

Secrets of the SaaS Masters

Did you know that there are over 700 venture backed SaaS companies in the market today?

With that many examples of the business model in existence we decided to analyze how some of the best performing companies were organized.

By looking at public financial data for two of the SaaS leaders – Salesforce and NetSuite you learn some interesting facts:

1. The operating expenses for sales and marketing of both companies exceed 50%. Their strategies have been to get market share at any cost, in order to scale to an appropriate size to go public. They committed to heavy, long term investments in sales and marketing.

S&M Expenses Exceed 50% of Revenue in Leading SaaS Companies

Income Statement Summaries for Salesforce.com and NetSuite

	Salesforce.com		NetSuite	
	2007	% of Rev.	2006	% of Rev.
Revenue	<i>thousands</i>		<i>thousands</i>	
Subscription & Support	\$ 451,660	91%	-	-
Professional Services	\$ 45,438	9%	-	-
	\$ 497,098		\$ 67,202	100%
Cost of Revenues				
Subscription & Support	\$ 61,457	12%	-	-
Professional Services	\$ 57,433	12%	-	-
	\$ 118,890	24%	\$ 22,993	34%
Gross Profit	\$ 378,208	76%	\$ 44,209	66%
Operating Expenses				
Research & Development	\$ 44,614	9%	\$ 20,690	31%
Marketing & Sales	\$ 252,935	51%	\$ 43,892	65%
General & Administrative	\$ 84,257	17%	\$ 14,619	22%
	\$ 381,806	77%	\$ 79,201	118%
Net Income	\$ (3,598)		\$ (34,992)	

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2. These expense levels required patient investors. Both companies were unprofitable for many, many years – Salesforce didn't reach consistent profitability until the first quarter of 2008, and NetSuite is hoping to reach break-even operating cash flow by the end of this year.

- Professional Services generates approximately 10% of the revenue at Salesforce. Is there an opportunity for them to get more revenue from services? Or is this the price they pay to grow such a robust ecosystem of partners?

Resulting in Strong Rates of Growth: (Comparables from Leading SaaS Companies)

Financial and Subscriber Comparison for Salesforce.com and NetSuite

Salesforce.com	2001	2002	2003	2004*	2005	2006	2007
Customer & Subscribers							
Customers	1,500	3,500	5,700	8,700	13,900	20,500	29,800
Subscribers	30,000	53,000	76,000	127,000	227,000	393,000	646,000
Subscribers/Customer	20	15	13	15	16	19	22
→ Customer Growth Rate	-	133%	63%	53%	60%	47%	45%
Revenue Ratios							
Revenue (thousands)		\$22,410	\$50,990	\$96,020	\$176,375	\$309,857	\$497,098
Revenue/Customer		\$6,403	\$8,946	\$11,037	\$12,689	\$15,115	\$16,681
Revenue/Subscriber		\$423	\$671	\$756	\$777	\$788	\$770
Employees			400	675	1,100	1,800	2,460
Revenue/Employee			\$127,475	\$142,252	\$160,341	\$172,143	\$202,072

* company started in 1999; IPO in 2004

NetSuite	2001	2002	2003	2004	2005	2006	2007*
Customers							
						5,400	
Revenue Ratios							
→ Revenue (thousands)		\$3,136	\$8,345	\$17,684	\$36,356	\$67,202	
Revenue/Customer						\$12,445	
Employees						600	
Revenue/Employee						\$112,003	

* company started in 1998; IPO in 2007

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What are the implications of this for the smaller SaaS based company – either privately funded, or with less patient investors?

We believe that many smaller SaaS based companies are guilty of under spending on sales and marketing. They aren't aggressively advertising, brand building and growing their ecosystems.

By not generating market leading customer momentum, they risk being irrelevant in their market segment. Being irrelevant is the path to a slow death. Without exciting momentum and the EBITDA to go with it, it will be difficult to find funding or an exit for your SaaS company.