

Bulletin

Worldwide Integration Server Software Platform Forecast and Analysis, 2002–2006

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IDC Opinion

How did integration server software platform (ISSP) vendors perform in 2001, and what characteristics will vendors need to be successful in the future?

Integration took center stage in 2001, as corporate IT managers declared achieving the elusive “integrated enterprise” to be their primary goal. While this focus on integration helped generate healthy gains for ISSP vendors, it did not result in what could be called phenomenal gains, given that some software markets have been known to more than double in the year that they take center stage. The ISSP vendors’ more limited growth rates in 2001 can be attributed to the cost and complexity of implementing their products, the economic downturn, and 9/11, which dampened customers’ willingness to undertake enterprisewide projects, and the relative maturity of the market when it was “discovered” by the mainstream. IDC expects these opposing forces of need balanced by challenges to generate healthy yet moderate growth for ISSP vendors during the forecast period.

In This Bulletin

Synopsis

This IDC bulletin examines the integration server software platform (ISSP) market and leading vendor performance and profiles for 2001 through 2006.

The study will address the effect that the economic downturn and the events of September 11 had on the ISSP market, and how vendors in this market have responded to the focus on integration that emerged in the market in 2001.

This study will help readers understand what trends are affecting the ISSP market, what strategies are most successful in addressing current prospective customers for ISSP products, and how trends — including standards-based integration and Web services — will affect this market moving forward.

The vendor shares and competitive analysis contained here update those found in *Businessware Management Systems Forecast and Analysis, 2001–2005* (IDC #24890, June 2001). The forecasts presented here update those published in *Worldwide Integration Server Software Platforms Forecast, 2002–2006* (IDC #26712, April 2002).

Methodology

IDC's industry analysts have been measuring and forecasting IT markets for more than 30 years. IDC's software industry analysts have been delivering analysis and prognostications for packaged software markets for more than 25 years.

The actual strategy incorporates information from four different but interrelated sources, as follows:

- **IDC's Software Census interviews:** IDC interviews all significant market participants to determine product revenue, revenue demographics, pricing, and other relevant information.
- **Product briefings, press releases, and other publicly available information:** IDC's software analysts meet with hundreds of software vendors each year. These briefings provide an opportunity to review current and future product strategies, revenue, shipments, customer bases, target markets, and other key product information.

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- **Vendor financial statements and related filings:** Although many software vendors are privately held and choose to limit financial disclosures, information from publicly held companies provides a significant benchmark for assessing informal market estimates from private companies. IDC maintains an extensive library of financial and corporate information focused on the IT industry. We further maintain detailed revenue by product area models on more than 1,100 worldwide vendors.
- **IDC's demand-side research:** This includes thousands of interviews annually and provides a powerful fourth perspective for assessing competitive performance. IDC's user strategy databases offer a compelling and consistent time-series view of industry trends and developments. Direct conversations with technology buyers provide an invaluable complement to the broader survey-based results.

Ultimately, the data presented herein represents IDC's best estimates based on the above data sources as well as reported and observed activity by vendor and further modeling of data that we believe to be true to fill in any information gaps.

In addition, please note the following:

- The information contained in this bulletin was derived from the IDC Software Market database as of May 2002.
- *All numbers in this document may not be exact due to rounding.*
- For more information on IDC's software definitions, see *IDC's Software Taxonomy, 2002* (IDC #26508, February 2002).

Please refer to the appendix for additional vendor and market-specific methodology.

Market Definition

Integration server software platforms provide a centralized infrastructure for application integration and business process automation. While integration server software platforms often leverage point-to-point middleware, in order to be included in this market, products must provide the facility to perform one or more of the following tasks:

- Significantly transform the content of messages beyond what is needed to translate between message formats, potentially based on business rules
- Respond to queries based on business logic and/or rules that are specific to the context in which the software is being used
- Integrate multiple custom and/or third-party applications into a "meta" application and/or an automated business process

These products are different from component-based deployment products such as application server software platforms in that they are primarily concerned with integrating existing standalone

applications and providing a deployment platform for implementing “meta” applications and/or business processes.

Situation Overview

Integration Server Software Platform Market in 2001

Despite the relative lack of change in the composition of the market's competitive landscape in 2001, the ISSP market was affected by dramatic changes last year. Like all markets, the economic downturn and 9/11 affected the market's ability to grow. As a result, ISSP market revenue grew by 24.8% from 2000 to 2001, increasing from \$1.51 billion to \$1.89 billion (see Table 1). Enterprise customers shifted away from enterprisewide integration projects, focusing instead on tactical integration projects that tended to decrease vendors' average revenue generated from each project. The ISSP market was also harder hit than other application development and deployment markets by the economic downturn because of the relatively high price per CPU of ISSP products. (Informally, IDC estimates that the average integration server from leading enterprise application integration [EAI] vendors sells for \$150,000 to \$250,000 per CPU.)

