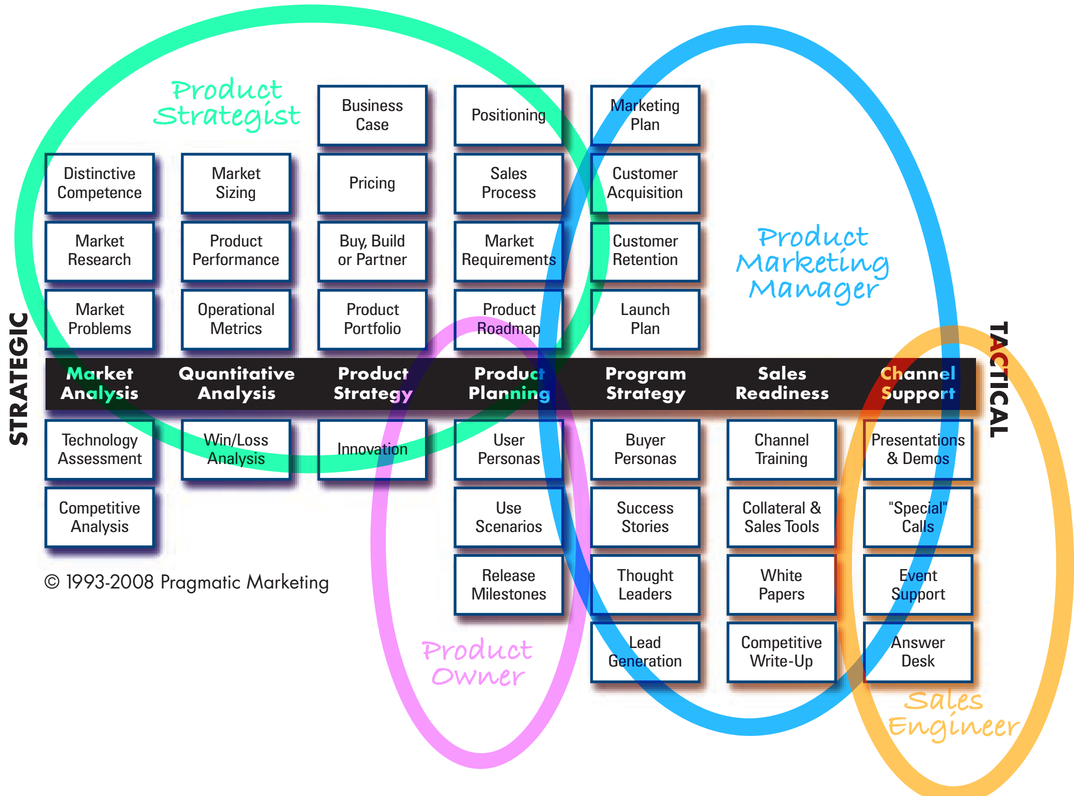
The four roles of a product manager

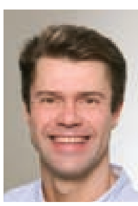
There are four distinct roles played by the product manager, which is a much larger function than that defined by a product owner. The four most common titles are product strategist, product marketing manager, product owner, and sales engineer. The accompanying diagram shows the four roles aligned with the Pragmatic Marketing Framework.

Each organization adapts these titles and the associated activities to the way it does business. If you're new to this product management framework, download the e-book *The Strategic Role of Product Management* at www.pragmaticmarketing.com/srpm.

It is common for product owners to report to the development organization, but product managers are increasingly reporting into their own department—separate from Development and from Marketing.

As you can see, the role of product management includes the responsibilities of product owner—plus much more. The practical product manager serves as a hub of market and product information, relies on business and technical savvy, and works closely with Development, Marketing, Sales, and other departments. Most of all, a product manager is the executive team's eyes and ears at the product level, making strategic decisions on the future of the product. TPM





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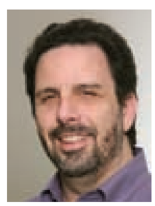

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The Industry Standard for Technology Product Management and Marketing

Practical Rules for

By Maureen Rogers

Some rules just aren't meant to be broken

(Part III)

Editor's Note: In Volume 6 Issue 4, Maureen Rogers applied her own interpretations and personal experiences of Pragmatic Marketing's 20 rules for product management success in Part II of her series of articles on this topic. In Part III, she continues the series with Rules 11-15.

Pragmatic Marketing's Practical Product Management seminar not only teaches product managers about the renowned Pragmatic Framework, it offers attendees 20 rules for product management success. Continuing our series of rules that just aren't meant to be broken, Rules 11-15 cover such critical topics as win/loss analysis, making a business case, and positioning your product effectively. Read on.

RULE #11

Don't expect your sales channel to conduct win/loss analysis.

I wish I had a Euro for every time I sat through a pipeline review meeting and, as last month's hot prospects transitioned into the "L" column, asked the question "Why'd we lose?"

I should have saved my breath. After all, just as the answer to "Why'd we win?" always turns out to be "superior salesmanship," the "Why'd we lose?" answer is invariably "Our price was too high," or "Our product stinks," or "They went with somebody else," or "They did nothing."

Let's face it, it's just not in the nature of most salespeople to analyze why a sale did or did not happen. Plus, you want and need your salespeople to look forward, not backward.

So who does win/loss analysis—and how do you go about it?

Ideally, your product marketing or product management team should conduct win/loss analysis. Alternatively, if you really think people are reluctant to be candid when talking with someone in-house, you should hire a third party.

Analysis should begin with a mini-debrief with the salesperson and (better yet) the sales engineer. An initial impression by those closest to the deal may yield a useful avenue for your questioning.

Prepare a specific list of questions—about your product, pricing, and process—to review with every prospect. If you have a complex sales process that involves many different people on the buying side—influencers, decision-makers, purchasers—try to talk to several of them. Realistically, this isn't always feasible—especially after a loss. And remember that a good, candid conversation with your prime sponsor is worth plenty; so don't get greedy.

Beyond specific questions about product, pricing, and process, try to flat out ask lost customers the following questions: What we could have done better? What would it have taken to win? Where did the competition outshine us? For a win, ask those same questions about the competitor.

Win/loss conversations should be brief (no more than 10-15 minutes), and they should take place within a week or two after the decision is made. Conversations are ideal, but email response works just fine.

It goes without saying that the information should be kept in some sort of a system—and in a systematic fashion—so that you can make some sense of it as a whole and not just look at disparate information points. This analysis is not all that easy to do when you're looking at subjective information, but there's no point in collecting win/loss data unless you're planning to draw general inferences.

Here are some ways your win/loss analysis can help you:

- Determining which features you need to add to your product
- Refining your pricing
- Shaping your marketing message
- Homing in on a more sharply defined target market
- Improving your sales and marketing processes

Yes, lots of good things can and will come from win/loss analysis. Just don't ask your sales folks to do the heavy lifting for you.

RULE #12

The answer to most of your questions is not in the building.

During the dot.com era, I worked for a large Internet Services Provider (ISP) where rank-and-file marketing people rarely had access to customers and prospects. I had come there from a small software company, where I went regularly on sales calls and frequently spoke with customers, so I knew I was missing something.

In my three years with the ISP, I went on a handful of calls. Our sales model was multi-layered, and there were often three or four folks just from Sales on every call. No room in that clown car for another body! If Sales brought another body along, it was typically a technical expert or a product manager.

During those years when I was starved for the outside perspective, I did participate in many events, speaking on behalf of the company, so I was able to have some interaction with customers and prospects. But it was way too limited. I also met often with industry analysts—another good source of insight and information. But I really missed customer and prospect interaction.

Several times I created customer surveys, but was not allowed to speak with customers directly; I had to go through multiple layers of the customer support organization.

All in all, it made for a very high frustration level, in which I always felt I had my nose pressed up against the window glass—able to see, but not communicate with the world outside.

Fortunately, I developed good relationships with enough of the technical sales folks and sales engineers to get my questions answered. But it was not really the same as building good relationships with customers or hearing first-hand what prospects were saying.

You really do need to get out of the building to truly understand how people use your products and services and to appreciate the benefits they derive. You need to get out there to see which parts of your message customers respond to and which parts draw blanks—or leave them cold.*

Obviously, you also need to stick your head out to get a sense of what's happening in the economy and technology—both in general and with your industry, your market, and your competition, in particular. (Thankfully, the Internet gives us all the chance to get our heads a bit out there.)

