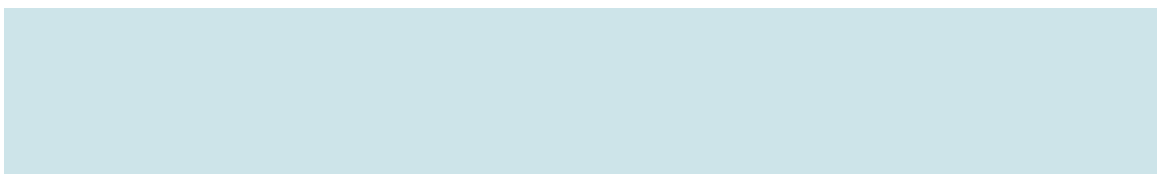




SugarCRM (vendor analysis)

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The Ovum view

SugarCRM has done impressively well since its launch in early 2004. It stands at the confluence of four high-growth IT market segments: small and mid-sized businesses (SMBs), customer relationship management (CRM), software as a service (SaaS) and open source software (OSS). It has also adopted a sensible strategy that keeps it close to its customers and partners, and identifies salesforce.com, rather than traditional CRM vendors, as its main competitor.

The company has been very clever to build what is essentially an OSS core for CRM, with the added scope to build modules, or buy them, to run on top of it. As it moves from early OSS adopters to the mainstream, and from small deployments to larger ones, the company needs to strengthen its partner network and direct approach to sales.

Company

Three former E.piphany executives (CEO John Roberts, CTO Jacob Taylor and Clint Oram, now responsible for managing SugarCRM's community) got together in April 2004 to develop the Sugar Sales component. They opened it to contributions from the open-source community via Sourceforge.net in June, moved out of stealth mode after a first venture capital injection in August, and launched a commercial version, Sugar Sales Professional, in October. The product received a fairly positive reaction from both community and customers. In less than a year it attracted 250 paying customers. It claimed about 800 of them in mid 2006.

Financial viability

SugarCRM does not release any financial details. We believe it will generate about \$15 million in 2006 and will not be profitable yet.

SugarCRM has plenty of cash following three rounds of venture capital funding, reflecting the new interest of venture capital companies in open-source application software companies. It first raised \$2 million in August 2004 from Draper Fisher Jurvetson (DFJ), then \$5.75 million in February 2005 from DFJ and Walden International, followed by \$18.77 million in October 2005 from the previous two investors, as well as New Enterprise Associates (NEA).

SugarCRM claims that it did not need the money for the third round just yet. However, besides speeding up investments in R&D, on-demand infrastructure and customer services, the third round enables it to benefit from NEA's contacts. NEA is an investor in arch-rival salesforce.com.



Products and services

Products

Functionality

SugarCRM markets the Sugar Suite of CRM (marketing automation, sales management and customer support) modules supported by reporting and collaboration modules. It comes in three editions, as shown in *Figure 1*: Open Source, Professional and Enterprise. The company launched the first two in 2004 and the third in August 2005.

Figure 1 Sugar Suite editions



Source: SugarCRM

It makes about two-thirds of its source code available to the open source community via Sugar Open Source. The extra functionality in the other editions is proprietary. There are clear differences between the Open Source and Professional editions, both in terms of technology (for example, workflow engine and wireless access) and functionality (for example, an extra contract management module). There is much less difference between the Professional and Enterprise editions. The company needs to evolve them separately to differentiate its offerings more strongly.

The company has kept upgrading its suite since the first release of Sugar Sales 1.1 in July 2004, at a pace that is unusual for enterprise business applications (except for SaaS ones) and may have made it hard for some users to keep up. Version 1.5, the first professional version of the product in September 2004, was followed by version 2.0 a month later, 2.5 in January 2005, 3.0 in April, 3.5 in August and 4.0 in December 2005. The latest version, 4.2, shipped in April 2006. Version 2.5 expanded from sales to customer service support and was the first to be marketed as Sugar Suite. Version 4.0 introduced much-needed workflow capabilities. Version 4.5 is to ship in summer 2006.