Toward the end of the year, the market began to recognize, along with the software industry as a whole, that integration was the primary problem that newly emerging Web services standards such as Simple Object Access Protocol (SOAP) could be used to solve. The concept of “standards-based integration” began to be used, the idea being that Web services could eliminate the need for costly, proprietary adapters for connecting applications to the integration server. Given that many enterprise application integration (EAI) vendors price a single adapter at half the cost of the integration server itself, this presents an opportunity for enormous cost savings on the part of customers and a gigantic threat to the business models of major EAI vendors.

In response, the vendors scrambled to position themselves and their products relative to Web services. Some embraced Web services from the start, while others cycled through several stages of denial before finally embracing the new standards. Almost all existing EAI vendors emphasized the fact that Web services standards themselves do not solve all of the problems of integration and that integration servers as well as proprietary adapters would be necessary for the foreseeable future. One of the most important outstanding questions in the industry today is how quickly enterprises will insist that EAI vendors lower the cost of adapters as a result of the promise of Web services. (Note that fully functional replacements for proprietary adapters don't have to be available for this price pressure to be exerted.)

Table 1
Worldwide Integration Server Software Platform Software Revenue by Vendor, 1999–2001 (\$M)

	1999	2000	2001	2001 Share (%)	2000–2001 Growth (%)
IBM	82.0	193.0	237.0	12.5	22.8
TIBCO	76.1	214.5	231.7	12.3	8.0
webMethods	27.4	132.8	169.7	9.0	27.8
SeeBeyond	31.1	79.1	135.9	7.2	71.8
Vitria Technology	24.0	101.3	104.5	5.5	3.1
Mercator Software	62.8	118.1	94.5	5.0	-20.0
Iona	28.8	52.0	77.0	4.1	48.2
Viewlocity	58.5	62.0	60.0	3.2	-3.2
Oracle	–	–	58.9	3.1	NA
Sybase	71.0	117.0	52.8	2.8	-54.8
CrossWorlds Software	9.9	27.3	43.0	2.3	57.5
GE Global eXchange Services	31.6	37.1	41.3	2.2	11.1
Microsoft	–	–	36.7	1.9	NA
BEA Systems	–	–	34.4	1.8	NA
Actional	10.0	21.3	28.0	1.5	31.8
Quovadx	15.8	22.4	23.0	1.2	2.5
SunGard Data Systems	20.0	22.0	22.0	1.2	0.0
Software AG	–	–	18.7	1.0	NA
Information Builders	–	–	16.5	0.9	NA
Netik	9.0	12.0	13.2	0.7	9.6
iE	4.0	12.0	12.0	0.6	0.0
Sun Microsystems	5.0	5.9	12.0	0.6	102.2
Enterworks	8.5	10.1	11.6	0.6	14.9
Peregrine Systems	18.5	33.0	10.0	0.5	-69.7
IntelliCorp	5.3	9.0	8.9	0.5	-0.7
Optio Software	3.0	6.1	7.2	0.4	18.0
Connexive	3.5	5.1	6.0	0.3	17.7
Fuego	2.9	4.6	6.0	0.3	30.4
Computer Associates Intl.	–	–	4.0	0.2	NA
Level 8 Systems	24.0	24.8	3.4	0.2	-86.3
Attunity	0.8	3.0	2.5	0.1	-16.9
Gresham Computing	1.4	2.4	2.4	0.1	0.9
Bremer Associates	0.7	2.0	2.3	0.1	16.2
Handysoft	–	–	1.7	0.1	NA
Metaserver	0.8	0.9	1.1	0.1	22.2
Subtotal	636.2	1,330.8	1,590.0	84.1	19.5
Other	76.0	183.2	299.7	15.9	63.6
Total	712.2	1,514.0	1,889.8	100.0	24.8

Source: IDC, 2002

Some vendors focused their products squarely at this emerging space, including Actional, BEA, Iona, Microsoft, and SilverStream, to name a few. Some of these vendors focused on Java-based standards, including Java Messaging Service (JMS) and Java Connector Architecture (JCA), as a way to standardize the entire integration stack. Others focused on implementing integration based on Web services standards alone. In any case, all of these vendors are offering their products that cost an order of magnitude less than traditional EAI offerings. Initial reception among customers for these products looks good, but it remains to be seen if they can replace the high-end systems at Fortune 500 companies on which the EAI vendors have built their businesses.