None of this is to say that there's not important "stuff" that you can and should find out within your own four walls. There are definitely people who know things, and you should know who they are and how to tap them. But, when it comes right down to it, there's really just one question that can only be answered inside the building, and that's "How does it work?" For everything else, you need to look outside. →

* I read *Tuned In: Uncover the Extraordinary Opportunities That Lead to Business Breakthroughs*, by Craig Stull, Phil Myers & David Meerman Scott *after* I'd written this article. *Tuned In* makes the excellent point that, in addition to speaking with customers, you should also make sure you spend time with non-customers, since they represent the majority of the market.

RULE #13

Every "product" needs a product manager and a business case.

In my experience, most B2B technology companies do see that all their products have a product manager. Sometimes the product manager winds up with multiple products—which is okay if they're on the smallish side and in the same family. If the products are on the biggish side and not well related, it can lead to product attention deficit disorder. But, fortunately, most products tend to have product managers.

But those business cases...

Products start out in many ways.

Sometimes (especially in the software industry) they get developed by someone who thinks it's a good idea and just goes ahead and does it. If that's the case, the product manager may be tasked with creating a business case after the fact, trying to figure out the positioning and all that other good stuff that should have been determined before the product was created.

Sometimes a product starts out with a business case, but it never really gets evaluated—let alone updated. And if you don't bother to regularly update your product's business case—or create it anew—you run into a lot of dangers:

- Missed market opportunities
- Missed product enhancement opportunities
- Pricing that leaves $$$ on the table
- Putting too many resources on Product X and too few on Product Y
- Hanging on to a product that really should be on an end-of-life path

We all know how easy it is to keep chugging along, doing the same thing quarter after quarter, year after year. If you're a product manager, you probably know this drill by heart. You do your job. You cover all the bases: product requirements, project plan, documentation, product launch, sales tools, sales training, marketing programs, etc.

It's so darned easy never to take the time to critically examine your product's *raison d'etre*—and really figure out if there's enough *raison* to keep the *d'etre* going.

Product managers, it's never too late.

If you have products with a business case covered by a spider web, it's time to create a new one. You may have some tiny little fear that a business case will end up putting your product out of business and your job at risk.

Truly, this is a remote possibility; and, in fact, the best way to make sure it doesn't happen is to ensure that the product(s) you manage have a strong business case behind them.

As the saying goes, the unexamined life is not worth living; and, in the end, the unexamined product is not worth managing.

RULE #14

Look for opportunities to deliver the remarkable.

I confess: When I first saw Pragmatic Marketing's word remarkable, my initial thought was, "Is this one of those annoying words like *passionate* and *personal brand* that pop up from time to time to test my gag reflex?"

But that first thought was fleeting.

As product marketers and product managers, we should want to deliver the remarkable in whatever we do. Think about it for a minute.

If you settle for "good enough" in your product and don't include at least a few "nice to have" goodies, your customers will greet the new release with "It's about time!" And your prospects will greet the product with "Big deal—now you have what everyone else does."

Is this the type of response you want?

No, you want your customers and prospects to have some sense of delight—something they hadn't thought of…something that's a bit out of the ordinary…something they'll find really useful, or at least interesting.

It could be something as simple as a last-minute time- or trouble-saving feature. Maybe it's a smooth integration with an application everyone in your target industry's using. Maybe it's something all-new, first-ever, state-of-the-art—that everyone will soon clamor to own. Your remarkable "thing" could be a couple of hours of installation support thrown in—not because installation is such a bear, but because every environment's different and anything can happen. Remarkable can be extending the number of seats the license will support.

You can be remarkable in your sales process by really and truly listening to what your prospects and customers are saying, and responding to them. You can be remarkable in your customer service process with a check-in phone call to follow up on whether or not last week's problem has been resolved. Don't forget the finance side of things, either. A lot of customers would find it quite remarkable if you contacted them to let them know you've discovered an overcharge, or that more attractive financing is available.

It's a tough world out there. In order to get noticed—and to win business—you need to do something to stand out. And it really doesn't have to be all that remarkable—just something simple for which your customers and prospects will love you.

RULE #15

With positioning, the focus is on what we do for the buyers.

We love our products.

We're proud of who we are and how we got here.

Yes, yes, yes…we know what went into developing them.

We want everyone to know about all the cool features.

But before we get too carried away, let's focus on messaging that's relevant to the people who are actually going to *buy* the product.

This rule is really resonating with me these days. I'm working with a new client, and there's a part of their history of which they are rightfully quite proud. In fact, they're so proud of it, that they pretty much lead off with it. Which would be fine and dandy—except that this little piece of information (which looms so mightily for "us") is stunningly irrelevant to the customers they're trying to attract.

At best, it's of passing interest—like finding out that the woman in the next office was an Olympic pairs skater, or that the sales guy you did booth duty with at the tradeshow is related to the almost-famous actor with the same last name.

So, when you're positioning your product, lead with what's important to the person who might be writing the check, not with what's near and dear to *you.*

I am not, by the way, advocating for positioning that excludes what the product actually does. I'm a strong believer that good positioning includes not just what a product does for the buyer, but what it does, period. I absolutely hate reading about how a product saves time and money, increasing your bottom line—and coming away without knowing whether we're talking about accounting software or a Ginsu knife.

So save the off-message information for footnotes, conversation, or company background.

Yes, it's interesting that your founder won the Pulitzer Prize. That your product was originally built to count hula hoops. That corporate headquarters is located in the old mill where Civil War muskets were manufactured. *Nice to know*...just *not need to know.*

Obviously, no one is going to make the positioning mistake of telling the audience what's in it for the company selling the product ("We need this product to be a success so that we can stay in business!"). But it's pretty easy to slip into talking about what's of most interest to us, rather than to focus on what the customer really wants to learn.

Sure, there are two sides to every transaction, and the buyer knows that there's something in it for us. But let's face it; all buyers really want to know what's in it for them. TPM

Maureen Rogers is a senior consultant with Communigration, specializing in strategic product marketing (market identification, product positioning, and product messaging) for B2B technology and services companies. A resident of Boston, Maureen is a graduate of MIT's Sloan School of Management and has more than 25 years experience as a product manager and product marketer. With her friend and colleague John Whiteside, she blogs on marketing at Opinionated Marketers (http://opinionatedmarketers.com) and, on her own, she writes about business, the workplace, and culture at Pink Slip (http://pinkslipblog.blogspot.com). Maureen can be reached at mrogers@communigration.com

Part IV of Maureen's article will appear in the next issue of *The Pragmatic Marketer.*

Are your product management and marketing teams overloaded with tactical activities, spending too much time supporting Development and Sales rather than focusing on the strategic issues of the organization?

The Pragmatic Marketing Framework

STRATEGIC

		Business Case	Positioning	Marketing Plan		
Distinctive Competence	Market Sizing	Pricing	Sales Process	Customer Acquisition		
Market Research	Product Performance	Buy, Build or Partner	Market Requirements	Customer Retention		
Market Problems	Operational Metrics	Product Portfolio	Product Roadmap	Launch Plan		
Market Analysis	**Quantitative Analysis**	**Product Strategy**	**Product Planning**	**Program Strategy**	**Sales Readiness**	**Channel Support**
Technology Assessment	Win/Loss Analysis	Innovation	User Personas	Buyer Personas	Channel Training	Presentations & Demos
Competitive Analysis			Use Scenarios	Success Stories	Collateral & Sales Tools	"Special" Calls
			Release Milestones	Thought Leaders	White Papers	Event Support
				Lead Generation	Competitive Write-Up	Answer Desk

TACTICAL

The Pragmatic Marketing Framework is the standard for product managers and marketers at thousands of companies. Since 1993, more than 50,000 people have been trained using this market-driven approach to creating and launching technology products.

learn industry best practices

Product Management training

Practical Product Management defines the strategic role of product management using the Pragmatic Marketing Framework (left). From how to identify market problems to delivering a successful product plan.

Requirements That Work shows you a repeatable method for writing clear requirements your team will read and use. It discusses techniques for prioritizing and organizing market requirements and clarifies the roles for team members.

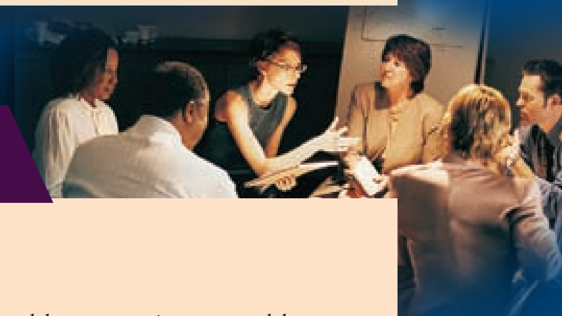
Pragmatic Roadmapping teaches techniques for developing, consolidating and communicating product plans, strategy and vision to multiple audiences—both inside and outside the company.

