Optimizing XaaS

How high-technology companies can optimize their subscription business models to drive revenue and innovation.

Executive Summary
High-technology companies have their eyes set on growth opportunities—the cloud/SaaS marketplace is expanding rapidly with enterprise, SMB and consumer customers using these services at an unprecedented scale. In fact, you are probably reading this right now on a mobile device, enabled by cloud computing services over a wireless network.

XaaS, or “everything as a service,” is an emerging business model that posits that everything from technology services through key business processes can be delivered as a service utility. As technology companies adopt XaaS, they realize the capabilities required to succeed with XaaS are vastly different from the attributes of traditional business models. They face challenges not only in embracing the mechanics of new forms of service delivery but in maintaining the balance between third-party-driven process innovation vs. shifting operational costs that are administered on a pay-per-use basis.

This white paper discusses practices that help technology companies deliver superior software services to their customers by running better (i.e., managing costs) and running different (i.e., enabling innovation).

Inside Xaas: The Subscription Business Model
All companies, especially enterprises, are increasingly wary of allocating huge up-front capital costs to computing—be it business applications, utility software or good old data centers. They are increasingly turning to the cloud and software as a service (SaaS): subscription-based offerings that allow customers to fund IT investments as operational expenditures, with no up-front capital spend. These subscription-based business models are what we see driving the adoption of XaaS.

Technology companies are at various stages of adopting subscription-based business models to deliver their products as cloud or SaaS offerings.

XaaS key characteristics include:
- High scalability.
- Multi-tenancy.
- Online and automated provisioning.
- Try and buy.
- Device independence that (in many cases) enables users to access software regardless of what device they are using.
- Location independence.
- Term-based billing or pay-as-you-go models.
XaaS refers to one or a combination of SaaS, infrastructure as a service (IaaS), platform as a service (PaaS), communications as a service (CaaS) or monitoring as a service (MaaS), as depicted in Figure 1.

Business and revenue models that support and enable XaaS are illustrated in Figure 2.

**XaaS Adoption, Optimization Techniques**

Traditionally, high-technology companies built perpetual-license products, upon which their existing business operating models are based. Moving to a subscription model presents operational complexity challenges to many technology companies. From our experience, the launch of new XaaS businesses outpaces a company’s operational ability to deliver and scale. The reality is that building the new XaaS capabilities required to embrace and succeed in a services-centric environment is hard work – it touches every major business function, from sales and marketing through customer support and product management, etc.

**Sales and Marketing**

- **Adaptation requirements:** XaaS relationships need more care and stickiness than those created by a traditional perpetual offering. That’s because customers have low up-front costs for these services and the barriers to switch to alternative providers are relatively lower. Most companies with a transactional, product-based and channel-centric mindset will need more preparation to deliver the world-class customer experience demanded by XaaS models. XaaS providers must adopt a new approach to selling – that is, a community-oriented way of building relationships.

The good news is that many high-tech companies are moving to a more consultative, business case-driven selling approach. This requires them to move from a “one size fits all” approach to a segmented model to ensure that sales and marketing can scale up and down depending on market conditions. A revised sales compensation model is also required to drive more relationship-oriented selling.

At a traditional software company, for example, incentive compensation for salespeople is tied to immediate payouts when a product is licensed and shipped. This approach changes when companies embrace an annual subscription, where customers are billed monthly on how much software is used. Careful hand-holding is often required to show the sales force what’s in it for them and the company over the longer term.

- **Optimization techniques:** XaaS vendors must adopt go-to-market strategies and sales tactics that are closely aligned with the

