

IBM Business Partner Profitability

Key Findings

► IBM Middleware: A 21X Sales Multiple

IBM business partners report that for every dollar a customer spends on IBM middleware, an additional \$21 is spent by that customer on related software, hardware and services¹.

► IBM Middleware Drives Services Revenue

Sales of such high-margin services as application development and consulting are driven by sales of IBM middleware. Business partners worldwide report that every dollar in sales of IBM middleware generates nearly \$8 in sales of their own companies' services. Considering that sales of services account for 62 percent of a typical business partner's annual revenue, the role of IBM middleware as a services revenue-driver is significant.

► The ROI of IBM Certifications: \$1 in Training Yields \$345 in Revenue

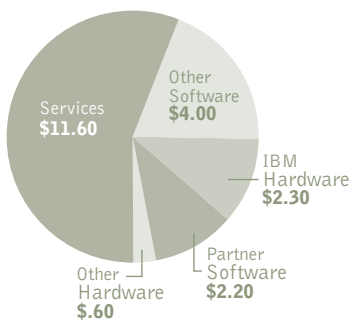
For every dollar invested in IBM software-related education, training and certification, business partners generate \$345 in software and services revenue resulting from their IBM practice. Business partners in North America, on a median basis, invest \$5,000 (per company) annually in IBM software-related education, training and certification. In return, business partners, on a median basis, generated \$1.73 million in IBM-related software and services revenue last year.

► More IBM Certifications Lead to Higher Revenue and Profits

Business partner organizations with more IBM software certifications report higher revenues and higher profits. On an average, per-employee basis, organizations with five or more IBM certifications report \$18,931 in revenue per employee and \$5,163 in profit per employee based on IBM customer engagements built on IBM middleware. For organizations with four or fewer IBM certifications, per-employee revenue reported is \$6,825 while per-employee profits are \$1,271.

IBM MIDDLEWARE SALES MULTIPLIER FOR PARTNERS

For every dollar a customer spends on IBM middleware, how many dollars of other related software, hardware and services are sold?

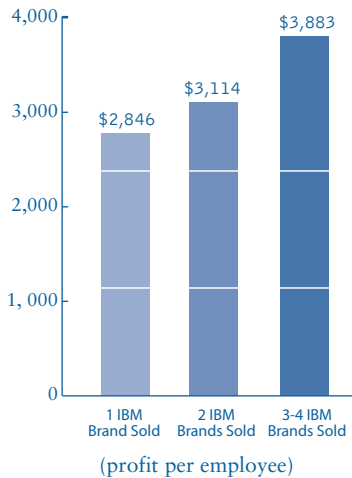


North American Data
Source: Reality Research & Consulting

¹ NORTH AMERICA. THE SALES MULTIPLIER IS \$13 FOR IBM BUSINESS PARTNERS IN EUROPE.

Figure 1

▶ IMPACT OF CROSS-SELLING IBM MIDDLEWARE



Source: Reality Research & Consulting

▶ Faster Sales Cycles for Organizations with More IBM-Certified Employees

On average, business partners with five or more IBM-certified employees sell their first \$100,000 of IBM middleware related products and services into a single new account in less than seven months; two months sooner than partner organizations that have four or fewer IBM-certified employees. The next \$100,000 of revenue into that account also comes sooner for organizations with more IBM-certified employees (14 months versus 18 months for a \$200,000 sale into a single account).

▶ Faster Sales Cycles from Cross-Selling IBM Middleware

Organizations that sell/influence three or more IBM power brands (DB2, Lotus, Tivoli, WebSphere) report that they sell their first \$100,000 of IBM-related products & services into a single account in seven months compared with eight months for organizations focused on only one IBM brand. The next \$100,000 of IBM-related products and services comes two months sooner in companies that cross-sell, resulting in a three month faster total sales cycle for the first \$200,000 of IBM-related products and services.

▶ Cross-Selling IBM Middleware Increases Revenue and Profitability

Business partner organizations that sell/influence three or more IBM middleware brands also report more than twice the revenue per employee and 36 percent more in profit per employee than organizations that sell only one IBM middleware brand. On an average basis, organizations selling three or more IBM middleware brands report per-employee revenue of \$16,116 and per-employee profit of \$3,883 on customer engagements built on IBM middleware. For organizations selling only one brand of IBM middleware, per-employee revenue is \$7,721 and per-employee profit is \$2,846. (see Figure 1).