New competitive threats emerged from the top of the software stack as well. Packaged application vendors, most notably SAP, began to announce integration offerings as part of their solutions. These offerings were usually positioned as targeted toward existing users of the company's software, but nevertheless represent a potential loss of opportunity for ISSP vendors. Furthermore, a number of packaged application vendors began to approach the emerging segment of business process automation, which is also being looked at by ISSP vendors as a growth area.

For their part, some ISSP vendors, most notably Vitria, began to assemble what they called "collaborative applications" based on their integration platforms. These offerings are intended to provide out-of-the-box solutions for specific application needs, usually targeted at a problem faced by a specific vertical industry that is particularly in need of integration functionality. One example is the Health Insurance Portability and Accountability Act of 1996 (HIPAA), which requires health insurance providers to standardize the format of electronic data to enable more efficient processing of insurance claims. This is an industry-specific problem that requires extensive integration functionality to solve, and a number of ISSP vendors have created offerings specifically targeted at this market.

The question arising from the trends noted above is whether integration will increasingly become an embedded component in applications or whether it will remain a separate enabling infrastructure within the enterprise. As long as the current economic situation remains, IDC believes that ISSP vendors will have to look toward providing solutions to more tactical, application-specific problems in order to generate revenue.

Performance of Leading Vendors in 2001

IBM

IBM and TIBCO continued their horse race in the ISSP market in 2001. After losing the top slot to TIBCO in 2000, IBM regained it in 2001, edging out its closest competitor by just over \$5 million. Last year, IBM engaged in a series of preparatory moves in anticipation of its big push into the integration market, which is underway as this document is being published. Big Blue's moves in 2001 consisted of

consolidating its integration products under the WebSphere brand name, thereby adding weight to the convergence of application server and integration server that IDC has identified.

IBM was also one of the few vendors in 2001 to undertake an acquisition, a move IDC expected to see from other EAI vendors but which didn't come to pass. IBM's acquisition of CrossWorlds (which wasn't completed until January 2002) was primarily made for the sake of the company's adapters and its work in business process automation, particularly straight-through processing.

TIBCO

TIBCO's license revenue actually grew 19.4% last year, but much of that growth came from the company's new portal product. As a result, TIBCO's revenue growth (license and maintenance) in the integration server market grew only 8%.

Throughout the year, TIBCO worked to add offerings to its portfolio that support prevailing standards such as J2EE (which it licensed from Sun in October) and Web services (with the release of its BusinessWorks product in December).

TIBCO was also one of the only EAI vendors to complete an acquisition in 2001, buying real-time data delivery vendor Talarian in April.

webMethods

Although webMethods generated healthy revenue growth in 2001, the company is struggling to cope with the prevailing trends in the integration server market, which tend to run counter to webMethods' long-standing strategy of providing enterprise integration platforms to the world's largest companies.

During the second half of the year, the company slowly came around to the fact that Web services, and therefore standards-based integration, are here to stay. The company now positions itself as an enabler of Web services technology, arguing that existing Web services standards are insufficient to securely and robustly integrate enterprise systems. While IDC agrees with this viewpoint, the question remains whether webMethods and other companies taking a similar approach will be able to maintain their price point as less expensive alternatives become available.

SeeBeyond

SeeBeyond spent much of 2001 struggling to shore up its foundering financial position. It began in October by naming former Oracle president and COO Ray Lane as chairman of the board. Lane has been instrumental in rehabilitating SeeBeyond's tarnished image. The company then raised \$15 million in December in private equity and an additional \$82 million from a sale of public stock in February. As of the company's first quarter earnings report, SeeBeyond had more than \$100 million in cash, quelling customers' fears that the company could go bankrupt.

Despite these challenges, SeeBeyond managed to grow its market share by two points, from 5.2% to 7.2% of the market, posting the highest growth rate of any of the top 10 vendors. The company added 47 new customers in the fourth quarter alone, including several in manufacturing, and generated 30% of its 2001 revenue from repeat customers. The company attributed its success to strong partnerships, which influence the majority of the company's sales, and its distributed architecture.

Vitria

Like many of the other EAI vendors, Vitria struggled to change course in 2001 as economic and technological changes swept through the ISSP market. Throughout the year, the company focused on shifting its focus from the telecommunications market, where it had generated a substantial portion of its sales in past years, to a more diverse set of customers, particularly focusing on healthcare, financial services, energy and utilities, and manufacturing. By the end of the year, Vitria's revenue was somewhat more evenly distributed, with the new verticals generating between 10% and 20% each of the company's revenue.

