**While there is interest in trying out the consumption business model, software companies must understand product usage in order to model the pricing impact on customers and revenue. But there are many important benefits and insights to be gained from usage.**

# The Benefits of Analyzing Product Usage to Optimize Operations and Drive Business Models

*March 2020*

**Written by:** Mark Thomason, Research Director, Digital Business Models and Monetization

## Introduction

The software industry is rapidly adopting the subscription business model for their "as a service" and on-premises applications for recurring revenue and increased customer engagement. IDC forecasts that 2021 will be the first year where the majority of software revenue will be from the subscription/recurring revenue business model. While cloud-based "as a service" delivery constitutes 39% of subscription revenue, an additional 11% will be from on-premises software that will be bundled with maintenance in a subscription or a contract. Common examples are Adobe's Creative Cloud and Microsoft's Office 365, which are sold as a subscription, but the products are still mostly on-premises with cloud-based features.

Leading companies are moving to the subscription business model for the recurring revenue, business agility, and business valuation and to support current and future software-as-a-service (SaaS) offerings. They are standardizing on SaaS-based monetization applications such as subscription management applications, which can manage the relationship and automate the billing and revenue recognition. These applications integrate with usage intelligence and entitlement applications to keep track of what customers are using and ensure they are authorized.

Of the 1,000+ software companies for which IDC tracks product-level revenue, 80% receive revenue from on-premises products, 61% receive revenue from SaaS, and 42% receive revenue from both on-premises and SaaS offerings (hybrid). The hybrid percentage is slowly rising as software companies transition their customers to cloud-based products. The velocity of the trend from on-premises to SaaS depends on the market, as some use cases benefited from the cloud more than others at first. For example, the collaboration tools (e.g., email) market greatly benefited from the advantages of cloud and is now over 75% SaaS, while the engineering application market is only 4% SaaS. Each market has its own drivers and inhibitors for moving to SaaS, as some benefit more from the connectivity of cloud, while others have use cases where the application operates in remote or high security environments where connection to the internet is unavailable or forbidden.

## AT A GLANCE

### KEY STATS

» Today, 80% of software companies receive revenue from on-premises products, 61% receive revenue from SaaS, and 42% receive revenue from both on-premises and SaaS offerings (hybrid).

» IDC forecast that in 2021, revenue from the subscription/recurring business model will overtake revenue from license and maintenance.

» 42% of respondents reported that they are interested in offering a consumption business model but need help with setting the right amount of consumption pricing.

Companies that are in the hybrid situation have the additional challenge and cost of supporting two development and delivery pipelines. However, they also have the advantage of the customer relationship and already serving customers' needs. Leading hybrid companies (e.g., Adobe) are adding cloud features to the on-premises products that they sell as a subscription so that they can understand usage of the product and make the ownership experience more cloudlike, such as using the log-in for entitlement (auto license key management), update alerts, upgrade suggestions, and training suggestions and for adding features that are cloud enabled (e.g., machine learning, collaboration, analytics). These actions are automated in coordination with the life cycle of the subscription so that customers get a consistent user experience across all products along with a feedback loop to customer success if there is an anomaly.

Given the reality that many software companies will be serving the on-premises and hybrid delivery models for many years to come, IDC recommends that software companies move to a subscription business model and leverage usage and entitlement data for the benefits discussed in the following section.

## Benefits of Leveraging Customer Usage and Entitlement Data

### Gaining Customer and Product Insights

The first benefit is foundational to product managers and product marketing: understanding how customers use a product, preferably down to the feature level. The optimal solution would leverage at least three data streams that provide continuous feedback of customer behavior and indicate customer satisfaction:

» **Account data:** Who the customer is, what the customer paid, and what else the customer has purchased (This data typically lives in customer relationship management [CRM] or subscription management products.)