▶ Business Partner ROI: 9 to 1 Investment to Profit Ratio

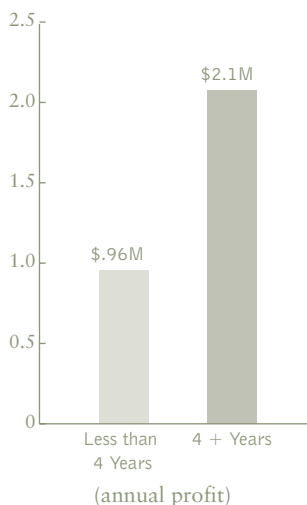
Business partners report that every dollar of investment into their IBM practice yields \$9 of profit. An average investment of \$179,000 yields \$1,678,000 in profits.

▶ IBM Business Partner Profits Get Better with Age

IBM business partner profits are higher for long-term partners. For partners that have been in IBM's program for four years or more, annual profits related to IBM middleware are an average of \$2.1 million. That is more than twice the average profits of \$.96 million reported by partners that have been with the IBM partner program for less than four years. (see Figure 2).

Figure 2

▶ PROFIT BY YEARS AS A PARTNER



Source: Reality Research & Consulting

Topics

- ▶ **SECTION 1:** Background and Objectives
- ▶ **SECTION 2:** Methodology and Partner Demographics
- ▶ **SECTION 3:** Partner Business Models
- ▶ **SECTION 4:** Customer Profiles
- ▶ **SECTION 5:** Business Partner Profitability
- ▶ **SECTION 6:** IBM Middleware Sales Multiplier for Business Partners
- ▶ **SECTION 7:** Impact of IBM Education & Training
- ▶ **SECTION 8:** Sales Cycle Acceleration
- ▶ **SECTION 9:** Business Partner ROI on IBM Software
- ▶ **SECTION 10:** Conclusions

1 Background and Objectives

Companies selling technology solutions today face an array of challenges. Integration of legacy systems with second and third generations of technology is complex. Convergence of different data types is increasing. E-business deployments require system-wide attention to detail. In addition to these factors, the market is more demanding. Buyers of technology solutions are scrutinizing all purchases and need to know the return on investment before they spend on technology.

Against this market background, *Reality Research & Consulting* believes that successful business partners need to:

- ▶ Leverage sales and technical knowledge across their organizations
- ▶ Maximize training and certifications in their organization's core competencies
- ▶ Develop selective vendor relationships based on mutual business-building

The purpose of this white paper is to help IBM business partners identify factors that will build their businesses and increase their profits based on the three success factors listed above. Benchmarks and data points in this white paper are from a research study commissioned by IBM. More than 500 business partners on three continents were surveyed in an effort to identify partner business drivers and build partner profitability.

Specifically, this survey focused on the profitability and ROI surrounding business partners' IBM middleware business – the business software used to support such operations as transaction processing, web application serving, networking, security, database, systems management, collaboration and other critical functions.

2 Methodology and Partner Demographics

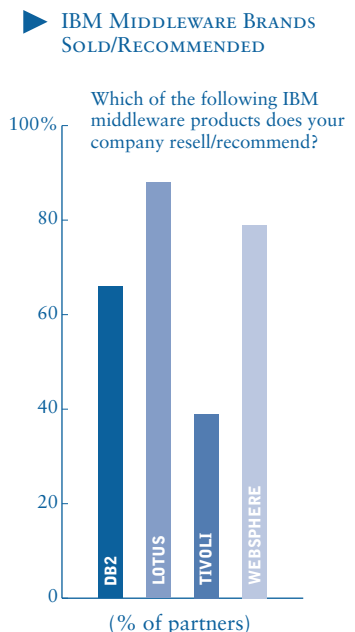
IBM commissioned Reality Research & Consulting, an independent market research unit of CMP Media LLC to conduct this research. Reality Research completed a total of 514 quantitative interviews with premier and advanced IBM partners in North America (232), Europe (265) and Latin America (17). Included in that number were 170 members of IBM's new Top Contributor Program.