In the fourth quarter, the company announced a new set of products, called "collaborative applications," that are built on top of the company's BusinessWare integration server. These new offerings are intended to provide out-of-the-box integration for specific products, such as achieving a single view of a company's customers or orders.

Other Vendors

Several traditional EAI vendors lost share in 2001; particularly, two companies that came by their EAI products through acquisitions: Sybase (which acquired New Era of Networks), and Peregrine (which acquired Extricity). Mercator also lost share, although the company began to stage a recovery toward the end of the year.

The year also saw several dominant vendors in other markets enter the ISSP space, including Oracle, Microsoft, and BEA. These "platform" vendors, along with IBM, which already has significant presence in this market, promise to change the dynamics of the ISSP space, which was previously dominated primarily by pure-play vendors.

Other vendors also shifted more of their focus to the integration server market, including Computer Associates, Iona, Sun Microsystems, and Software AG.

Consolidation in the market slowed paradoxically, with IBM's acquisition of CrossWorlds representing the only significant merger of existing players.

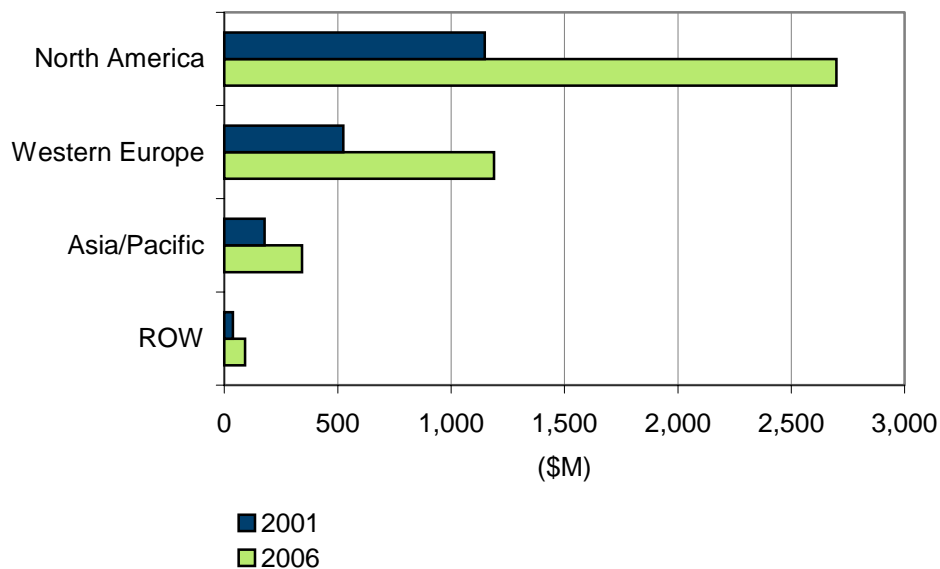
Finally, some vendors began to talk about plans to leave the ISSP market. In particular, Viewlocity is shifting to focus on supply chain enablement solutions, and Peregrine plans to use the technology it acquired from Extricity primarily to provide integration functionality in its other product offerings.

By Geographic Region

North America's share of the worldwide ISSP market fell in 2001 as the economic situation and the aftereffects of 9/11 hit the United States the hardest. Nevertheless, North America retained a 60.8% share, down from 65.5%. Growth in other regions continued, helped by the fact that integration server software adoption was not as widespread in these other regions at the beginning of the year as it was in North America.

As a result, Western Europe saw its share rise from 25% to 27.7%; Asia/Pacific's share rose from 7.4% to 9.4%, and the rest of the world's share remained essentially flat at 2% (see Figure 1).

Figure 1
Worldwide Integration Server Software Platform Revenue by Region, 2001 and 2006