Deployment

Sugar Professional Edition (SPE) and Sugar Enterprise Edition (SEE) are available in three deployment options: Sugar On-Premise, Sugar Cube (appliance) and Sugar On-Demand (hosted). Slightly less than two-thirds of the company's customer base has opted for Sugar On-Premise, slightly over one third has turned to Sugar On-Demand, while only about 5% (but growing to 10% over the next year according to SugarCRM) have picked Sugar Cube. The latter has proved particularly successful in the public and financial service sectors.

Sugar On-Demand comes in two versions: a multi-tenant database version limited to between 300 (SPE) and 500 (SEE) users, and a dedicated database (and server) version. Made-to-order Sugar Cube also comes in two versions that can run either SPE or SEE. Sugar Cube 1005 can handle up to 100 users and 1 million data rows, while the 3005 version handles up to 400 users and 10 million data rows. Multiple Sugar Cubes can be clustered, allowing multiple machines to work with the same database.

Technology

Sugar Suite is accessible via a standard web browser. SPE and SEE are both accessible via wireless devices. SEE is the only one to feature offline client synchronisation.

Originally built on top of a LAMP (Linux, Apache, MySQL and PHP) software stack, Sugar Suite expanded to the Windows operating systems, then the Oracle database (9i and 10g). Only SEE supports Oracle. Version 4.5 of both SPE and SEE will add support for the Microsoft SQL Server database, as well as other Microsoft products. It will be 'optimised' for Microsoft's technologies. These moves open up more opportunities for SugarCRM, but increase development costs. Salesforce.com, for example, does not have this problem, as it only needs to support a single architecture and database. Sugar Suite also runs on Unix, BSD and Mac OS X.

Services

SugarCRM is keen not to compete with its channel partners from a service point of view. It intends to remain a software vendor with no more than 30% of revenues from services. Considering its reliance on third-party channel partners, this is a sensible strategy.

SugarCRM provides professional services covering various aspects of CRM adoption (such as strategy development and TCO/ROI analysis), as well as Sugar Suite implementation services that deliver a variety of customisable options.

In April 2006, the company announced the Sugar Network, which provides Sugar Open Source users with support (one support case per year plus access to Sugar Support Portal to access forums, documentation, product alerts and bug trackers), as well as product extensions (plug-ins for Microsoft Outlook and Word) and online training. However, Sugar University's online training modules will not be available



until summer 2006. Sugar Network is included with SPE and SEE subscriptions which also include source code, 12 months of updates, installation assistance, as well as trouble ticketing with patch and fix distributions.

In addition, SPE and SEE subscriptions respectively feature SugarCRM's standard and extended support plans. The first plan offers four business hours maximum response time for Priority 1 (P1) cases and is limited to online support. Extended support is faster (two business hours) and adds phone support during business hours. There is also a Premium Support option that offers one-hour response time, 24x7x365 access to experts, after-hours phone support for P1 cases, a dedicated support representative and quarterly account reviews.

Licensing and pricing

Licensing

SugarCRM sells annual licences rather than perpetual ones. It licenses its software on a per named user basis, which requires users to keep a tight management of who is entitled to what. Its Sugar Public License (SPL) is a derivative, more restrictive, version of the Mozilla Foundation's Mozilla Public License (MPL) 1.1 that has not been approved by the Open Source Initiative. It requests code changes to be disclosed if the software is distributed to a third party, but prevents the modified code from being sold. It also requests each user interface screen to display the 'Powered by SugarCRM' logo and a copyright notice that direct users back to www.sugarcrm.com.