Product Marketing training

Effective Product Marketing teaches how to create successful go-to-market strategies using a structured, repeatable framework that supports an organization's goals for growth in revenue, market awareness and customer retention.

New Rules of Marketing shows how to harness the power of online marketing using blogs, viral marketing, podcasts, video, search engine marketing and thought-leadership to reach buyers directly.

In addition to the extensive published schedule, training can be conducted onsite at your office allowing a more focused discussion for your specific goals.



achieve market-driven success

With guidance from Pragmatic Marketing experts:

Align your organization with the market. Identify gaps between your current state and best practice to enable your strategy and tactics to focus on market-driven success.

Accelerate your product plan. Uncover the market problems your product can solve in its next release.

Optimize your go-to-market programs. Understand recent wins & losses, and learn how evaluators review your offering to create compelling marketing messages in the language of your buyers.

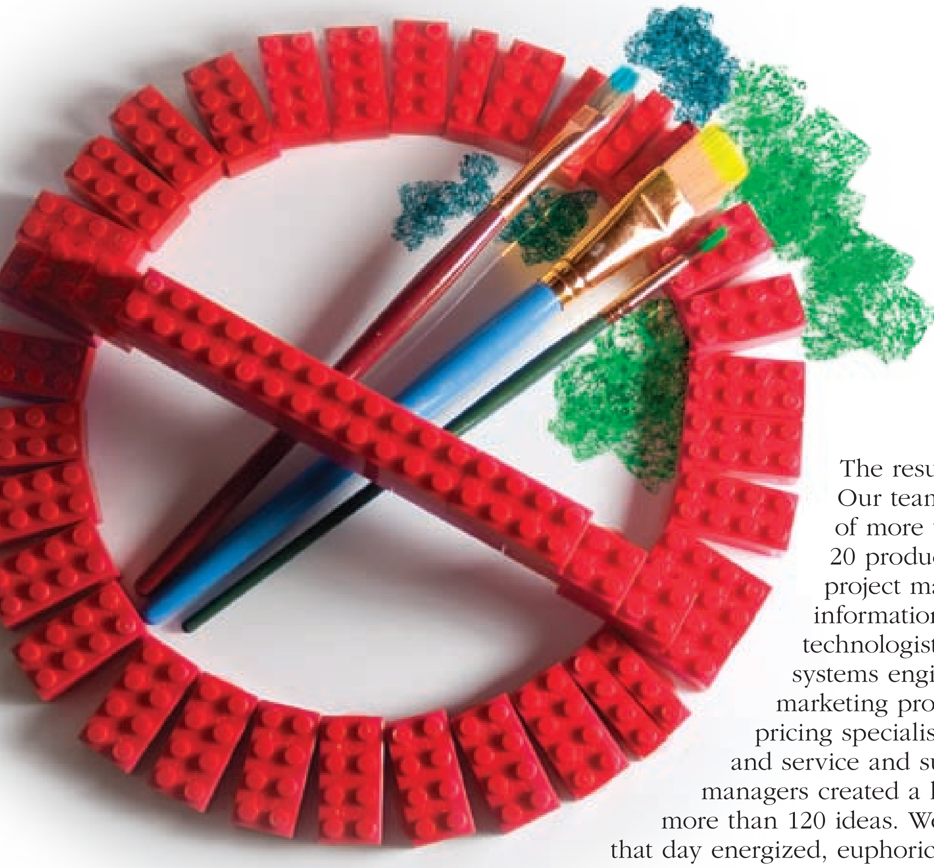
participate in a thought-leading community

For more than 50,000 visitors per month, *PragmaticMarketing.com* is a dynamic, growing resource center with hundreds of articles, tips and techniques, expert blogs, a job board, book reviews, informative webinars, links to peer networking groups and much more.

When Creative Is the Wrong Tool!

The Ideative Process:

By Robert S. Siegel



The exercise was simple and, best of all, fun. The facilitator asked us to ignore the barriers and think creatively, freely, outside the box; pretend for a little while that there were no problems with order-entry systems, billing systems, or state and federal regulators. We were free to brainstorm. Our goal was to generate as many ideas as possible. No idea was a bad idea.

The result? Our team of more than 20 product and project managers, information technologists, systems engineers, marketing pros, pricing specialists, and service and support managers created a list of more than 120 ideas. We left that day energized, euphoric, and full of the future.

The revenue ultimately produced from the ideas generated that day? $0. Products launched? 0. The cost for the brainstorming session and all the follow-up work to evaluate the ideas must have been staggering. More than 20 expensive people spent the entire day in a fancy meeting room with facilitators and catered meals. When you throw in the research and development time and money spent over the next few months on the 30-40 ideas that weren't immediately tossed out afterward as "too silly," you can only conclude that we threw a lot of money and time into a sort of touchy-feely black hole.

The brainstorming methodology we used that day would have been fine had we needed a "creative" session. The problem we faced, however, was not one that could be solved by freeing our minds and souls from reality. The problems were real, and we needed ideas founded within the constraints of a real technology business in a competitive world of limited resources and unlimited demands.

Too bad we spent the day trying to be creative. We should have been learning to be "ideative" instead; a skill that would have given each of us the lifelong ability to generate innovative, realistic ideas by using our constraints, not ignoring them.

Ideative is often better than creative

When I ask a person if he or she is "creative," the common response from product and marketing managers, engineers, financial managers, and just about everyone else in a business discipline is "No!" And that negative answer is often quite forceful. Yet when I describe ideative—the ability to *proactively* and *regularly* produce unique and valuable ideas for new products, services, and solutions—I often get a positive, confident "Yes!" response.

a Better Tool for Our Constrained World

In fact, most of the feedback from my publications and talks about the ideative approach has been from people telling me that by simply making them aware of their ideative abilities and showing them the tools to expand those abilities, they have become far more ideative. I sometimes wish it were more complex than that!

Throughout the business world, just about every one of us is looking for viable ideas to build into new products, services, and solutions. Creative, the standard term for ability in these areas, has a connotation that is often associated with painters, poets, and writers—not the typical manager worried about ROI, pricing, launch plans, and sales objectives. In fact, the word "creative" is often associated with the kind of people that have no ability to face real business challenges.

You may not be creative but you *are* already ideative...

While creativity is a skill few people are born with, ideative skills can be used by anyone willing to grow their knowledge and experience by exploring and having fun.

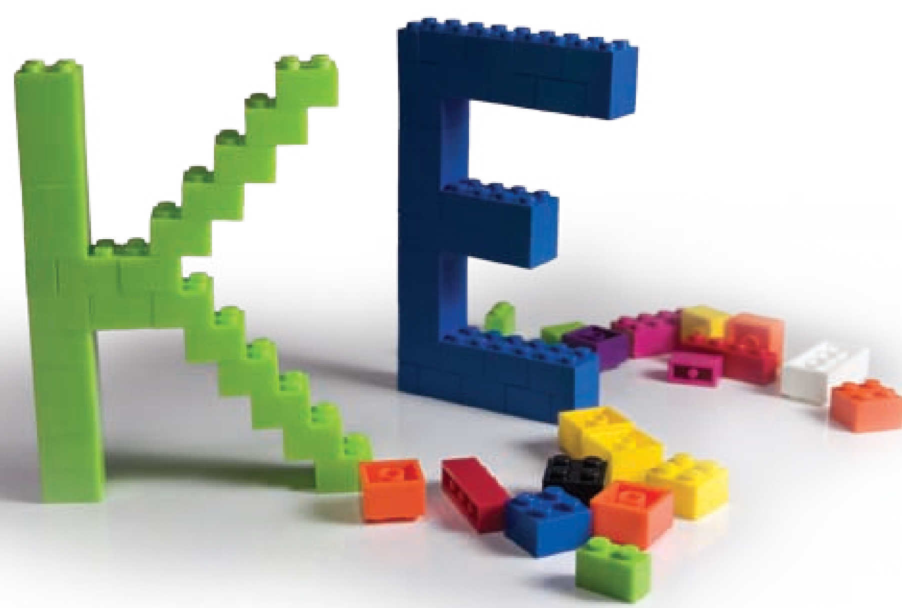
The ideative process begins with a deliberate effort to increase your Knowledge (K) and Experience (E) of the subject for which you want to develop ideas.

Remember LEGOS? Try this simple thought experiment. Think about the variety of constructions you can build from just 25 LEGO blocks. The options are incredible. Now imagine what you can do with a set of more than 5,000 blocks of varying colors, sizes, and shapes. What if you add other brands of building toys: ROBOTIX or Erector, for example? The connectors won't match, but that's okay; variety is better. Now stretch yourself beyond building toys to include completely unrelated items. Add Hot Wheels cars, a piece of fruit, a stapler, and a toy space suit. Now consider all the things you can do by combining these items. You can develop an endless variety of stuff if you are willing to collect and combine anything and everything.