All interviews were conducted via telephone from Nov. 30, 2001 through Jan. 3, 2002. Interviews were conducted on a "blind" basis in which IBM was not identified as the sponsor of the survey.

Sample for the survey was drawn from the IBM PartnerWorld for Software Partner database. The 514 completed responses reflect a margin of error of +/- 4.4 percent at a 95 percent level of confidence.

Figure 3 identifies the brands of IBM middleware sold and influenced by the business partners surveyed. As the percentages in Figure 3 indicates, the vast majority of IBM partners are selling/influencing two or more brands of IBM middleware. In fact, six out of 10 partners sell three or more brands of IBM middleware. This implies that there are synergies in selling/influencing across IBM's family of middleware products in such areas as technical compatibilities and integration, and in leveraging IBM sales certifications throughout business partner employee staffs.

Figure 3



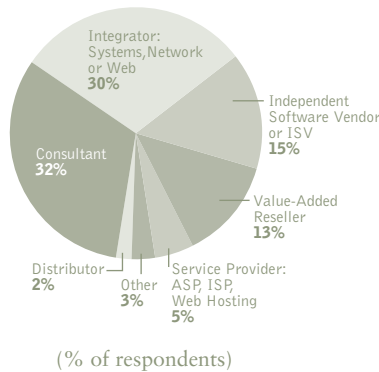
Base: 514
Source: Reality Research & Consulting

Figure 4 identifies the term that survey respondents said best describes their companies' business model. In keeping with industry trends, the largest segment of business partners have adopted the consultant business model. These business partners emphasize the services side of their businesses. Moreover, as consultants, these companies position themselves as strategic partners to their customers, stepping above the price-driven, profit-draining pitfalls of product order-takers.

Figure 5 reports total annual revenue for survey respondents. Where relevant throughout this white paper, analysis will focus on segmentation of business partners by total annual revenue. This segmentation is important because Reality Research believes that business partner companies do not scale uniformly from low revenues to high revenues. Instead, employee allocations, revenue mix, core competencies, customer segments and other factors typically differ depending on the annual revenues of business partners.

Figure 4

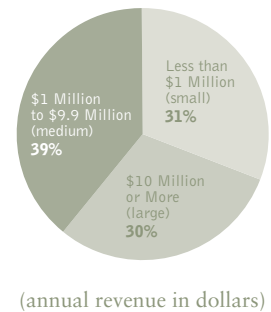
SURVEY RESPONDENT DEMOGRAPHICS:
BUSINESS MODELS



Base: 514
Source: Reality Research & Consulting

Figure 5

SURVEY RESPONDENT DEMOGRAPHICS:
TOTAL ANNUAL REVENUE



Base: 436
Source: Reality Research & Consulting

3 Partner Business Models

Consistent with overall industry trends, IBM business partners have migrated to a revenue mix in which IT services such as application development and consulting drive the largest portion of their overall sales. This is positive for a couple of reasons. One is that it limits business partner exposure to price wars and the resultant profit margin erosion that come from a heavy reliance on solely reselling products. The second reason is that sales of services are a long-term account control tactic that helps business partners learn more about their customers' technology needs.

An analysis of small (less than \$1 million in annual revenue) business partners shows that these companies are the most reliant on services, deriving 71 percent of sales from services. This is understandable because small business partners are more vulnerable to product price pressures from such sources as on-line catalog resellers and retailers (see Figure 6).

Figure 6

REVENUE SOURCES FOR AVERAGE PARTNER			
What percentage of your company's revenue in the last 12 months came from:			
TYPE OF REVENUE SOURCE	% of total	Small	Med/Large
IT SERVICES	62%	71%	57%
INTERNALLY DEVELOPED SOFTWARE	13%	15%	13%
RESALE OF HARDWARE	11%	4%	14%
RESALE OF SOFTWARE	8%	5%	9%
RESALE OF PACKAGED OR MANAGED SERVICES	4%	2%	4%
INTERNALLY DEVELOPED HARDWARE	2%	2%	2%
OTHER	2%	1%	2%

Base: 514
 Source: Reality Research & Consulting
 (Percentages do not add to 100 because of rounding)

An analysis of small (less than \$1 million in annual revenue) business partners shows that these companies are the most reliant on services, deriving 71 percent of sales from services.