**Defining XaaS**

![Figure 1](image-url)
Modeling XaaS

<table>
<thead>
<tr>
<th>#</th>
<th>Revenue Model</th>
<th>Pricing Strategy</th>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Recurring Revenue Model,</td>
<td>Subscriptions per user, per month,</td>
<td>Brand loyalty, since a one-time sale can become a recurring sale. Lower</td>
<td>Fixed fee as per unit (month, users, transactions) which can get underutilized.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>per transaction.</td>
<td>cost than purchasing the product.</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>Metered services (pay-per-use).</td>
<td></td>
<td>Customer has access to potentially unlimited resources but only pays for the</td>
<td>More complexity in implementation and monitoring.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>actual use.</td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>Pay as you go.</td>
<td></td>
<td>More beneficial than subscription as payments are more usage-based.</td>
<td>More complexity in implementation and monitoring.</td>
</tr>
<tr>
<td>4</td>
<td>Try Before You Buy</td>
<td>Tiered pricing depending on period of</td>
<td>Free version for evaluation which will attract more customers for upsell</td>
<td>Conversion of free users to paying customers is a challenge.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>usage.</td>
<td>later.</td>
<td></td>
</tr>
<tr>
<td>5</td>
<td>&quot;Freemium&quot; Model</td>
<td>Free to customers.</td>
<td>Give away service for free in return for customer’s personal details, and</td>
<td>Network of other consumers for the customers’ personal details needs to be built.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>convert them into paying customers later.</td>
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</tr>
</tbody>
</table>

Figure 2

preferences of key influencers and buyers of specific SaaS solutions or cloud services. While most B2B XaaS vendors gravitate toward a transactional sales model characterized by inbound marketing and inside sales, the sales model can also be defined according to the average selling price (AvSP), a statistic that can illuminate the complexity involved in navigating the sales/purchase cycle (see Figure 3).

Quote to Cash and Revenue Recognition

- **Adaptation requirements:** Due to product/service uniqueness and the complex competitive landscape, software companies moving to the XaaS model often struggle with assessing how to price their services. XaaS providers find it difficult to implement new pricing models other than traditional pricing. New pricing models (e.g., subscription-based or usage-based payments) require new capabilities to execute. This often requires companies to take additional time and educate themselves as well their customers on the value of variable pricing.

Revenue recognition for XaaS companies is quite complex, particularly for companies that are accustomed to traditional licensing models. Inability to manage business capabilities from an end-to-end perspective — including pricing, packaging, usage metering and

Making Sense of SaaS

<table>
<thead>
<tr>
<th>Sales Model</th>
<th>Best for</th>
<th>Implications</th>
</tr>
</thead>
<tbody>
<tr>
<td>Customer Self Service</td>
<td>Low AvSP products which have a</td>
<td>• Marketing has near-complete responsibility for revenues.</td>
</tr>
<tr>
<td></td>
<td>fairly noncomplex sales cycle.</td>
<td>• Awareness, outreach and automation to drive the sales/purchase cycle without sales team involvement.</td>
</tr>
<tr>
<td>Inside Sales</td>
<td>Once AvSP rises beyond a threshold.</td>
<td>• Transactional model characterized by high volume sales and support operations, quick sales cycles and rapid onboarding enabled by as much customer self-service automation as possible.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• XaaS vendors need to invest in tools, training, incentives and metrics to drive efficiency and transactions.</td>
</tr>
<tr>
<td>Enterprise Sales</td>
<td>Enterprise XaaS products.</td>
<td>• Targeted acquisition of customers with a consultative, business-case-driven approach.</td>
</tr>
</tbody>
</table>

Figure 3
billing - could result in pricing anomalies, revenue leakage and market share erosion, all of which can be avoided.

XaaS requires a new contracting capability as well, particularly when the same customers are buying both traditional and XaaS offerings. XaaS contracts often have payment terms, billing schedules and renewal clauses that are different than traditional contracts, and contracting groups must be able to execute both types of contracts in a way that focuses on closing deals quickly and maximizing revenue.

- **Optimization techniques:** The balance between pricing a service and at the same time managing product features is critical to keeping the revenue engine purring. Deciding on the optimum price for XaaS services requires balancing factors such as the complexity of developing products, acquire and serve costs, churn and cash flows. Figure 4 depicts this balancing act.

**Customer Support**

- **Adaptation requirements:** In a traditional model, service and support typically focus on the technology involved and “fixing” any shortcomings or issues that prevent the provided technology from operating in the intended fashion. In an XaaS model, however, the focus shifts to business enablement: helping customers leverage the solution to realize business value.