In addition, in February 2006, SugarCRM became the first commercial open-source application vendor to adopt the Microsoft Community License (MCL), one of Microsoft's three Shared Source licensing models (that also include the Microsoft Reference License – MRL – and Microsoft Permissive License – MPL). It plans to introduce MCL with version 4.5 of its offering. MCL is less restrictive than SPL but more restrictive than MPL. MPL allows anybody to modify and redistribute source code and to charge a licence fee for any added code. MCL enables users to keep modified code to themselves (and limits what third parties can do with modified code that includes Microsoft source code). MRL only allows licensees to view (Microsoft) source code but not modify or redistribute it.

Pricing

Sugar Network costs \$119 per user, per year. Additional single support cases cost \$95 each (or \$400 and \$750 per year if bought in sets of five or ten).

SPE and SEE are available for \$239 and \$449 per user, per year respectively for on-premise deployment (SugarCRM does not limit customers to a set number of cases). Their hosted equivalent starts at \$39.95 and \$74.95 per user monthly, respectively with subscriptions sold in three-month or one year increments (six month increments for the Sugar Dedicated On-Demand version). Some companies (such as iRadeon),



are also offering Sugar Open Source on a hosted basis at a much lower price (from \$4 to \$9 per user per month, based on the number of users in iRadeon's case).

Sugar Cube 1005 and 3005 respectively start at about \$4,500 and \$8,000, excluding Sugar Suite subscription costs. Pricing drops with volume licensing.

Market strategy

Positioning

A CRM vendor that targets SMBs

SugarCRM benefits from the current CRM renewal business in SMBs, while having to cope with an increasingly competitive landscape.

CRM was fashionable at the turn of the century then fell out of grace. It is back in fashion: according to the US National Venture Capital Association, between early 2004 and late 2005 CRM companies received more than \$400 million in funding, reflecting this new-found interest (open-source start-ups received about the same amount in 2005). The first wave of CRM solutions targeted large companies; the latest is interested in SMBs (companies with up to \$1 billion in revenue), a large, and largely untapped (especially from a CRM point of view) segment increasingly targeted by every software vendor.

An SMB player moving up-market

Mainstream open-source software adoption started with the Linux operating system and various development tools. It then moved up the software stack towards middleware and application server technology. It is about to reach business applications, including business intelligence tools, content management applications and ERP/CRM solutions. These solutions are proving more successful in the SMB market than their predecessors, which were predominantly adopted by large enterprises.

SugarCRM claims 800 customers (against about 22,700 for salesforce.com in May 2006) and 10,000 users. The company originally targeted SPE at small deployments of five to 20 users. It now targets SEE at 100 to 500+, or even 1,000+-seat deals. However, it will take time to reach Fortune 100 companies. SugarCRM may have been rather successful in moving customers from Sugar Open Source to SPE, but the move from SPE to SEE has barely started. The company will have to prove its ability to grow its subscriber base at a faster rate than its customer base the same way salesforce.com moved up from 13.9 subscribers per customer in fiscal Q4 2004 to 19.6 in Q1 2007. However, with an average of 17 users per customer it is not too far behind.

Like salesforce.com does at the moment, SugarCRM can successfully target large decentralised organisations with multiple small offices spread over a large geographic area. Unlike salesforce.com, which has quite a number of customers with more than



1,000 users – including Cisco, its largest with over 6,000 users – the company has yet to announce big deployments, although it is likely to do so before the end of the year. Its only large and publicly announced deal so far is with US tax consultants BDO Seidman (December 2005). Over two years, BDO Seidman will roll out SPE (but not SEE) across 30 offices and 250 independent partners (independent CPAs and consulting companies) across the US to reach a grand total of up to 9,000 users. The customised solution developed jointly by SugarCRM and the BDO Seidman IT team will not be a fully-fledged CRM system but a communication and resource sharing platform between BDO and its partners.