Ideative people collect their life's learning, travels, education, business, family, and social experiences. They combine these "building blocks" in unique configurations, just as you did in the preceding experiment. Your objective—to become ideative for life—means that you will stretch yourself, explore, and have fun as you work intensely to add new blocks of K and E.

By now, you probably realize that you already have the foundation to be ideative with just the building blocks that are already part of your life. Think about all of your experiences and your education—not just college but all the way back to elementary school and before. Every block stored in your brain can be utilized in idea assembly. Add in all the things you've done, from the mundane to the dramatic, and you will find that you already possess a rich store of ideative building blocks.

The ideative process begins with a deliberate effort to increase your Knowledge (K) and Experience (E) of the subject for which you want to develop ideas.



Now, grow even more ideative

To build on top of your ideative foundation, you need to more intensely live and learn. You could decide to begin by sharpening the definition of some of those blocks you already have. Visit the playground where you played when you were nine, pick up a book on biology and relearn the basics of cell structure that you forgot immediately after high school finals, or spend a couple of hours with your parents and siblings going through photos from way back when.

I actually *like* to help my kids with their homework. I have re-learned history and science, and recalled some of the books I read as a child. (In the interest of full disclosure, I must point out that I will suddenly discover an emergency causing me to rush to the office if either child ever needs help diagramming sentences.)

You will probably find that adding new blocks to your store of K and E is the most fun and exciting part of growing your ideative abilities. You have a business degree…so why not take an art class? You've traveled to Europe…now try Southeast Asia. You're a beer drinker…so take a wine course or a wine tasting tour.

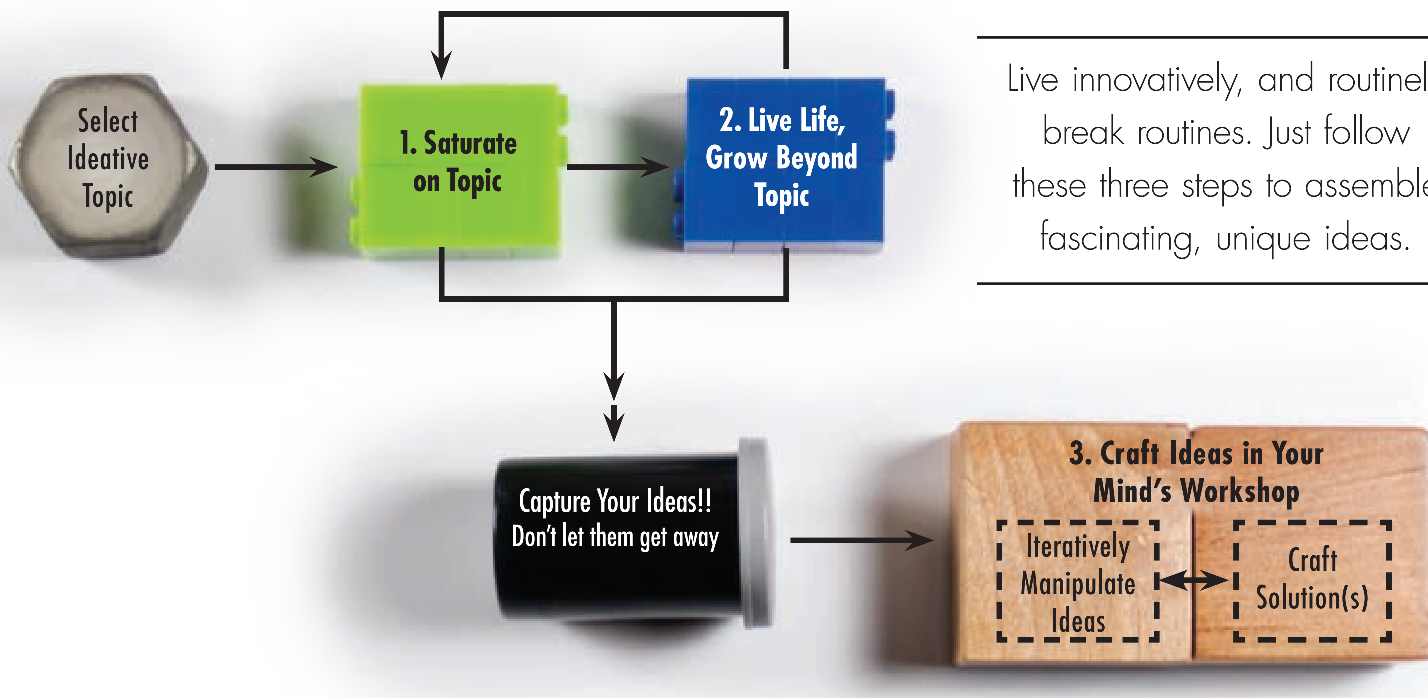
Live innovatively, and routinely break routines. Just follow these three steps to assemble fascinating, unique ideas:

1. **Saturate your brain with K and E in your ideative area.** Then add more K and E. Know *everything* possible about your ideative subject, its history, successes and failures, how your ideative subject works and doesn't work, its future possibilities and risks. Think, eat, and sleep on your subject until it follows you into your dreams.

   Study everything you can find. Talk to the subject matter experts. Ask questions; then ask unusual, even bizarre questions that require explanation. The more people explain the problem from different aspects or viewpoints, the greater the depth of your understanding. Make sure each block of K and E you add is as ***vivid*** as possible.

2. **Live life, learn, and grow beyond your ideative subject.** Applying solutions from one discipline, product, or industry to another seems like a fundamental approach to almost any challenge. It's a shame we don't do it more often.

   Think broadly about the problem you are trying to solve. Grow your knowledge and experience in areas not directly related to your discipline, and beyond.



Live innovatively, and routinely break routines. Just follow these three steps to assemble fascinating, unique ideas.

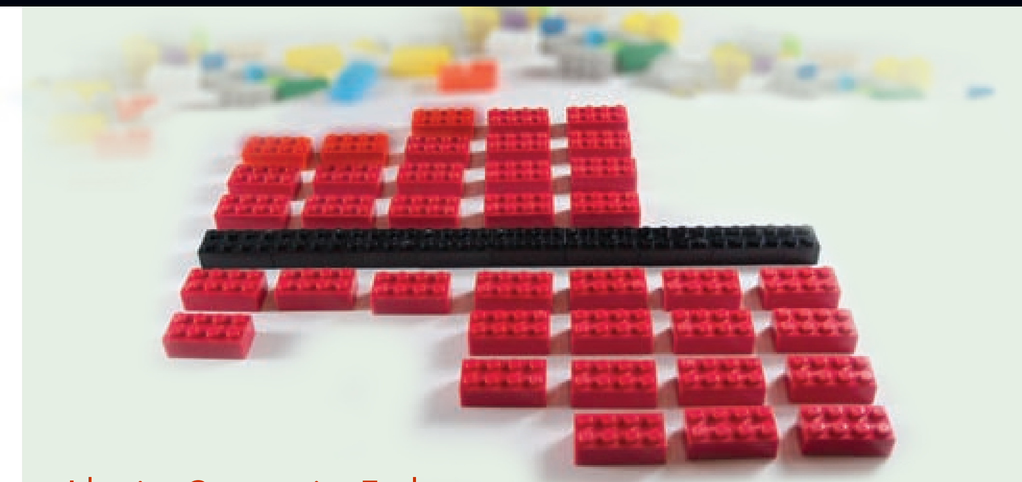
Learn and experience things that are different for you. By routinely breaking routines, you'll learn to take "blocks" from one field or discipline and use them in other fields to develop ideas. These *universal* blocks will stimulate your ideative constructions the way unique blocks enable a child to build distinctive structures with building blocks.

You also need to go beyond subjects related to work. You have a life outside work. There is no reason you can't apply those blocks of K and E to your work. The more information stored in your brain, and the more vivid that information, the more neurons impacted. That means that even seemingly unrelated blocks of K and E can be assembled in ways that connect and create value. The unrelated information stimulates your neurons; and, when your neurons fire, they trigger chain reactions. It's been proven that a dynamic mind will grow more dynamic as you challenge yourself.

3. **Craft ideas in your mind's idea workshop.** Your brain can be thought of as an idea workshop where you build ideas the way children build with building blocks.

   Begin with a list of your constraints, like the inventory of materials for a construction project. Nothing helps to break a problem down into individual building blocks more than staring at all of them at once. From there, you can break the constraints down into individual blocks and build with and around them. Combine related and unrelated constraints in different ways. Keep anything that looks like an idea.