In contrast, medium and large business partners (\$1 million or more in annual revenue) are better positioned to compete on volume pricing and derive one-fifth of their revenues from resale of hardware & software. Sales of services for these larger business partners account for about half of their revenues. Identification of revenue sources is important in helping partners understand their business drivers.

Application development and professional services such as consulting are the dominant primary services for IBM middleware business partners (see Figure 7). Primary services are defined as those that account for 50 percent or more of the business partner's total services-related revenue.

Figure 7

PRIMARY SERVICES SOLD BY PARTNERS			
Please classify the following services according to their contribution to your revenue:			
TYPE OF PRIMARY SERVICE SOLD BY PARTNERS	% of partners	Small	Med/Large
APPLICATION DEVELOPMENT	54%	61%	56%
PROFESSIONAL SERVICES (SUCH AS CONSULTING)	54%	54%	53%
SYSTEMS/SOFTWARE INTEGRATION	31%	22%	33%
SOFTWARE CUSTOMIZATION	25%	21%	28%
WEB SITE DESIGN/MAINTENANCE	16%	22%	14%
SOFTWARE SUPPORT/MAINTENANCE	8%	11%	8%
TRAINING AND EDUCATION	7%	9%	5%
SERVICES PROVISION (SUCH AS ISP, ASP, XSP & WEB HOSTING)	3%	2%	3%
OTHER	4%	2%	6%

Base: 451
 Source: Reality Research & Consulting

IBM Business Partner Profitability

Collaboration, Knowledge Management, eCommerce, Content Management, CRM and Website Management are the key technology areas that IBM Middleware Partners are focusing on today (see *Figure 8*). Larger organizations are more likely to have a broader technology focus with Business Intelligence, Vertical Market Solutions, SCM, ERP and eLearning also playing a large role.

Figure 8

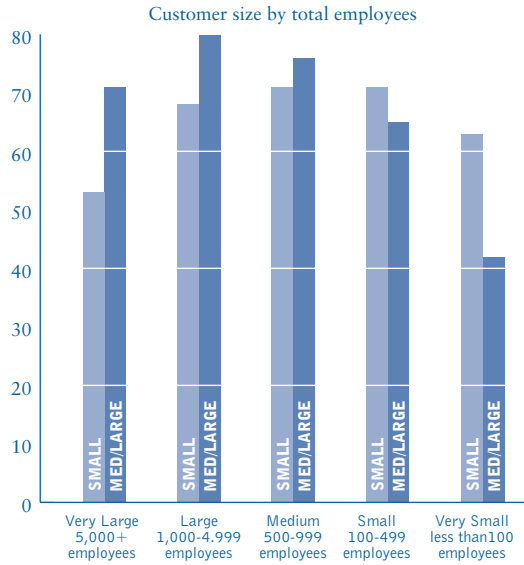
PARTNER TECHNOLOGY FOCUS			
Does your company specialize in any of the following:			
TYPES OF TECHNOLOGY SOLUTION	% of partners	Small	Med/Large
COLLABORATION	74%	81%	73%
E-COMMERCE	65%	59%	68%
KNOWLEDGE MANAGEMENT	64%	70%	63%
CONTENT MANAGEMENT (EASY ACCESS TO CENTRALIZED ELECTRONIC)	63%	65%	65%
CUSTOMER RELATIONSHIP MANGEMENT (CRM)	56%	57%	57%
WEBSITE MANGEMENT	55%	54%	55%
BUSINESS INTELLIGENCE	47%	38%	50%
VERTICAL MARKET SOLUTIONS	40%	27%	44%
SUPPLY CHAIN MANAGEMENT (SCM)	28%	17%	32%
ENTERPRISE RESOURCE PLANNING (ERP) (SOFTWARE)	27%	21%	32%
E-LEARNING	25%	23%	26%
OTHER	20%	10%	23%
NO SPECIALTY	3%	2%	4%