A vendor that rightly positions itself against SaaS vendors

SugarCRM defines itself as a third-generation CRM vendor, following first-generation closed source software vendors like Oracle, and second-generation closed source SaaS vendors like salesforce.com. Only one third of its customer base has opted for Sugar On-Demand since its launch in November 2004. However, SugarCRM is right to battle even more fiercely against second generation vendors than first generation vendors with a flexible offering that not only gives the choice between single-tenant and multi-tenant options, but also enables customers to move easily between traditional, appliance-based or hosted deployment options. It is also right to have adopted a rather aggressive hosted pricing strategy. Pricing is less an issue in on-site deployment, as CRM application implementation costs far outweigh software ones, but it is key to compete with the likes of salesforce.com.

A pragmatic 'commercial open source' vendor

SugarCRM has adopted a pragmatic 'commercial open source' strategy that has driven it away from open source orthodoxy towards mixing open and closed source software and practices. It will do SugarCRM no harm. SMBs, and the partners that cater for their needs, are a pragmatic bunch, unlikely to be bothered by Sugar Suite's proprietary extensions, licence limitations, support for Oracle and Microsoft databases, and the increasingly tighter partnership with Microsoft.

Oracle support was required for it to move higher up the enterprise market. With more than a third of its installed base running on Windows, the company is also right to have a dual Linux-Windows strategy. Most other open source software vendors do. SugarCRM has gone one step further though. It was the first to adopt a Microsoft-defined open source licence. It was also the second (after JBoss in late 2005) to enter into a partnership with the view to optimise its offering for Microsoft platform technologies. We see these moves as positive ones considering the fact that many mainstream SMBs are quite happy to use Microsoft technologies, and are wary of any wall-to-wall move to open source. However, it should position its software against Microsoft's CRM offering more aggressively.

The need to build on its initial success

The company's ambition to move up-market will not only require stronger product functionality but, more importantly, stronger direct and indirect sales channels, and a



higher-profile marketing strategy. This will be key for SugarCRM to cross the chasm, not only between early OSS SMB adopters and mainstream ones, but also between SMBs and large companies.

The company argues that being open source makes it more effective than its competitors – both first- and second-generation ones – from a sales and marketing point of view. It has indeed managed to create a positive feedback loop, whereby its product suite has proved good enough to attract an active and growing community of partners and customers that work at strengthening the suite, thus attracting more organisations. This positive feedback loop has enabled the company to increase mindshare and market share, while keeping sales and marketing costs at a much lower level than that of the competition.

In the battle to build a viable alternative to traditional CRM players and more established software-as-a-service CRM players, SugarCRM needs to tackle the issues that these other participants have faced and that they all still face, such as channel strategy, distribution models and the definition of a compelling value proposition. These elements of sales and marketing execution are likely to be greater determinants of success than technology alone. These are issues that all early stage software organisations need to address as they move towards scale and maturity. SugarCRM's status as an open source provider alters the nature of some of the challenges, through, for example, the ability to 'try before you buy', but many of the issues remain. Two areas where we would like to see SugarCRM focus its attention are in marketing and value proposition articulation.

In the marketing area SugarCRM has adopted a fairly low-key approach. Given the highly competitive market we would like to see SugarCRM be bolder in its market messaging and to look at altering the direct-indirect channel mix – driving growth will need well structured incentives for both direct sales and indirect sales partners. Cost savings are an element of the value proposition for SugarCRM. However, we would like to see the proposition evolve to encompass a broad value analysis, adding a more business-focused set of messages around business value – moving the buying point from the IT cost savings debate into the line-of-business decision-maker's mindset. The existing focus on the proportion of revenues that fund R&D, as opposed to other activities, needs to be broadened along the lines we have mentioned – it is too narrow a message in its current form.

By developing its marketing and value proposition along these lines, SugarCRM will have greater ability to push for growth.

Competitive differentiation

Community spirit

SugarCRM has been very successful in building a community around its open source product. It quickly managed to get a strong following among open source developers that led to the March 2005 launch of SugarForge.org to:



- encourage the development of third party extensions. These range from document and knowledge management systems to timesheets, database back-ups, data synchronisation, mobile device connectors and language packs. Essentially, it is offering a service where R&D effort in the core 'non-differentiating' layers of CRM is pooled, allowing others to build vertical/function-specific layers on top.
- provide support and information services, including development and implementation advice, user forums and customer feedback.