The corollary to each of these three steps is: Find time to relax and allow your K and E to ferment. Don't forget to let your mind wander. Some of your best ideas will appear to you during down time, a car ride, a shower, or while relaxing to music. Saturate your brain and the ideas will burst out. You'll find the process is like a star that has sucked in all the surrounding matter causing a massive explosion—in other words, an ideative super nova.



Ideative Construction Tools

1. **The Pragmatic Marketing Framework** is an excellent example of a tool for pulling your K and E blocks into a bill-of-materials to create your blocks for idea assembly.

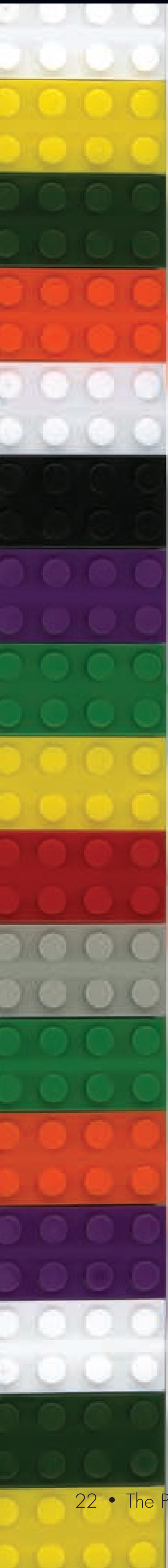
   Imagine you are a product manager for an accounting software product, and are facing a scenario where the IRS issues an assessment on fuel use as part of the new President's energy independence program. The assessment comes just weeks before your next release. Your product has to handle the new IRS assessment, you cannot miss the release date due to Wall Street expectations, nor can you expect to make your product comply in the short timeframe.

   Use the Framework to focus your mind on the specific work functions cited within each box. (Forget about that silly cliché "think outside the box"—there are too many opportunities inside the box!)

   Next, integrate the boxes and seek solutions. For example, begin with the Distinctive Competence block: Say your accounting software's Distinctive Competence is the capability to analyze components of cost across international divisions and currencies. Next, look at Positioning: Maybe you highlight flexibility. Then you analyze your Sales Process and find that the sales cycle and adoption timeframe is longer than a month. Your Distinctive Competence of cost analysis allows your product's users to meet the IRS requirements through a manual work-around for a short time. You find that you can get the update out a month after the scheduled time, as long as you inform your customers about the manual work-around. Problem solved.

2. **I work extensively with a model called the Customer Learning Curve.** The Customer Learning Curve teaches you to manage your marketing according to your customer's state of mind relative to your product. This tool guides you toward solutions based on your customer's Awareness of your product, their ability to Access the product, whether they Learn to Use the product, and other steps. By isolating marketing problems according to the customer's state of mind, you develop better problem definition, enabling tighter focus on solution development.

3. **Tools like mind maps, pyramid diagrams, branch diagrams, and two-by-two boxes** are also great tools to help you set your blocks up like a list of materials for ideative assembly.



Focus on vivid K and E: ideative's most potent variable

To take full advantage of the ideative process, you need to more vividly live and learn. Vivid K and E—the most potent component in the ideative concept—is about using your five senses and your emotions with as great a depth and breadth as possible.

The more vivid your K & E, the more connections your brain creates, which brings more areas of your brain into play in the form of larger neural circuits. Thanks to phenomenal advances in neuroscience, we know that storage and retrieval of memories occurs in multiple areas of your brain. The information gathered through our sight, sound, smell, touch, and taste is stored in different locations depending on the sense, the type of sense, and also the emotions that are attached to that information.

The vivid aspect of the ideative process tells us that idea creation can be vastly improved if we get out into the field with our products and services and meet with customers and our frontline personnel. Working with our products, literally touching them—and hearing and seeing customers use them—draws on our senses and emotions in ways that simply cannot be done from our desks and conference rooms.

In my experience, many product and marketing managers are weak at vivid K and E because they lack the time, resources, and financial justification to conduct vivid-boosting activities. The reports, presentations, and business cases we use for K, and the work that develops E, provide what we need to perform well at our jobs. Besides, what can you do at work to increase the depth of the emotional and sensory components of your K and E?

Answer: A lot.

First, I can't say enough about the need to enjoy the ideative process and the development of ideas. The most fundamental component of ideative skill is to immerse yourself into your ideative subject; and, to do that thoroughly, you have to enjoy what you're doing. So even if you're stuck reading a report, find vivid ways to read that report. Listen to music while you read, find a buddy and discuss the report as you go along, or draw charts and work through the data.

Whenever possible, get closer to the data by getting out in the field to work with customers, your sales reps, and your support team. Expose yourself to your customers' problems and opportunities. Be the one to meet your customer face-to-face to say "No" to something you wish you could offer. Or, you try to fix a couple of little problems that irritate customers, but are too small to be prioritized and fixed. That's emotional. Don't forget to enjoy the success when you exceed customer expectations and the customer expresses delight.

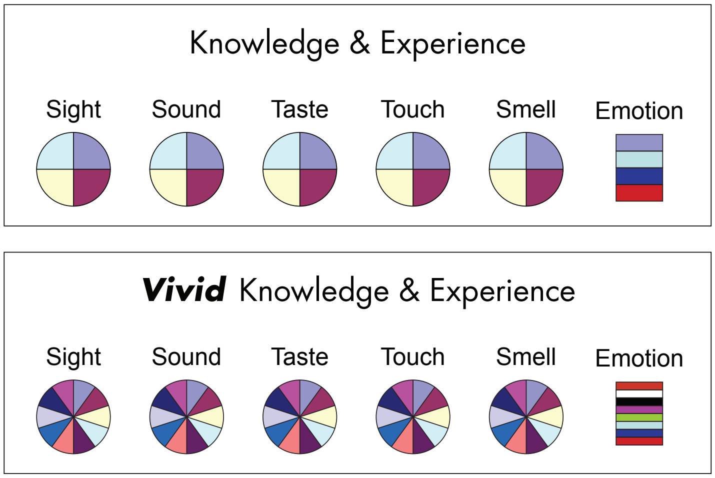
But how will an ideative approach help with barriers and constraints?

Barriers and constraints can help you develop better products and services. This statement may be tough to accept, because we normally think of barriers and constraints in terms of their ability to disrupt, even to destroy, product development work—or at least to make our lives very tough.

I always like to point out to product managers that if our jobs were easy, the companies we work for wouldn't need us. Because of that simple fact, barriers and constraints are our friends.

Barriers and constraints challenge your ability to succeed. If you succeed despite the constraints, you and your product will be stronger—much like an athlete improves his or her game by competing against tougher and tougher opponents. For example, if you are forced to cut your product development budget due to budget constraints, you will look for more efficient methods to achieve your objectives. The increased efficiencies you develop may not be equal to the results you would have obtained if you were fully funded; but, because you were forced into more efficient spending, you are now in position to obtain more per dollar.

Use constraints to isolate and define the problem—and to filter out distractions. Then break the constraint down into individual building blocks and build with them. Think of constraints as a set of blocks with strange, even defective connectors. They're tough to play with unless you think like a kid and improvise. By better understanding the constraint, you better understand the possibilities. Respect the constraint, knowing you ***will*** develop a solution.



Vivid Knowledge and Experiences create more blocks for use in Idea assembly

Ten Ways to Routinely Break Your Routine—in Vivid Fashion

1. **Hold a conversation with a new person every day.** Expand your world beyond people who are similar to you. Talk with people from other countries, other cultures, or other job functions. You'll learn about ways of life and outlooks on life that are incredibly different from your own.

2. **Avoid wasting time; you have far too little.** Don't watch television. Yeah, I know, you mostly watch the history and science channels. People tell me that all the time. Turn it off and go do something else. Anything else.

3. **Waste time.** Relaxation frees the subconscious to connect the blocks of your knowledge and experiences. When you free your mind, your subconscious has more power to bring in random thoughts or connect items that are not necessarily related to each other. Just don't waste your time watching TV.

4. **Use your lunch—not just to eat with friends or to run errands.** Go to museums, new restaurants, new parks, try new foods. So many people waste lunch time (this writer could certainly do better) working at their desks or going to the same restaurant with the same people and eating the same food. New friends, foods, and activities are vivid.

5. **Read books from the Dummies series on subjects for which you have no current use.** Even better, read children's books; they're faster. There are millions of subjects which you can experience with just a few minutes each day.

6. **Play with LEGOS and Tinkertoys and Lincoln Logs.** The building challenges, the quick creation of *something* is both a puzzle-solving exercise and an expansion of visualization skills. In addition, anything that triggers childhood memories is good.