Base: 514
Source: Reality Research & Consulting

4 Customer Profiles

The large customer segment (1,000 to 4,999 employees) receives the most attention from business partners with more than three-quarters of the total base selling to this segment. This large customer segment is served by four out of five medium and large partner organizations (\$1 million or more in annual revenue), but more than two-thirds of small partners (less than \$1 million in annual revenue) also sell into this segment. This implies that the size of the business partner does not inhibit sales to large customers, providing that the business partner can demonstrate a core competency (see Figure 9)

Figure 9
▶ CUSTOMER SEGMENTS SERVED



Base: 514
Source: Reality Research & Consulting

5 Business Partner Profitability

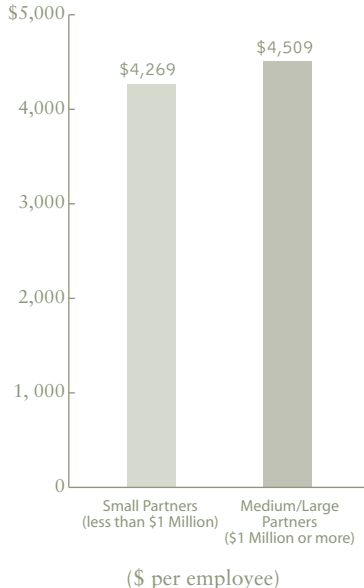
The impact of IBM middleware on business partner profitability is important to examine because on average, IBM middleware represents 69 percent of business partner software-related revenue. This includes software products and services. **The average gross profit margin on IBM middleware business reported by partners is 24 percent, with an even larger gross profit margin on services of 33 percent.**

Gross profit margins, however, are just one measurement of business partner success. An equally valuable perspective is gained by examining profit per employee. Figure 10 shows that medium and large business partners (\$1 million or more in annual revenue) are achieving the most profitable returns on a per-employee basis at \$4,509 on customer engagements built on IBM middleware. This demonstrates a high level of productivity. Small business partners (less than \$1 million in revenue) are not far behind, reporting a per-employee profitability of \$4,269 on customer engagements built on IBM middleware.

The average gross profit margin on IBM middleware business reported by partners is 24 percent, with an even larger gross profit margin on services of 33 percent.

Figure 10

▶ PROFIT DOLLARS PER EMPLOYEE ON IBM MIDDLEWARE ENGAGEMENTS

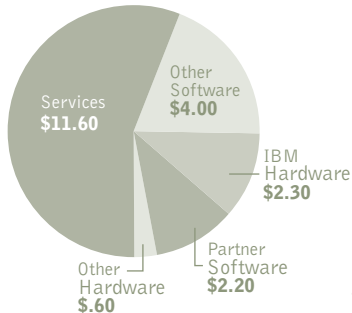


Source: Reality Research & Consulting

Figure 11

IBM MIDDLEWARE SALES MULTIPLIER FOR PARTNERS

For every dollar a customer spends on IBM middleware, how many dollars of other related software, hardware and services are sold?



North American Data
Source: Reality Research & Consulting

6 IBM Middleware Sales Multiplier for Business Partners

Business partners were asked to calculate how much additional revenue was generated by each dollar a customer spends on IBM middleware. Specifically, business partners were asked to calculate the revenue generated for their own software, other companies' software, IBM hardware, other companies' hardware and their own companies' services.

Business partners calculated that for every dollar a customer spends on IBM middleware, an additional \$21 is spent by that customer on related software, hardware and services² (Figure 11). Sales of services account for more than half of this additional \$21. This is consistent with the finding that services account for an average 62 percent of all business partner revenue. Moreover, considering that average gross profit margins for business partners on IBM middleware-related services are 33 percent, this "sales multiplier" for services is also driving partner profitability.