At the end of 2005, SugarForge involved over 3,000 developers and managed over 130 projects. This grew to nearly 5,000 developers and over 200 projects in early June 2006 (and from 265,000 downloads in October 2005 to nearly 1.7 million downloads against 350,000 downloads for Sugar Suite itself between July 2004 and June 2006).

SugarCRM's partners are the main engine behind SugarForge. Active partner involvement in the development of Sugar Suite and, more importantly, Sugar Suite add-ons has proven key to attracting customers to both SugarCRM and its partners. The more SugarCRM expands beyond early open-source SMB adopters that like to tinker with source code towards mainstream ones that wisely don't, the stronger the role of its partners in SugarForge. SMBs do not have the time to tamper with open source code. Those that do should be better off doing something else entirely.

Like Sugar Suite itself, Sugar Suite add-ons come in two versions: free open source and commercial with the free option available on SugarForge.org. In order to boost partner revenues, the company is working on a commercial alter-ego of SourceForge, dubbed SugarExchange, for partners to sell the commercial version of the software components that they have developed. This will no doubt increase partners' dedication to Sugar Suite.

Customisability

SugarCRM makes the usual open source claims in terms of better quality (based on the openness of the source code and the development process) and innovation. The latter is less defined in terms of new design or functionality than in terms of adaptability to customer feedback and product (as well as product interface) customisability. Customisability is key to attracting both SMB users and channel partners and to competing with the likes of salesforce.com, which also defines customisability as one of its key differentiators.

The company claims that PHP, the language that underpins Sugar Suite, makes it easier to customise the product. We believe that customisability comes more from the fact that Sugar Suite supports customisation in a way that many other CRM products fail to do based on:

- tools for non-technical people to configure, rather than customise, the application
- a modular design with a plug-in architecture for third party extensions. Since version 3.5 (the SEE version in August 2005), Sugar Suite features the Sugar Module Loader installation utility for adding or removing third-party add-on



modules, and simplifies customisation upgrades via event handlers that preserve modifications. However, SugarCRM wisely recommends reviewing user feedback on SugarForge for each extension before loading them.

This allows channel partners to easily add value to the product. The danger is to customise the wrong thing and/or lock the customer into a highly customised product. Channel partners have a key role to play at both levels. SugarCRM needs to make sure it does not play the 'customisability to lock customers in' card too blatantly.

In March 2006, the company joined the Eclipse Foundation as an Add-In-Provider member (so did salesforce.com), claiming that the Eclipse IDE was the development platform of choice for the SugarForge community members.

The company is right to emphasise product interface customisability to boost software adoption by end users. Accessing Sugar Suite through a web browser, users can choose their own 'skins' to suit their individual tastes and manage multiple information sources through Microsoft Outlook integration and content syndication. The company distinguishes between user types (for example, Field workers versus office workers) and role to adapt its software to specific tasks. Its interface is relatively similar to salesforce.com's, making the switch easier.

Sales strategy

Channels

SugarCRM sales team (representing about 25% of its workforce of about 70 employees in mid 2006) is split into three teams. The first two teams are direct salespeople, respectively in charge of SMB and large corporate accounts. The third handles the channel that generates between 30% to 40% of total revenues.

The company benefits from leads generated via the SugarForge community, which also enables channel partners to show off their expertise and dedication, and turn unpaid support or contribution into a commercial relationship.

SugarCRM claims about 150 active partners, up from about 45 in mid 2005, although its website only lists slightly more than 60 of them. This number excludes the 20 companies or so, such as iRadeon that provides Sugar Open Source on a hosted basis, which are not official SugarCRM partners. Any company can pick up Sugar Open Source and offer it provided it displays the 'Powered by SugarCRM' logo.