7. **Create a piece of art and enter it into an art exhibit.** My guess, call it an educated guess, is that most of my readers cannot even take this suggestion seriously. But listen: Product and marketing managers who have survived more than two years in their jobs, share a combination of tenacity and courage; without those traits you wouldn't have survived. So how about taking some of that tenacity and courage and give art a try? Carry a camera with you and capture some interesting scenes. Try drawing and see what you get.

8. **Try writing a short story.** You don't have to be Hemingway. Trouble coming up with an idea? Write the story about a character doing what you do, at work, home, having fun, whatever. Two thousand words are all you need.

9. **Expose yourself to a wide variety of music.** Thanks to the Internet you can now listen to anything imaginable and more. Search for Native American songs or folk Indian music. If you normally listen to american pop, try some jazz or classical.

10. **Change your schedule: If you normally arrive at work at 8 a.m. try 9 a.m. and 7 a.m.** You'll see your world differently, you'll sense different emotions in the people you meet, and you'll even hear different sounds. Try getting up with the sun and going outside to listen to the birds and feel the early morning breeze. It's wonderful.

A final challenge

When you finish this article, don't move on to something else right away. Stop. Experience what you have just read—in a vivid way. Notice the type, the ink, the texture of the paper. Notice the shapes of the letters, their serifs, colors, and the background. Think about the colors of the page. Think about how you would encourage someone who has not read this article to expand his or her ideative skills. To whom would you send this article, and what do you hope he or she would gain? How can you encourage the people around you to become more ideative?

Remember, the ideative process is a powerful tool for creating new products, services, opportunities, and solutions. You already have ideative abilities—so now go out and put them to work for you.

TPM

Robert S. Siegel is a senior product manager at EarthLink and founding partner of Glacial Artifacts. He spent ten years as a senior product manager at BellSouth, now AT&T. He has lectured on Product Management, and is working on his book, Ideative; Purple Hair People with Nose Rings Need Not Apply, *and a book with two partners,* The Marketing Epiphany. *Siegel writes on business, political satire, and fiction. You can contact Robert at robertsiegel@earthlink.net*

The Economics of

Software as a Service (SaaS)

VS.

Software as a Product

By Scott Sehlhorst

There are numerous ways of selling software these days. Software as a Service (SaaS) has been in the consumer market for a while, and is now making significant inroads into the enterprise software space. If you're considering purchasing or using software, you should understand what SaaS means and how it differs from software products of the past.

This article is not about the challenges of product management for a SaaS *product*, nor is it about multi-tenant architectures and other SaaS implementation details. This article looks simply to compare—*from the customer's point of view*—software purchased as a service versus software purchased as a product. ➔

Software as a *Service*?

Software as a *Service* is an interesting concept. It implies that, instead of purchasing the software, you are purchasing it as a service—which really means the right to use the software.

You are also (usually) purchasing a hosting and infrastructure service along with the rights to use the software. SaaS providers maintain the hardware, perform upgrades, backup your data (sometimes), and otherwise perform all of the "keep the lights on" services and activities required to keep the software running.

Imagine a typical, 1990s style software purchase:

- You buy a source code control system.
- You set up a server and install the software.
- You pay ongoing support costs: providing power to the server, keeping the server cool, applying security and operating system updates to the server.
- You pay costs associated with administering the hardware and labor costs to update and upgrade the software.
- You carry risks—a botched upgrade or a hardware failure—which can cause downtime or lost data.
- You bear the costs of designing and maintaining a secure system. Do you allow your people to access the software (on the server) from other computers on your network? Do you allow them to access the software when they are not on the network (travelling, working from home, etc.)? How do you prevent your competitors from stealing or, even worse, destroying your data?

Now imagine that you're outsourcing all of the "keep the lights on" activities above:

- You pay an IT services firm to manage the hardware and the software for you, including the security model.
- And you just use the software.

That's one of the benefits of purchasing SaaS. To really grasp the economics of SaaS you have to contrast it with the economics of software license purchases.

Widespread misunderstanding

There is a widespread misunderstanding about *purchasing* software. In the last section, we used the word "purchase," but that isn't completely correct. You don't purchase a copy of the software; you purchase a restricted *license* to use the software.

You probably have heard the phrase "site license," which means that you are purchasing the right for everyone in your building (or company) to use the software.

Sometimes software is sold in terms of "numbers of seats"—the number of people that are licensed to use the software at any one time. You might have 100 engineers who share ten seats (single-seat licenses) of analysis software. Since each engineer only spends about 5% of his or her time using the software, they can easily share licenses. At any given time, five engineers (on average) will need to use the software. With a license for ten simultaneous users, each engineer is likely to be able to use the software whenever he or she desires.

So, even when you think you are *purchasing* software, you aren't. As with SaaS, you are purchasing the *right to use the software*.

Economics of software licensing

There are infinite creative ways to purchase a software license. The most common situation is that you purchase a license, and then later purchase upgrades.

An obvious example is Microsoft Office (productivity software). Microsoft releases a new version of Office every couple of years. If you own the previous version, you can purchase an upgrade for less than the cost of buying the software for the first time. You are not *required* to purchase an upgrade, of course, but you may *want* to in order to capitalize on the latest features and fixes—and to stay current. If the people with whom you work all upgrade, you may want to upgrade, too—so that you can use the documents they create.

Microsoft does a good job of providing free utilities to read documents from the newer versions, and allowing people with newer versions to create documents that can be used by people with older versions. Microsoft, therefore, gives you a choice. They rely on market forces to create the pressure to upgrade, but you never *have to* upgrade.

On the other hand, Intuit, makers of Quickbooks (small business accounting software), is a little pushier. Intuit releases a new version of the software every year. Once a new version of Quickbooks is released, support for some or all of the integrated online services is dropped for older versions of the product. You can continue to use your old version, unless you want to use one of the integrated services.

When companies sell software (licenses), they usually sell a version of the software, and then make updates to that software with some frequency—anywhere from daily to annually. Companies also manage those updates as two distinct types of updates:

- **Minor updates** are usually free and often include bug fixes or features that were intended to be in the major release, but were delayed. Or they might just be the introduction of capabilities with "small" value to their customers. A lot of software will automatically notify you, download the update, and install it for you. That's great service.
- **Major updates** usually require the purchase of an upgrade. Major updates are usually more significant; they introduce capabilities that have "large" value to their customers or are intended to make the product appealing to additional markets.

To understand the economics of software license purchases, you have to look *at both* the value over time and the costs over time of purchasing a software license. ➔

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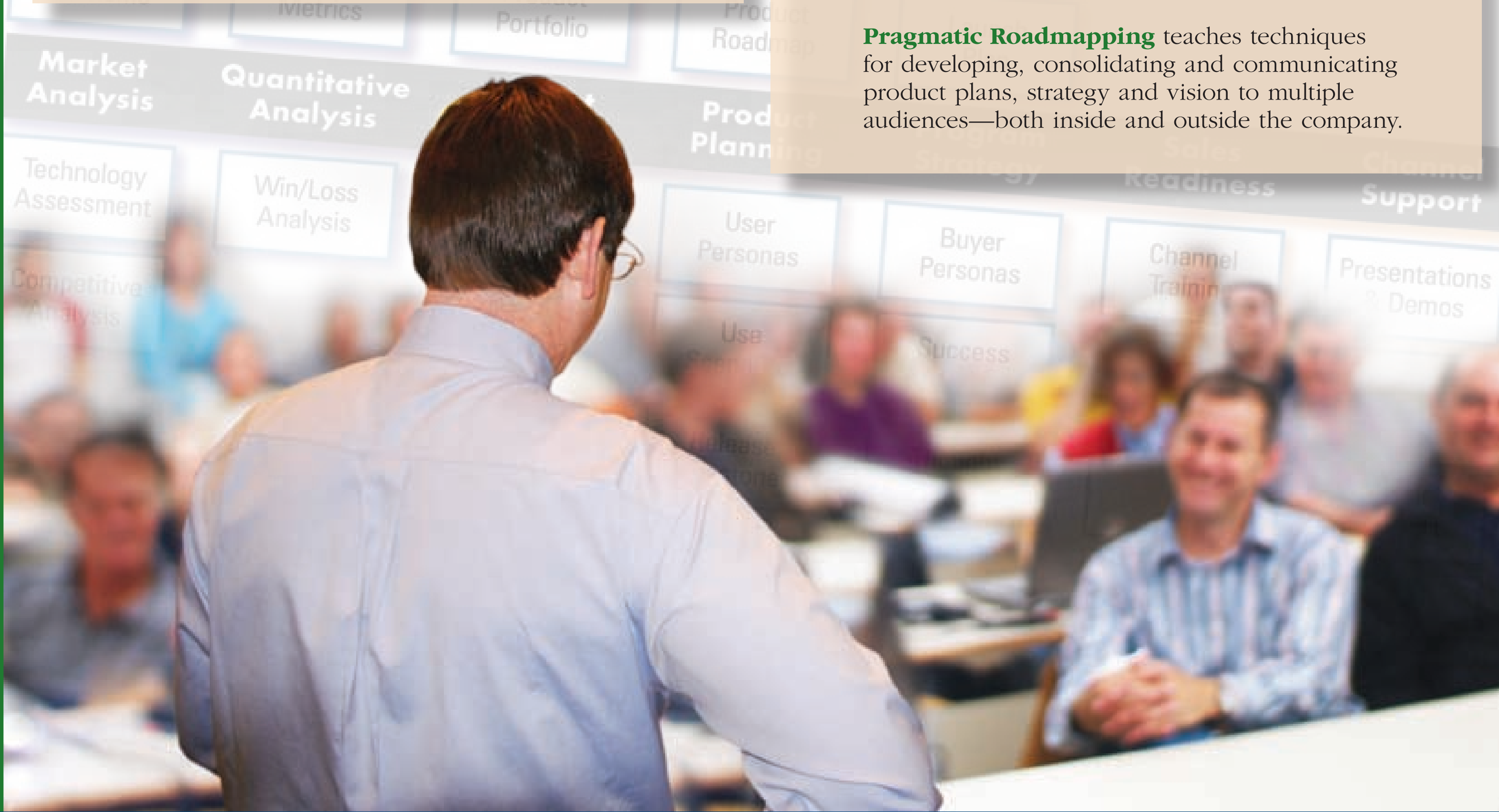