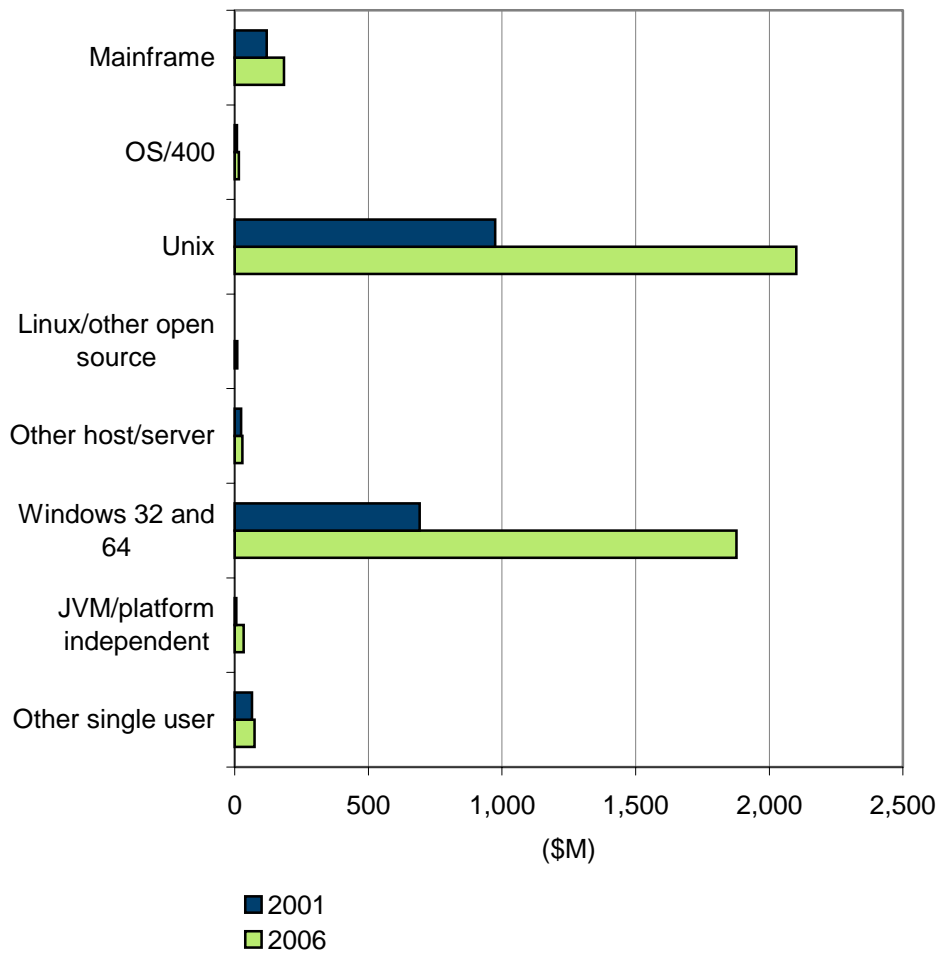


Source: IDC, 2002

By Operating Platform

Unix retained its lead, and even grew a bit to represent 51.6% of the market, reflecting that the leading vendors deploy the majority of their ISSP products on Unix platforms. Windows' share slipped slightly, however, from 37.2% to 36.6%. To some extent this may reflect the increasing use of Java and J2EE-based standards in integration products. Other platforms' shares generally remained flat or slipped slightly. Linux and other open-source platforms made their debut at a miniscule 0.09% of the market, as did JVM-based platforms, with 0.3% market share (see Figure 2).

Figure 2
Worldwide Integration Server Software Platform Revenue by Operating Environment, 2001 and 2006



Source: IDC, 2002

Future Outlook

Vendor Profiles

IBM

Having completed its acquisition of CrossWorlds, IBM announced extensive plans for its integration product line at its DeveloperWorks conference in May. In addition to plans to integrate the CrossWorlds functionality with its MQ Integrator and MQ Workflow products to address business process integration needs, highlights from the announcement included the following:

- A focus on portals as an integration technology
- A lower cost integration server called MQ Event Broker
- An EDI-focused offering called WebSphere Data Interchange

- Industry-specific versions of WebSphere Integrator

On one hand, it may seem that IBM has responded to criticisms that its product line is too complicated by adding more products. On the other hand, IBM has honed the target markets for these products much more sharply than it had with the previous lineup. It should be easier for IBM to target subsets of the enterprise market with these new solutions than it was with the prior offerings.

Given the focus IBM is placing on the entire WebSphere family and the depth of its offering, IDC expects IBM to continue to do extremely well in this market.

TIBCO

Given CEO Vivek Ranadive's presentation at its May Strategic Directions conference, TIBCO seems to be arguing that it can now offer a complete offering to customers thanks to its broader product line — one that addresses “people, processes, and partners.” Ranadive went so far as to refer to the TIBCO offering as a new Internet operating system, a sure sign that a vendor wants to be perceived as a platform player. On one hand, this strategy seems to run counter to customers' reluctance to invest in enterprisewide integration backbones. On the other hand, it may signal that TIBCO wants to compete in a different market altogether, namely the ebusiness platform market, and particularly with IBM's broader WebSphere product offering, rather than focusing specifically on integration offerings.