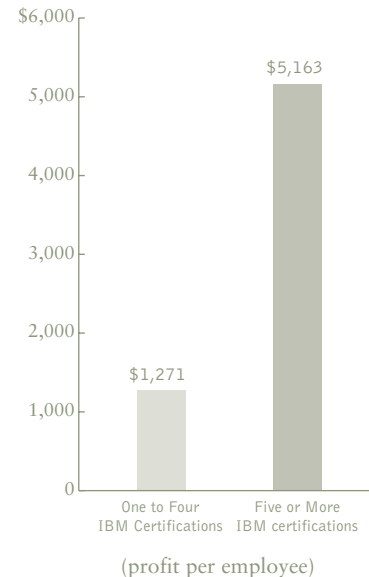
7 Impact of IBM Education & Training

For every dollar invested in IBM software-related education, training and certification, business partners generate \$345 in software and services revenue resulting from their IBM practice. Business partners in North America, on a median basis, invest \$5,000 (per company) annually in IBM software-related education, training and certification. In return, business partners, on a median basis, generated \$1.73 million in IBM-related software and services revenue last year.

Additionally, organizations with more certifications also report higher profitability. On an average basis, organizations with five or more IBM certifications report \$5,163 in profit per employee based on customer engagements built on IBM middleware. For organizations with four or fewer IBM certifications, the per-employee profit is \$1,271 per employee (Figure 12).

Figure 12

THE IMPACT OF CERTIFICATIONS ON PROFITABILITY



Source: Reality Research & Consulting

On an average basis, organizations with five or more IBM certifications report \$5,163 in profit per employee based on customer engagements built on IBM middleware.

² NORTH AMERICA. THE SALES MULTIPLIER IS \$13 FOR IBM BUSINESS PARTNERS IN EUROPE.

8 Sales Cycle Acceleration

One of the factors behind a successful business partner organization is the ability to accelerate sales cycles. This is especially important when it comes to adopting and selling new technologies. To measure this, IBM business partners were asked to specify the length of time required to sell their companies' first and second \$100,000 of IBM middleware-based products and services into a single new account (see Figure 13).

Findings indicate that sales cycles may be linked to the number of IBM-related certifications. Selling the first \$100,000 in IBM middleware products and services into a single new account comes sooner for business partner organizations that have five or more employees who are IBM-certified. **On average, business partners with five or more IBM-certified employees sell their first \$100,000 in IBM middleware products and services into a single account in less than seven months. That's nearly two months sooner than partner organizations that have four or fewer IBM-certified employees.**

A similar relationship between the number of IBM-related certifications and sales cycles occurs in the sale of the second \$100,000 in IBM middleware products and services into a single account. Business partners with five or more IBM-certified employees sell their second \$100,000 in an average 7.3 months. Again, that is nearly two months sooner than partner organizations that have four or fewer IBM-certified employees.

Cross-selling/influencing three or more IBM middleware brands (DB2, Lotus, Tivoli, WebSphere) also accelerates sales cycles. Selling the first \$100,000 of IBM-related products and services into a single account occurs one month sooner for business partner organizations that sell/influence three or more IBM middleware brands versus only one IBM brand (8.4 versus 7.2 months). Selling/influencing the second \$100,000 of IBM-related product and service revenue comes another two months sooner (9.5 versus 7.7 months). **Therefore, organizations selling/influencing 3 or more IBM brands have increased the speed of their sales cycles by 3 months for the first \$200,000 (17.9 versus 14.9 months) of IBM-related product and service revenue over organizations focusing on only one IBM brand.**

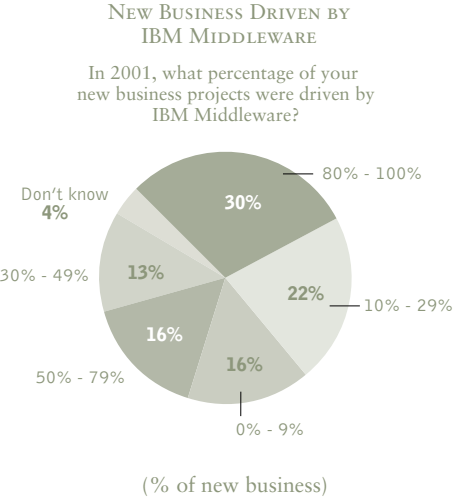
Figure 13

SALES CYCLE FOR FIRST & SECOND \$100,000 OF IBM MIDDLEWARE				
\$ amount of IBM middleware-based revenue	Partners selling only 1 IBM brand	Partners selling 3 to 4 IBM brands	Partners with <5 IBM-certified employees	Partners with 5+ IBM-certified employees
FIRST \$100,000 SOLD	8.4 months	7.2 months	8.5 months	6.6 months
SECOND \$100,000 SOLD	9.5 months	7.7 months	9.0 months	7.3 months
FIRST \$200,000 IN TOTAL	17.9 months	14.9 months	17.5 months	13.9 months