SugarCRM enables its channel partners to generate both:

- one-off revenues from CRM-related professional services, Sugar Suite customisation to meet geographical and/or vertical market requirements, and from add-on extensions either directly or via the forthcoming SugarExchange
- recurrent revenues from support and/or hosting services.

The company rightly tries not to compete with its partners for service revenues. As it moves up-market, it will need to:



- develop a more direct sales channel
- find larger, more influential, partners, then train them
- boost the quality of its channel partners via certification programmes or add-on ratings; for example, to boost user confidence.

Geography

The company's indirect channel network has enabled it to have a geographical reach that is unusual for a company its size and age. About a third of its customers are outside the US, including about 20% of them in Europe. This is not bad for a company that does not have a direct presence in Europe. However, with 23 channel partners listed on its website at the beginning of June 2006 (four in Germany and the Netherlands, three in France, two in Switzerland and the UK, one in Italy, Portugal, Spain, Luxembourg, Sweden, Finland, Poland and Romania), Europe outnumbered all other regions. Other listed partners included one African (Nigeria), 22 North American (19 of them in the US), five Latin American (Argentina, Brazil, Chile, Columbia and Mexico) and 13 in Asia-Pacific (five in Australia, two in New Zealand, Hong-Kong and Japan, and one in Singapore and Thailand). Most of these partners are small companies operating at national or regional levels, except for Optaros which is present in Germany, Switzerland and the US.

In late 2005, the company opened an office in Shanghai to house about seven engineering and quality assurance staff. The team will grow and take up more development work, helped by the fact that Yun-Ping Hsu, vice-president of engineering, can speak Chinese natively.

Sugar Suite deployments can have multiple languages available to users with each user picking his or her language preference. Version 4.5 is due to ship in summer 2006, and will provide enhanced support for multibyte character sets and UTF-8, along with support for complex character representations like Kanji.

The company claims that its software has been translated into 40 languages. In fact it is really available in 27 languages: while there are 40 language packs (up from about 15 in mid 2005) developed by resellers as Sugar Suite extensions, many of them are redundant. There are, for example, three Brazilian and simplified Chinese language packs and two packs for Danish, French, Hungarian, Norwegian and Portuguese. This may confuse users and shows the need for the company to channel its partners' ingenuity more proactively. Nonetheless, the number of language packs reflects the vitality of SugarCRM's community of partners.

Partners

SugarCRM's reseller partner program which was launched in December 2004 distinguishes between small business, premier and OEM partners. Both small business and premier (systems integrators and consulting companies) partners benefit from SugarCRM's lead referral programme, but only premier ones have access to technical phone support. Both can resell Sugar On-Demand but only premier ones can sell the dedicated hosted solution.



Out of about 150 active partners, the company claims that 90 of them are Premier partners. However, many of them are too small, and it needs to recruit, then train, larger partners. It also has just a couple of OEM partners and needs to be much more proactive in attracting these types of partners. Fortunately, it has just brought in an Oracle veteran to head its partnership programme, so more is to come in this area.

Key partners include Novell, Oracle and Microsoft. The company joined the Novell Market Start programme in September 2005, the same month it joined Oracle PartnerNetwork. Market Start is the most useful program. It enables SugarCRM to leverage Novell's support organisation and channel partners, including (since early 2006), Novell's training partners.

SugarCRM partnered with Microsoft in February 2006 to enhance interoperability between its offering and Microsoft's technology, and adopt the Microsoft Community License. That same month it partnered with SpikeSource, agreeing to distribute the Spike Stack LAMP certified software stack and resell the Spike Net update service. Spike Net includes a one-year subscription to MySQL AB's Network open-source database update service. It is also negotiating with SAP to optimise Sugar Suite for technologies the same way it is being optimised for Microsoft ones.

Technology partners include mobile/wireless technology vendors Funambol (April 2005) and Sona Mobile (February 2006 – two months before salesforce.com's acquisition of Sendia, a maker of mobile technology).



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