TIBCO is also working hard to shed its reputation as a company laden with legacy baggage. TIBCO's success in 2002 and 2003 will be largely dependent on its ability to convince reluctant IT managers, many of whom have older TIBCO products in place, to buy into its new strategy.

webMethods

webMethods spent the early part of 2002 focusing its efforts on areas that a number of other vendors had tackled in 2001 — namely, Web services and vertical diversification. With regard to the latter, webMethods announced customer wins and a new advisory board to tackle the government sector, as well as a business unit targeted at the financial services sector.

Despite its newfound interest in Web services, webMethods is sticking to its strategic guns more faithfully than its competitors, and so far the strategy seems to be working, at least relatively speaking. webMethods was the only one of the top 5 pure-play ISSP vendors to generate a sequential revenue increase (albeit small) in the first calendar quarter of 2002. Although it seems unlikely that standards-based integration offerings won't begin to erode webMethods' ability to generate revenue gains in the future without a shift in strategy, it's possible that the company can continue to increase revenue by beating its smaller rivals in sales situations.

SeeBeyond

SeeBeyond is betting its future on the value of its distributed architecture, going so far as to sponsor a research lab to confirm that it is the only integration server software vendor with a truly distributed architecture. SeeBeyond argues that this architecture enables its integration solution to scale more effectively than alternatives.

At the same time, SeeBeyond executives recognize that integration software buying patterns have shifted from strategic, enterprisewide solutions to more tactical, problem-focused solutions, with demand for the solutions to break even in terms of ROI within as little as 90 or 180 days. As a result, the company is working to develop offerings that can target these requirements. It is also focusing on maintaining its high rate of partner-influenced sales, which rose to 73% of license revenue in the first quarter.

Vitria

Vitria's collaborative applications strategy became the company's primary focus in early 2002, representing a certain divergence between itself and the other major EAI vendors, which have not focused as extensively on prepackaged integration solutions.

Vitria is also pushing the concept of a Common Information Model (CIM), which involves the aggregation and synchronization of data from various systems into a reusable component. Vitria uses CIM in its CRM integration offering to synchronize data between packaged applications such as Siebel, Oracle, and SAP.

CIM components can be used in a business process automation solution. As this is where Vitria's strength lies, IDC believes that Vitria will succeed to the degree that it is able to convince customers of the value of business process integration.

Market Characteristics in the Future

Forecast and Assumptions

The ISSP market is expected to achieve a faster growth rate than many other software markets during the forecast period. The compound annual growth rate (CAGR) from 2001 through 2006 is forecast to be 18%, reflecting long-term, healthy demand for products that address enterprise integration needs. The market is expected to more than double to \$4.3 billion by 2006, representing significant opportunities for leading vendors. Year-over-year growth rates are shown in Table 2.

Although performance of the leading vendors has not improved as some had hoped it would in early 2002, we are still forecasting an increase in the growth rate for the year. The growth rate is then expected to decrease slightly in 2003. If the economic situation fails to improve substantially in the second half of 2002, however, some of the growth forecast for 2002 could be pushed into 2003.

Table 2
Worldwide Integration Server Software Platform Software Revenue by Region and Operating Environment, 2000–2006 (\$M)

	2000	2001	2002	2003	2004	2005	2006	2001 Share (%)	2001–2006 CAGR (%)	2006 Share (%)
Geographic region										
North America	991.1	1,149.5	1,466.6	1,756.7	2,069.3	2,384.4	2,700.1	60.8	18.6	62.4
Western Europe	379.1	524.4	670.0	795.3	928.6	1,060.7	1,190.5	27.7	17.8	27.5
Asia/Pacific	112.6	178.1	214.6	239.7	264.3	296.1	343.0	9.4	14.0	7.9
ROW	31.3	37.8	47.7	56.2	66.0	77.4	91.6	2.0	19.4	2.1
Total	1,514.0	1,889.8	2,398.9	2,847.9	3,328.3	3,818.6	4,325.3	100.0	18.0	100.0
Operating environment										
Mainframe	104.1	119.1	131.5	141.0	155.7	170.9	184.1	6.3	9.1	4.3
OS/400	12.0	8.7	10.2	11.6	13.1	14.5	15.9	0.5	12.8	0.4
Unix	749.2	974.4	1,242.6	1,480.1	1,687.7	1,891.8	2,101.9	51.6	16.6	48.6
Linux/other open source	–	1.7	2.7	3.9	5.5	7.3	9.5	0.1	41.1	0.2
Other host/server	22.0	23.6	26.2	26.5	27.1	28.1	28.7	1.2	4.0	0.7
Windows 32 and 64	563.4	691.2	907.9	1,103.1	1,350.5	1,607.5	1,877.1	36.6	22.1	43.4
JVM/platform independent	–	6.4	8.4	11.5	17.2	24.9	33.8	0.3	39.5	0.8
Mobile and embedded	–	–	–	–	–	–	–	–	NA	–
Other single user	63.3	64.7	69.3	70.1	71.6	73.6	74.3	3.4	2.8	1.7
Total	1,514.0	1,889.8	2,398.9	2,847.9	3,328.3	3,818.6	4,325.3	100.0	18.0	100.0
Growth (%)	NA	24.8	26.9	18.7	16.9	14.7	13.3			