Customer-facing support representatives must be able to converse with customers in ways that help them to realize the promised benefits of the solution provided. Since greater adoption/usage leads to greater revenue, the support function’s ability to focus on ensuring customer adoption/satisfaction is critical. Management must shift from thinking of service and support as a cost center and acknowledge the fact that support, training, professional services, sales support and quality assurance are core capabilities that elevate customer relationships and not separate entities.

- **Optimization techniques:** Companies can provide more effective customer support by:

  - **Adopting a customer-centric, consultative approach** to enable customers to best use the service, liaise with product teams on feature requests and generally serve as internal advocates for customer success. This will help customers to drive user adoption and recognize ROI benefits long after the initial implementation and rollout.

  - **Shortening the duration of the transactions by use of better tools or training,** thereby delivering enhanced support team value.

  - **Establishing user communities via platforms of exchange** that will enable users to help each other. It will result in the reduction of the volume of service requests.

**Cloud/SaaS: Subscription Business Model**

In an XaaS model, however, the focus shifts to business enablement: helping customers leverage the solution to realize business value.

![Figure 4](Image)
for the support team. Among the other advantages:

› Higher user adoption as the community helps customers get the most value from the product/service.

› An available pool of users for real-time validation and testing.

› Great source of feedback that can be leveraged for product/service improvement.

Product Management
Product management is integral to any XaaS offering – more so than it is with on-premise products. XaaS products need to be robust to ensure customer stickiness due to the relatively lower exit barrier.

Given customer bias toward “try and buy” transactions, investing in strong product management will help XaaS providers create products that can effectively convert trial-period customers into paying customers.

Analytics-Guided Innovation
The XaaS product landscape at every layer (see Figure 1, on page 2) is becoming very innovative, and technology companies are continuously looking to add features that will ensure customer acquisition. XaaS providers are beginning to amass enormous quantities of cross-customer and product usage data. Insights from these data sets help to develop and launch new capabilities in existing and adjacent markets. From baselining data definitions and benchmarking, high-technology companies can make data-driven decisions to prioritize product innovations and feature development/execution plans.

As these offerings become more mature and buyers become more sophisticated, data usage analytics represent a smart path to the next profitable frontier. For example, our analysis of the intersection of customer data and product usage telemetry data provides distinct clues on the most widely used/least used XaaS product features by various customer segments. This data can be interpreted by product management teams to prioritize future product innovations.

Solutions and Best Practices
As they transition to an XaaS model, technology companies must review their offerings and focus on customer experience and revenue generation. Figure 5 highlights the key considerations for a company to reshape offerings for delivery as XaaS.

Best Practices
• **Plan first:** Identify key offerings and initial price points and go-to-market strategy. Companies need to provide a number of different subscription plans, targeted toward different market segments and hence containing different services and features.

For example, Microsoft created Office 365 (a subscription-based service that offers access to various services and software built around the Microsoft Office platform) in various subscription plans (see Figure 6, on next page).

Making the XaaS Segue
In the XaaS model, multiple customers may share the same physical products in a multi-tenant model. Product pricing is primarily based on the capabilities of the product. Customers are going to make an up-front investment and amortize the cost over a period of time. With XaaS, the pricing is primarily driven by the units of measure. For example, price might be a cost per seat per month. Over time the model can be successful, but it requires a pricing methodology that also accounts for customer churn/deactivations.

» Build an effective go-to-market strategy. Companies need to properly plan their go-to-market strategy for their XaaS applications and focus on various important aspects.

EMC, a leading cloud service provider (CSP), has formed a go-to-market strategy for adopting XaaS based on the following aspects:

› Strategy: This is an initial engagement to define an effective go-to-market strategy to avoid the pitfalls associated with a "build it and they will come" approach by understanding the full gamut of implications in delivering a PaaS offering.

› Product inception and marketing: Building on results from due diligence and business plan acceptance, organizations must develop a product marketing strategy, including solution specification and design and partner selection, and also budget for piloting and launching the offering.

› Marketing communications plan: Marketing plans are necessary to deliver appropriate and timely internal and external communications regarding the new offering.

› Integration certification: This involves the ability to integrate the offering into the overall billing and customer support systems that the service provider currently deploys.