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Figure 1. Software Value Model

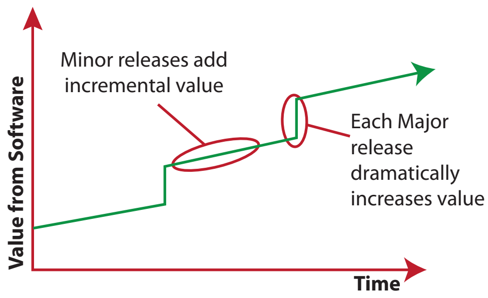


Figure 2. Customer perspective of value over time

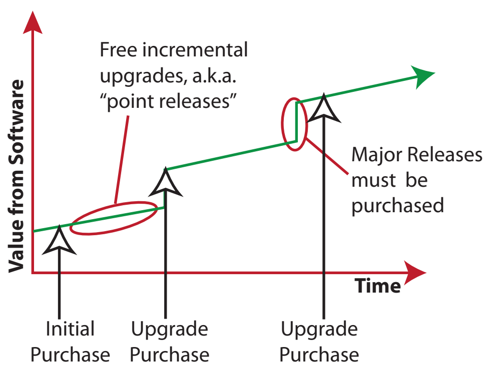


Figure 3. Incremental value to the customer

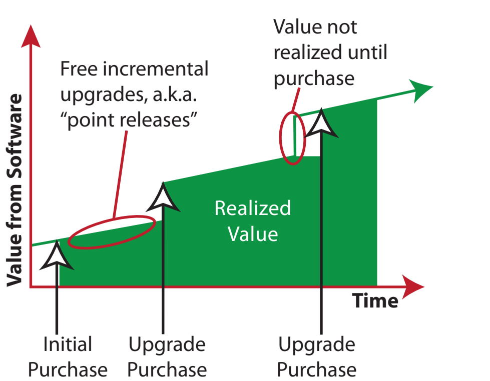
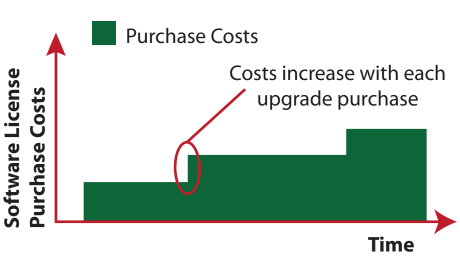


Figure 4. License costs over time



To keep this simple, we'll assume the model described previously—minor updates happen frequently and are free, and major updates require the purchase of an upgrade to the latest version of the software. We'll also assume that every new update introduces something valuable to the customer.

Figure 1 demonstrates the value model for software over time from the software company's perspective.

The axes represent increasing value (up) versus the passage of time (to the right). Time starts when you purchase a license to use the software. You're immediately getting value. As minor updates are released to customers, the value gets marginally higher. Whenever a major release is made, the value curve jumps up dramatically. This represents the introduction of new, valuable capabilities.

As each new customer purchases a license to the latest version of the software, the company gets more revenue. As each existing customer purchases upgrades to their existing software, the company gets more revenue. Clearly, a company makes money both from finding new customers and from keeping existing customers.

Companies typically make more (per purchase) from finding new customers than from getting existing customers to upgrade. Until a product builds a large base of existing customers, the company's financial focus will be on finding new customers. Satisfying existing customers is at risk of becoming a secondary priority, purely based on economics. Yes, this is an incomplete picture; there are other factors, but it is absolutely an influence.

Software license benefits

This article starts with a promise to look at SaaS economics from a customer's perspective. If the model in Figure 1 represents how a software company views its products, consider **Figure 2**, which reflects how a customer might view the same thing. Remember—in our example, we have a perfect product manager—every update has the same perceived value to customers as it does to the company. **Figure 2** overlays customer purchasing behavior on the value model.

As a customer, you make an initial purchase (the left-most callout), and then get free incremental increases in value from each minor release. You also purchase an upgrade to the latest version of the software as soon as it is available. You then start getting incremental value from the minor updates to *that* version of the software.

The older version does not keep getting updates, so if you don't purchase the upgrade, you don't get the benefits of the latest minor releases. A second major release happens, but you don't purchase it for a short while. Then a minor release is made, with a fix to an annoying bug that really bothers *you*. So you purchase another upgrade.

The value *to you, the customer,* looks like the steps reflected in **Figure 3**.

The green area represents the value you get. It's worth noting that the value is often a function of how much you use the software (enabling the benefit); and, as such, it is a function of time. The more you use it, the more value you get.

In **Figure 3**, you will notice that you do not get the value of the last major release until you actually purchase it. You also do not get the incremental value of minor releases that happen after that release. Once you purchase the upgrade, you immediately get the benefits of all the minor releases as you get "back in the game."

SaaS — a simple definition

Software as a Service is usually provided as follows:

1. A company creates a software product and hosts that product on multiple servers. The company manages the hardware and software—and realizes the cost of that management.

2. Customers *subscribe* to the service—getting the right to use the software for as long as they continue to pay the recurring subscription fees.

3. The company makes both major and minor updates to the software, and the customers *automatically* get those updates as part of their subscription.

There are many examples of SaaS; some obvious ones are Salesforce.com, Kadient's inciteKnowledge, and 37signals' Basecamp.

Software license costs

Your costs over time are also important. **Figure 4** shows that the obvious costs are the checks you write to the software company to pay for the software and for the major upgrades. But this chart can also be a little misleading—as we are depicting "one time costs" that add up over time. Showing this as a stair-step area instead of a series of spikes will make sense as you keep reading. The key thing to appreciate is that once you make a purchase, your license purchasing costs do not go up again until you make another purchase.

At the start of the article, we identified several "ownership" costs—supporting the software and hardware, for example. It is critical that you keep those costs in mind when evaluating software license purchases. These costs are ongoing costs—so the more you use the software, the more the costs add up.

There are also *training costs*—the cost of lost productivity as people learn to use the software and adapt to changes in the software. **Figure 5** reflects the ongoing infrastructure and training costs as they expand over time.

When you combine these costs, you get a model for the total cost of purchasing a software license over time. The jargon for this is Total Cost of Ownership (TCO), reflected in **Figure 6**.

As you can see, "purchasing" software one time actually has a continuously increasing total cost of ownership. Different types of software will have different relative costs for infrastructure support, training expense, and license fees. But generally, training expenses are much lower than the other costs of ownership.

SaaS economics

SaaS is purchased with the same mechanics as subscribing to a magazine or cable television or satellite radio. You pay a recurring fee for the right to use the software, just as you pay a recurring fee for the right to watch cable television. You might even get a discount for purchasing a longer-term subscription and paying up front. When you want to stop using the service, you stop paying the fee.

The model for creating value with SaaS products is the same as with licensed software (Figure 1). Where things change *slightly* is in the value model from the perspective of the customer as shown in **Figure 7**.