Source: IDC, 2002

Subsequent years show a sequential decline in growth rates. By the end of the forecast period, the growth rate is expected to drop slightly below the historic software industry average, reflecting the maturity of the market at that time.

By Geographic Region

Regional shares of the ISSP market will remain steady during the forecast period, reflecting somewhat equal growth worldwide. After extremely strong growth between 2000 and 2001, Asia/Pacific's share will decrease slightly to 7.9% by 2006, while North America's share will rise slightly to 62.4%. Shares represented by Western Europe and the rest of the world will remain substantially flat. In general, this trend reflects the more mature use of technology in the United States and the subsequent greater need for integration in the short and medium term. It is hoped that by the end of the forecast period, companies still ramping up their use of information technology will take integration needs into account during initial deployment,

thereby decreasing the need for expensive post-production integration projects.

By Operating Platform

Trends in terms of operating platforms will remain consistent through the forecast period. Linux and platform-independent platforms will increase their shares of the ISSP market, while most other smaller markets decrease slowly. Unix will lose ground, decreasing from 51.6% to 48.6% by 2006. Windows share of the market will increase slightly, from 36.6% to 43.4%. To some extent, this may reflect Microsoft's increasing attention to integration, both through BizTalk and the .NET Framework.

Forecast Assumptions

- The economic rebound has already begun, with the IT rebound to follow soon.
- The recovery in IT spending during 2002 will be gradual and will vary by specific market segment and geography.
- There will be no more major terrorist attacks in the United States.

A change in these assumptions could significantly affect the forecast presented in this study.

Revenue Growth Enhancers

The following factors will tend to support continued positive growth in the ISSP market:

- Increasing interest in deploying Web services could drive integration server software sales.
- IT managers consistently express the need to integrate their companies' infrastructures. This need should drive continued interest in ISSP products, although this interest may remain tactical during the economic downturn.
- Some application vendors, most notably Siebel, are seeking to include integration servers inside their application offerings. This should provide ISSP vendors with opportunities for OEM sales, although these sales could generate price pressure if the integration server begins to be perceived as enabling technology.
- ISSP vendors are also building complete software solution bundles, in conjunction with partners, which are designed to target particular vertical industries and horizontal applications. These bundles will be attractive to companies with smaller IT departments and could expand the deployment of integration server software.

Revenue Growth Inhibitors

The following factors will tend to inhibit growth in the ISSP market:

- The advent of standards-based integration offerings could generate significant price pressure on traditional EAI vendors.
- The continuing economic downturn will continue to depress IT spending budgets through at least 2002. This is likely to limit deployment of enterprisewide integration backbones for at least 12 to 18 months.
- The complexity of integration continues to suppress adoption rates. Failure on the part of ISSP vendors to address this issue could have a negative impact on market growth in the years ahead.

Essential Guidance

To compete successfully in the ISSP market, vendors must address the following issues.

Services-Based Integration

After more than a year of hype, the industry has settled on integration as the primary purpose for Web services, at least for the foreseeable future. ISSP vendors must recognize that, particularly given the economic downturn, IT managers are going to be very attracted to standards-based integration solutions that cost a fraction of the price of traditional EAI platforms.

As a result, ISSP vendors are going to have to improve their ability to demonstrate concrete ROI for integration projects, not only in terms of technological benefits, but also in terms of business benefits, such as productivity, labor costs, business efficiency, and improved customer service. In the end, however, vendors may need to look forward to a time when they cannot demand millions of dollars for an enterprisewide integration platform, and revamp their business plans accordingly.

Competition from Platform Vendors

While the leading EAI vendors are well known in certain circles, their mindshare in the broader market pales in comparison to behemoths such as IBM and Microsoft. As these larger platform vendors turn their attention to integration, ISSP vendors will have to find ways to raise their profiles. One important way to do this will be to partner with leading packaged application vendors and with system integrators.