» **Entitlement data:** A living record of which products and features the customer has access to, when the customer received the product, and when the customer changed or expanded the contract

» **Usage data:** A rich data set that describes when the customer installed or started using the product, which features the customer uses, and the sequence in which the customer uses the features

This data is used together to provide a contextualized customer-centric view so that companies can understand how customers use their products across all delivery models to give them a bigger picture of customer needs and trends, such as:

» Provide data on feature success and priorities for feature investment, enhancement, and end of life

» Forecast scalability needs for IT and Internet of Things (IoT) infrastructure

» Support marketing/sales with actual usage data and insights

» Find superusers and identify testimonial candidates

» Determine uptake of packaged offerings to drive repackaging or new business model

» Validate marketing/education campaign (observing usage change after campaign begins)

For companies that want to better understand their customers, this data can be analyzed with the following data not only to discover affinities, cohorts, and shared behavior but also to uncover deeper insights:

» **Internal customer data** (e.g., sales revenue, buying/renewal frequency, other products used, customer lifetime value, or customer churn)

» **External firmographic data** (e.g., company revenue, number of employees, location, growth rate, or industry)

### *Improving the Customer Experience and Proving Value*

Once entitlement and customer usage data is analyzed, the insights can be put to work to automate tasks that are commonly manual processes in companies (if they are done at all). Because the insights can be highly contextualized, they can be used to drive personalized messages to stakeholders in the company (e.g., sales, support, success teams) or to customers themselves. The following are a few areas that can be improved:

» Prove business value during renewal time by providing salespeople and customers with usage data and relate this to value (e.g., time saved using app). Allow customers to see their usage in their customer portal.

» Benchmark usage across all users to understand macro patterns so that automated actions can be taken if a customer's usage falls below the norm. Examples are sending training videos if a customer doesn't succeed in using a feature, alerting the customer success or renewal team if usage drops off unexpectedly, and messaging a customer with a suggestion to try another product if the customer frequently uses a particular feature.

» Enable a data-driven perspective on the customer value versus the engineering effort (cost) that went into creating the feature.

### *Business Model Innovation*

Perhaps the biggest benefit for leveraging usage and entitlement data is creating and improving revenue opportunities. Many software companies base the pricing and bundling of a new offering on assumptions derived from surveys of sales representatives and customers. Once the product is launched, product managers typically manage by exception, addressing pricing and bundling issues when sales or success presents them with feedback. The main reason why pricing and bundling problems are addressed so infrequently is the risk of making a poor decision on ambiguous data.

Leveraging insights from a constant stream of usage and entitlement data can remove this ambiguity and provide the company with a data-driven perspective of metrics that customers value.
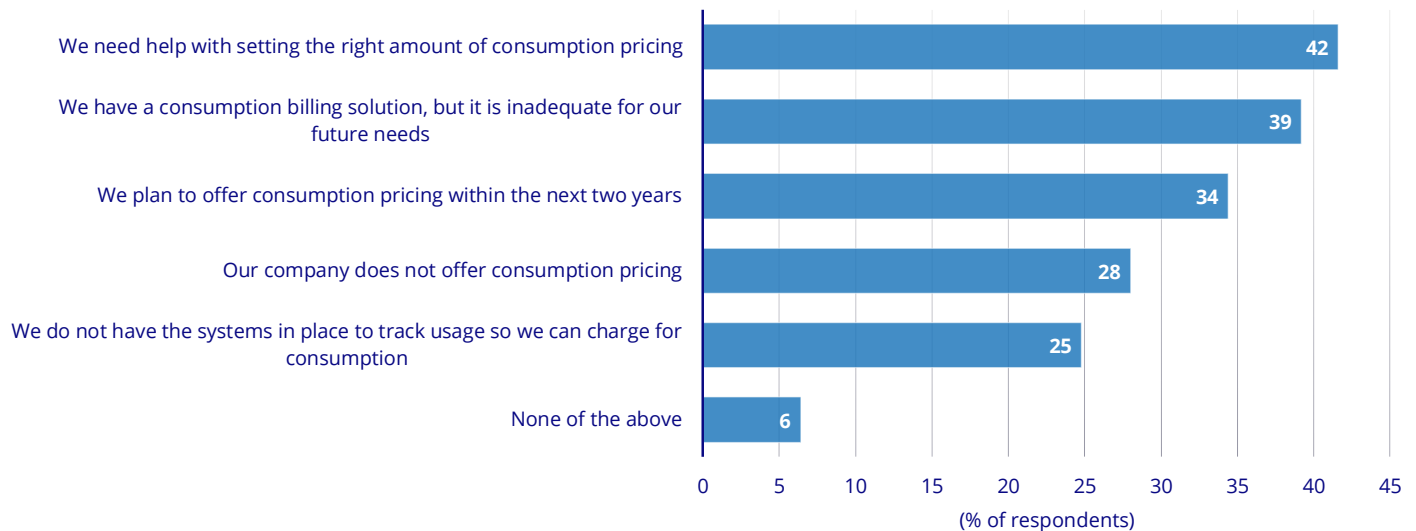
**Ready for a consumption business model? First, you must understand product usage.**