Here, there is a single trigger to the realization of value—starting the subscription. You automatically get the minor and major updates "for free" by continuing to pay the subscription fee. ➔

Figure 5. Ongoing software costs

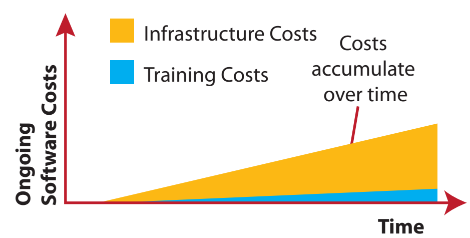


Figure 6. Total Cost of Ownership (TCO)

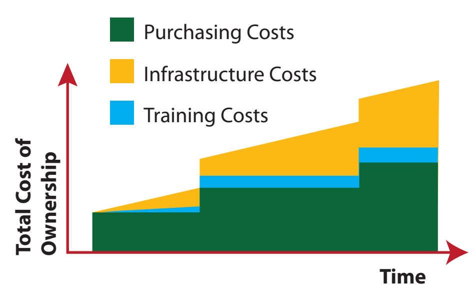


Figure 7. SaaS customer value model

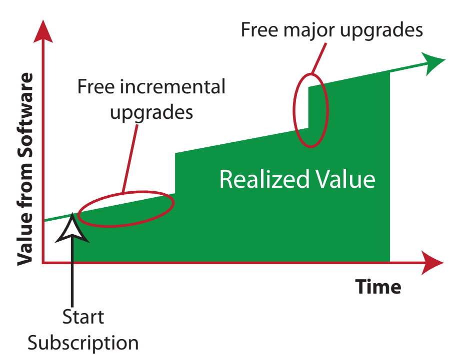


Figure 8. Ongoing SaaS costs

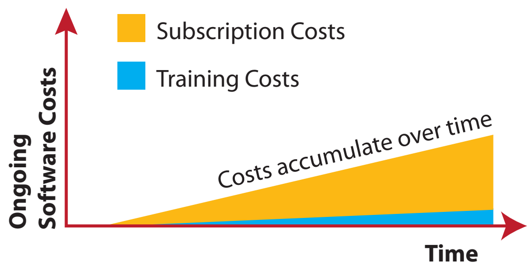
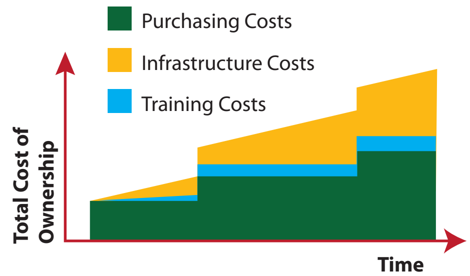


Figure 9. Total Cost of Ownership



SaaS costs are different

Where SaaS differs from the purchase of a license to use software is on the cost side (**Figure 8**).

The training costs associated with using software have nothing to do with the mechanism for payment, so those costs are the same. The cost of subscribing to the service (yellow region) is new, and goes up over time. It is also typically higher than the training costs. Note that there are no "large purchase" spikes in the costs, because you never purchase a license. And there are no infrastructure costs, because the company that provides the service realizes those costs.

The idea is that this approach is more cost effective when it comes to infrastructure costs, so the company can pass on those savings to you.

Comparing the two cost models side by side (**Figures 8** and **9**) is the way to really see the difference.

Both models have costs that increase over time. For many technical reasons, the SaaS architecture is more efficient and has lower costs for the software company, which tends to result in lower costs for the customers. This is not always the end result, but it is directionally correct.

Another interesting factor is the financial pressure on the SaaS provider. Where a software licensing model creates pressure to prioritize finding new customers, a SaaS model creates pressure to keep existing customers.

SaaS providers get the same revenue from a new customer as from an existing customer—as opposed to the "new vs. upgrade" dynamic seen with software licensing models. In most cases, it is cheaper to keep an existing customer than to find a new one.

The net result: financial pressure to retain existing customers. This pressure can drive a different behavior, more like that of a retail sales model, where keeping your existing customers is critical.

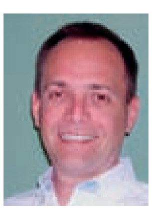
Conclusion

The SaaS model ultimately provides the same type of products as a software licensing model—but with a better economic model, one that is lower in cost to the customer and structurally inclined to keep getting better *for the customer* with every new release.

Personally, I like the idea of purchasing from a company that is financially motivated to keep *me* happy, not one that is pressured to find another customer as soon as I've written my check.

The best companies try to reinvent themselves and improve their products continuously. Over time, the best companies will move to SaaS models, which align their financials with their objectives.

TPM



Scott Sehlhorst has been helping companies achieve Software Product Success for more than a decade. Scott consults as a business architect, business analyst, and product manager. He has also worked as a technical consultant, developer, project manager, and program manager. Scott has managed teams from 5 to 50 persons, and has delivered millions of dollars in value to his customers. Contact Scott at scott@tynerblain.com, or join in on the Tyner Blain blog at http://tynerblain.com/blog

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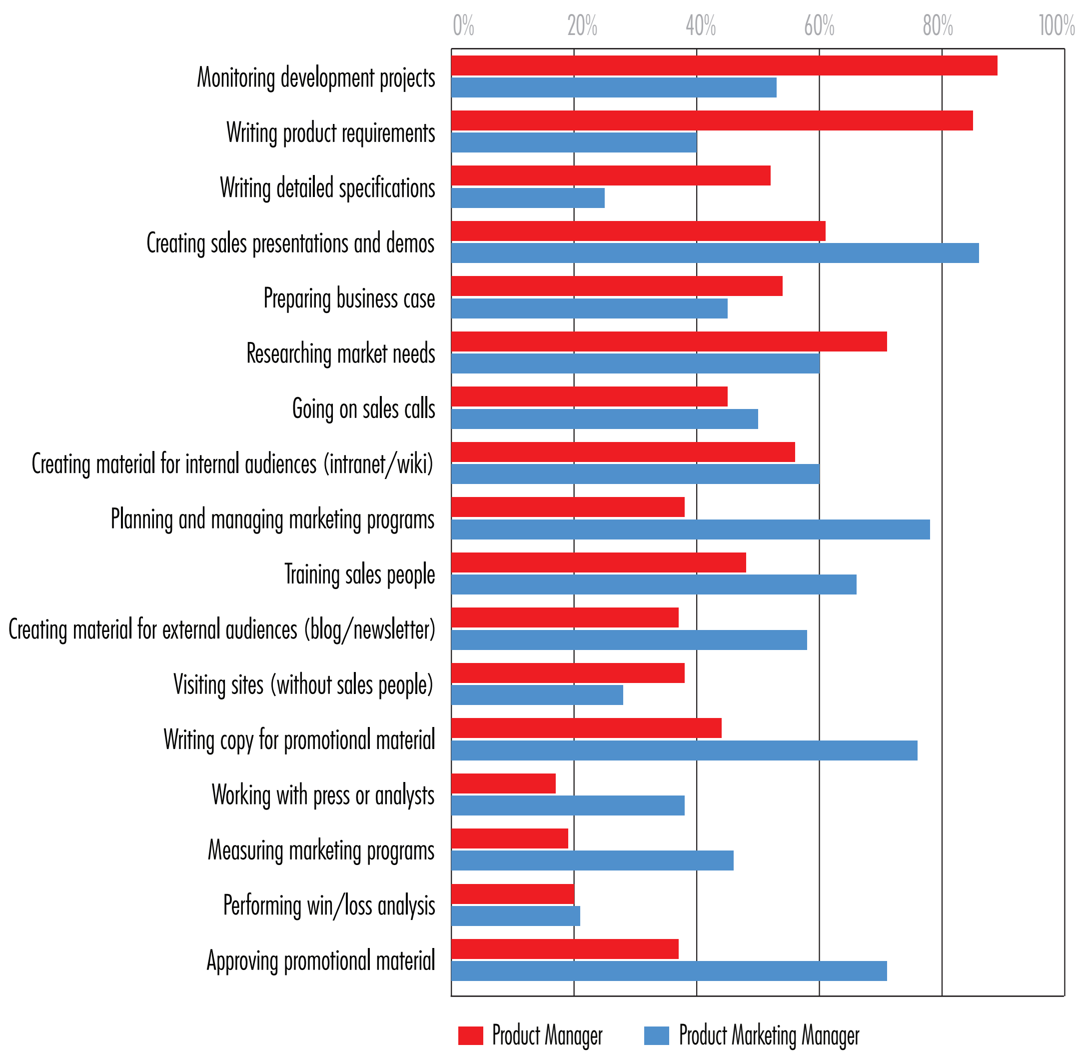

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