› Operational readiness: This involves analysis to determine service levels and develop the necessary governance structure around the general availability.

› Sales: The readiness of existing sales force for new XaaS solutions should be assessed, including analy-

### Subscription Plan, Target Customer Segment, Features

<table>
<thead>
<tr>
<th>Subscription Plan</th>
<th>Target Customer Segment</th>
<th>Features</th>
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<tbody>
<tr>
<td>Office 365 Home Premium</td>
<td>Mainstream consumers, families.</td>
<td>• Most Office applications for home/noncommercial use (excluding InfoPath and Lync) on up to five devices.</td>
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<tr>
<td></td>
<td></td>
<td>• 20 GB of additional SkyDrive storage.</td>
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<td></td>
<td>• 60 minutes of Skype international calls per month.</td>
</tr>
<tr>
<td>Office 365 Small Business</td>
<td>Businesses with 1-10 employees and limited IT experience.</td>
<td>• Hosted Exchange, SharePoint and Lync services only.</td>
</tr>
<tr>
<td>Office 365 Small Business Premium</td>
<td>Businesses with 1-10 employees and limited IT experience.</td>
<td>• Office applications on up to five devices per user.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Hosted Exchange, SharePoint and Lync services.</td>
</tr>
<tr>
<td>Office 365 ProPlus</td>
<td>Professional users.</td>
<td>• Office 2013 Professional Plus applications for up to 25 users on up to five devices per user.</td>
</tr>
<tr>
<td>Office 365 Midsize Business</td>
<td>Businesses with 10-250 employees.</td>
<td>• Office 2013 applications from ProPlus.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Hosted Exchange, SharePoint, and Lync services.</td>
</tr>
<tr>
<td>Office 365 Enterprise</td>
<td>Enterprises/large businesses.</td>
<td>• All Office applications.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Hosted Exchange, SharePoint, and Lync services.</td>
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<tr>
<td></td>
<td></td>
<td>• Enterprise-specific compliance and support.</td>
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</table>

Figure 6

Moving Microsoft Office to the Cloud

In the XaaS model, multiple customers may share the same physical products in a multi-tenant model.
ses of direct versus indirect channel selection, sales training, incentives and support processes.

- **Plan for integration of financials.** The organization’s internal systems need to be integrated with revenue recognition models dictated by its XaaS offering. Revenue models vary on the level of complexity involved in implementing and monitoring product/service usage. Internal systems should be in tune with the overall revenue model followed by an organization (e.g., recurring revenue, try-before-you-buy, Freemium, etc.) to ensure a smoothly functioning organization.

- **Invest in customer adoption:** Create a red-carpet treatment for new XaaS customers. With XaaS models, the initial investment can be much lower. This enables customers to leverage “try and buy” offers, thereby foregoing long decision cycles. “Try and buy” offers allow lower levels of the customer’s organization to make the decision on the use of the service, since the required up-front investment is low or even non-existent.

As customers leverage the service with little or no initial investment, they will need a seamless way to change their billing to increase the volume of usage and extend or renew the duration. Customers expect a no-touch mechanism to renew at their current levels and a very low touch for any change in service. XaaS vendors need to operationalize their learnings to ensure a smooth experience for customers. This means:

  » **Having the ability to follow through on functional requests:** Some XaaS customers have seen smaller vendors struggle with timely follow-through on all their requests. XaaS vendors need to make sure that all functional requests are diligently addressed to meet key customer requirements.

  » **Overcoming integration issues:** Some customers have complained that they lost prior functionalities and tools they’d been using when they transitioned to XaaS. Vendors need to be able to assure customers that they have the necessary tools, pre-built connectors and skilled developers to ensure that XaaS offerings compare favorably with on-premise integration capabilities.

  » **Demonstrating a breadth of functionality:** Many XaaS vendors are new and therefore their core functionality and value proposition remains a work-in-progress. In many application areas, there is still a gap between functionality available on-premise and XaaS options. The breadth of functionality needed today and tomorrow must be carefully examined, communicated and provided to customers and prospects.

Customers expect a no-touch mechanism to renew at their current levels and a very low touch for any change in service.

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