» Create data-driven subscription feature tiers by understanding which cohorts of users value specific features. For example, if a company offers subscriptions focused on company sizes (e.g., small and medium-sized business and enterprise), customer usage data grouped with firmographic data can show if enterprise users are getting value from the features in the enterprise tier—or if the company needs to reconfigure the tiers.

» Discover value metrics to drive a consumption business model. In a recent IDC *SaaSPath Survey* (see Figure 1), respondents reported that they are interested in offering a consumption business model but need help with setting the right amount of consumption pricing. Insights from tracking customer usage can show how much of a feature or resource is used by specific groups of customers so that consumption pricing can be modeled. While consumption pricing can provide higher margins, a best practice is to limit consumption impacts to less than 50% of fixed pricing because customers and vendors want predictability.

» Discover upsell and cross-sell opportunities. Analyzing and benchmarking usage and entitlement data across several products can enable data-driven messages to try a complementary product. This message can go directly to the customer or the sales team to engage the customer.

FIGURE 1: *Consumption Pricing Insights from IDC's SaaSPath Survey*
Q *Which of the following statements apply to your company regarding consumption pricing?*

| Statement | % of respondents |
|---|---|
| We need help with setting the right amount of consumption pricing | 42 |
| We have a consumption billing solution, but it is inadequate for our future needs | 39 |
| We plan to offer consumption pricing within the next two years | 34 |
| Our company does not offer consumption pricing | 28 |
| We do not have the systems in place to track usage so we can charge for consumption | 25 |
| None of the above | 6 |

*n = 125*

*Note: Multiple responses were allowed.*

*Source: IDC's SaaSPath Survey, April 2019*

## No Need to Build Your Own Solution

Just a few years ago, if companies wanted the capability to track and analyze customer usage and entitlement, they had to build their own solution. IDC talked to several companies that either have used spreadsheets or have built their own solution to perform this function, and they indicated that they were happy at first. But commonly we found that the solution did not keep up with application change or allow the companies to scale the solution, as the team that created the solution had moved on. Companies that grew by acquisition had several solutions, which made it impossible to get a single view of the information.

While web analytics products (e.g., Google Analytics) can be used for usage analytics on some SaaS applications, the level of detail can be low because the product doesn't know who is logged in or have an idea of what feature is being accessed. Homegrown entitlement solutions often lead to revenue leaks because they lack the deep integration with software delivery/provisioning, activation and enforcement.

The good news is that commercial products available today can collect and analyze entitlement and usage data across several software delivery methods, including software as a service/platform as a service/infrastructure as a service, on-premises software, software embedded in IoT devices, and APIs. Having a product that spans delivery methods simplifies the effort needed to get a single view of the customer across several products so that customer journeys can be mapped and actionable insights can be automated. These products are starting to leverage advanced analytics and machine learning to discover anomalies and trends such as which customers are likely to churn based on customer behavior. This data can be directly integrated with subscription management, CRM, and customer success applications to provide automated actions for billing and support.

## Considering Flexera Software

Flexera Software was established in 1988 and has over 50,000 customers. Flexera's solutions help software and IoT companies build and deliver secure products while protecting their intellectual property (IP).

