

Vertical Markets, and the Rise of the Partner May 18, 2005

Several macro trends are working their way through the CRM industry right now and having a direct impact on how CRM is sold. These trends include application hosting, tailoring horizontal CRM applications to fit the specific needs of vertical markets, and increasing reliance by software vendors on reseller channels to better meet the demands of specialized markets.

Even in application hosting, whose major attraction is seen by many as its low cost and pay-as-you-go pricing model, vendors are embracing an indirect model. But at the end of the day, how software is sold is far less important than ensuring that a CRM application — or any other business application for that matter — fits the customer's need. Moreover, "fit" is not a one-time issue for most customers. As their businesses change and their requirements evolve, companies of all sizes require relationships with vendors who understand their businesses and their industries.

The reseller market

Frequently, for smaller companies, these vendors are resellers of major software brands who make it their business to bring advanced technology down to them. But resellers are not literally defined by the category designation. If they were, there would be little reason for the primary vendor to give up part of its margin so that another organization could sell its product.

The reseller channel makes the lion's share of its revenues by adding services and by adding value to the primary product, and increasingly, that's where verticalization comes in. Many of the resellers I have spoken with have carved out fairly narrow niches in the market where they have developed expertise — financial services for example — or specialized applications that improve the suitability of horizontal CRM appli-

cations to specific markets. Thus, in return for giving up some profit margin, software vendors gain a competent sales force and some valuable domain expertise that they may not be able to develop in-house.

The reseller channel — or lack of one — can act as a significant barrier to entry for software vendors with expansion in mind. Without a strong and knowledgeable channel, many vendors will simply be out of luck. Frequently vendors of enterprise software build large systems and big corporate infrastructures when selling to early adopter customers, who are frequently large companies. When the time comes to address the needs of smaller companies, many enterprise vendors fall down. Their products are too big and complex and require too much configuration and customization for smaller companies who cannot afford the overhead.

Predicament for vendors

The software market and the CRM market in particular, has reached the point where successful companies know they need to embrace the indirect channel if they expect to garner a significant portion of what many call the "mid-market".

Verticalization and the rise in importance of the indirect channel — are vital to the future success of all CRM vendors and they drive a certain sense of urgency in the industry. The availability of resellers to partner with vendors entering the indirect channel is somewhat inelastic, meaning competent resellers do not spring up overnight.

A reseller channel takes time to build and many of the software vendors entering the indirect market today find themselves competing for the attention of the same resellers. These resellers have spent years building their companies, their vertical market expertise and products, as well as their reputations and some will not be eager to

swap those positions simply to go with a new supplier.

Any decision by a reseller about who to partner with goes far deeper than revenue splits. Since the majority of a successful reseller's revenue can come from selling additional services and specialized products, resellers need to carefully consider how their companies will transition to working with a new or additional vendor partner and the costs involved.

The model franchise

Computer hardware technology has been sold through the reseller channel for decades. For many OEM's enlisting smaller companies specialized to understand and serve the needs of disparate customer bases makes good economic sense. For some percentage of the margin, OEMs can quickly and effectively develop a focused and professional sales team to carry their products into specialized customer areas.

Until relatively recently, the same approach has not been as popular in CRM industry. One primary reason is that CRM started out as an enterprise solution. But as CRM demand has shifted from large enterprises to what many refer to as the "mid-market" a booming opportunity has developed for third parties that can provide the service, support and expertise to help turn generalized CRM into solutions specialized for vertical markets.

The economic drivers for CRM are not very different from the drivers for hardware companies that develop third-party channels. It is too costly and too time consuming — or both — for a single vendor to develop and maintain all of the vertically oriented solutions that are needed by the market. Vendors that try this approach soon find they are resource constrained or that they are missing key markets. By partnering with knowledgeable third parties, software companies — especially CRM vendors — have been able to reach their intended markets cost effectively and with products that embody the domain expertise that comes from working within that market.



About the Author



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Denis Pombriant is a well known thought leader in CRM and he is the founder and managing principal of the Beagle Research Group, a CRM market research firm and consultancy. In 2003, CRM Magazine named Pombriant one of the most influential executives in the CRM industry. Pombriant's latest white paper, "The New Garage" discusses the emerging new enterprise software industry business model.

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