Base: 514
Source: Reality Research & Consulting

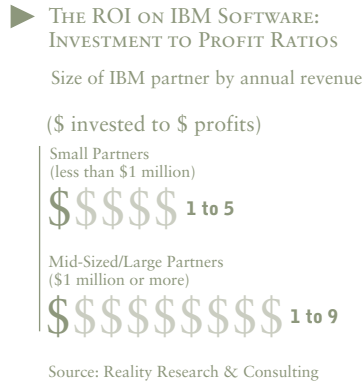
On average, IBM business partners report that nearly half (48 percent) of their new business projects in 2001 were driven by IBM middleware (Figure 14). At the top of Figure 14, note that 30 percent of business partners report 80 to 100 percent of their new business projects in 2001 were driven by IBM middleware. Small partners (less than \$1 million in annual revenue) uncover an even larger proportion of new business projects because of IBM middleware (67 percent).

Figure 14



Base: 514
Source: Reality Research & Consulting

Figure 15



9 Business Partner ROI on IBM Software

As discussed earlier, one of the factors for business partner success is to develop selective vendor relationships based on mutual business-building. An important method to assess whether a vendor relationship is helping to build a partner's business is to measure the return on investment. The data from this survey clearly suggest that IBM, in fact, delivers an excellent return on investment to its partners.

IBM business partners were asked to calculate how much money they invested annually in being an IBM business partner. The investments business partners made were broken out in the following categories:

- ▶ IBM Value Package
- ▶ Overhead costs such as office space, networking and systems
- ▶ Indirect sales channels
- ▶ Education, training, and certification testing
- ▶ Marketing support and co-marketing
- ▶ IBM-related personnel payroll costs
- ▶ Other

On average, business partners calculated that they invested \$179,000 annually to run their companies' IBM software-related business. The average annual profit related to this IBM software investment is \$1.678 million. **That means for every \$1 invested annually in running your IBM software business, the average return in profits is \$9.** Figure 15 segments this investment-to-profit ratio by size of partner business.

10 Conclusions

- ▶ IBM provides an excellent return on your overall investment. IBM business partners, on average, report a 9 to 1 ratio of profit dollars to investment dollars.
- ▶ IBM provides a 21X sales multiple. For every dollar a customer spends on IBM middleware, an additional \$21 is spent by that customer on related software, hardware and services³.
- ▶ IBM middleware drives highly profitable services revenue. IBM business partners report that every dollar in sales of IBM middleware generates nearly \$12 in sales of their own companies' services³. And this services revenue generates a 33% profit margin.
- ▶ IBM provides an excellent return on investment for your education and training dollars which will also improve your overall business results (revenues, profits and sales cycles). The ROI of IBM Certifications: \$1 in training yields \$345 in revenue. More certifications yield higher overall revenues and profits for your business. Increasing the number of IBM-certified employees can also speed-up your sales-cycles.
- ▶ Increasing the number of IBM brands sold/influenced (DB2, Lotus, Tivoli, and WebSphere) can also positively impact your bottom line. Selling/influencing more than one of IBM's middleware brands will yield you higher revenues, greater profits and faster sales cycles.

³ NORTH AMERICA. FOR IBM BUSINESS PARTNERS IN EUROPE, IBM MIDDLEWARE GENERATES \$5 IN SALES OF THEIR OWN COMPANIES' SERVICES.



Notes

Contact Information

Nancy Lawler
Sr. Manager, Software Group Market Intelligence
IBM Software Division
Phone: 914-766-1256
E-Mail: nlawler@us.ibm.com

Eve Gelbein-Zuber
Manager, Business Partner/Channels Market Intelligence
IBM Software Division
Phone: 919-543-0360
E-Mail: zubereve@us.ibm.com