The use case in this IDC Technology Spotlight focuses on Flexera's Monetization Platform. The platform enables software companies to manage entitlements, deliver software and updates, provision customers and users, and analyze usage. It works as a central monetization back office for entitlement and consumption data across application delivery methods: on-premises, embedded, and cloud. The solution supports all common monetization models and provides opportunity for smart packaging by differentiating product editions through licensing mechanisms.

In February 2020, Flexera acquired Revulytics, a private company based in Waltham, Massachusetts, and established in 2006. The acquisition of Revulytics added significant depth to Flexera's analytics and data visualization capabilities to deliver actionable insights for product and compliance teams, reducing churn and shrinkage and enabling the consumption business model.

The platform is one of the few that support both on-premises and SaaS applications so that companies can manage and analyze usage and entitlement data across their entire offering portfolio to achieve a single view of the customer. The result enables companies to continually understand the value customers derive from their applications, which allows for data-driven strategic decisions and agile control.

The platform has the following functionalities: Entitlement Management, Software Licensing, Software Delivery and Updates, Usage Intelligence, Compliance Intelligence, and Renewals and Customer Growth.

### *Challenges*

Flexera's Monetization Platform faces the following market challenges:

» **Relative data importance.** Most software companies view usage tracking as a nice-to-have, and investment is not prioritized.

» **"Build versus buy" question.** Because entitlement and usage tracking software *is* software, most engineering departments take on the challenge because it seems elementary to create, especially for SaaS-only products. However, they typically don't build the capability to scale bigger than the current requirements, and software teams are resource constrained. Buying a solution requires cash and engineering time to integrate the solution.

» **Competition.** Entitlement control and usage analytics across several deployment types (on-premises and SaaS) has only a few competitors. However, if a company needs just usage analytics on SaaS, this capability can also be found within a growing number of product and customer experience applications.

## Conclusion and Essential Guidance

Given the market trends to subscription and "as a service," IDC recommends that all software companies consider the subscription business model and continuously leverage customer data to help them package and price new business models more often. This transition requires agility to try packaging and pricing models and a tight feedback loop to understand what worked to enable quick iteration to success.

IDC recommends that on-premises software companies looking to move to SaaS analyze usage data on their existing product to understand which features to carry forward and which to abandon. Because they can't analyze usage data without tracking it first for a few months, the sooner they start, the more data they'll have to analyze.

IDC believes that leveraging the insights from product usage and entitlement data is in its early days. While technology for tracking usage has been around for years, machine learning tools that monitor usage data and analyze the output with ease and at scale are just getting started. If Flexera can address the challenges described in this paper, the company has a significant opportunity for success.

# About the Analyst

*Mark Thomason, Research Director, Digital Business Models and Monetization*

Mark Thomason is Research Director for IDC's Digital Business Models and Monetization practice. Mr. Thomason's research coverage examines traditional and emerging monetization models for digital products and services and identifies disruptive business models and technologies such as cloud services, product-to-"aaS" transformation, and monetization enabled by innovation accelerators such as IoT.

## MESSAGE FROM THE SPONSOR

**Flexera**

Learn more about Flexera's solution for Software Monetization and Usage Analytics:

*https://www.flexerasoftware.com/monetize/products.html*

**IDC** Custom Solutions

The content in this paper was adapted from existing IDC research published on www.idc.com.

**IDC Research, Inc.**

5 Speen Street
Framingham, MA 01701, USA

T 508.872.8200

F 508.935.4015

Twitter @IDC

idc-insights-community.com

www.idc.com

**This publication was produced by IDC Custom Solutions.** The opinion, analysis, and research results presented herein are drawn from more detailed research and analysis independently conducted and published by IDC, unless specific vendor sponsorship is noted. IDC Custom Solutions makes IDC content available in a wide range of formats for distribution by various companies. A license to distribute IDC content does not imply endorsement of or opinion about the licensee.

External Publication of IDC Information and Data — Any IDC information that is to be used in advertising, press releases, or promotional materials requires prior written approval from the appropriate IDC Vice President or Country Manager. A draft of the proposed document should accompany any such request. IDC reserves the right to deny approval of external usage for any reason.