Business Process Automation

IDC believes that the future of integration technology lies on the route to business process automation. Rather than focusing on the systems that need to be integrated, business process automation takes a top-down approach to integration, examining business processes and then figuring out which systems are needed to automate these processes.

Not only can business process automation provide a way for ISSP vendors to demonstrate ROI, but it can also catapult vendors into a new arena: that of composite or tailored applications. IT managers and packaged application vendors are realizing that packaged applications are well suited for automating commoditized business processes, but less well suited for automating processes that are strategic or specific to the business. On the other hand, many companies are loath to invest the time and money it takes to build fully custom applications. The compromise lies in composite or tailored applications, which build customized code that leverages existing systems to perform a majority of the fundamental tasks in the business process. While it may be some time before this concept achieves mainstream adoption, integration server software vendors would be well served to begin positioning themselves to play in this redefined market in the near future.

Learn More

Related Research

- *Enterprise Integration Trends* (IDC #27146, May 2002)
- *Worldwide Application Integration Software Forecast Summary, 2002–2006* (IDC #27149, May 2002)
- *Worldwide Application Development and Deployment Forecast Summary, 2002–2006* (IDC #26882, April 2002)
- *Worldwide Integration Server Software Platforms Forecast, 2002–2006* (IDC #26712, March 2002)
- *Web Services: A Context for 2002* (IDC #26375, January 2002)

Appendix: The Treatment of Computer Associates' Revenue and Its Effect on Market Data

Change in Accounting Method

Near the end of calendar year 2000, Computer Associates Inc. (NYSE:CA) changed its method of recognizing and reporting software revenue.

Under the old method, the company recorded the total value of the booking of a new or renewed long-term software “right-to-use” contract by amortizing the part associated with software maintenance over the life of the contract and then recognizing the remainder as immediate revenue. (For one-time sales, such as are typical for many client/server products that were sold through channels of distribution, all revenue was recognized immediately.)

This method not only permitted, but required, the immediate recognition of some portion of the long-term contract revenue. As the company stated in published explanations of the shift:

“Accounting rules such as detailed in AICPA Statement of Position (“SOP”) 97-2 (as amended by SOP 98-4 and SOP 98-9), (define) the criteria for recognizing revenue. To the extent that

maintenance fees are “bundled” together with license revenue, the maintenance fee must be “unbundled” and recognized over the life of the contract period. Consistent with the aforementioned guidance, one must have vendor specific objective evidence (“VSOE”) to determine the value of maintenance contained within a bundled license and maintenance contract. This determination is neither arbitrary nor “discretionary.” Based upon the VSOE established for maintenance, a fixed percentage of bundled contracts is deferred.”

In other words, the treatment depended significantly on the wording of the contract.

Starting late in calendar year 2000, CA introduced its “new business model,” which substantially changed the accounting method by which revenue is recognized. Under the “new business model” approach to revenue recognition, CA accounts for contracted revenue in a prorated manner over the life of the license term, thereby deferring recognition of some revenue. This is in sharp contrast to the previous method of recognizing all of the nonmaintenance software license revenue immediately upon the signing of a contract. In terms of overall revenue impact, deferred revenue accumulates over time, as more “new business model” contracts are signed, although if sales are at a constant rate the “inflow” of new deferred revenue eventually matches the “outflow” of recognized revenue.

It is important to point out that, while the new business model has caused CA to change the way the company recognizes revenue, it does not necessarily change the company’s overall cash generated from operations. The company has also had a practice of reporting some results as if they were using the old recognition method as a basis for comparison.

The Effect of the Change in Accounting Method

Under the new method that started with the last calendar quarter of 2000 (CA’s third quarter of FY01), CA has been reporting revenue on what it calls a “ratable basis,” while deferring to future quarters the Residual Value of the committed contractual amounts. Residual Value (also called deferred revenue) has thus translated into revenue in future quarters until the end of the contract period. This resulted initially in a considerable reduction in recorded revenue (a drop of well over 50% in the first quarter in which this was done). For example, in April 2001, CA reported that it recognized about \$732 million in revenue in its last fiscal quarter of FY01, while at the same time holding more than \$1.3 billion in Residual Value that was also committed for this quarter but not reported as revenue. Under the old reporting method, this would have been recorded as somewhere in the region of \$1.44 billion of immediate revenue, so the quarter’s results were cut in half. But, as CA continues to build this Residual Value pool, reported revenue will presumably ramp back up. By the time two years have gone by, the effect will be fairly neutral, except that the quarter-by-quarter results will tend to be more predictable and will have far less seasonality (that is, no end-of-year sales bump).

The Effect on Calendar 2000 Results

The effects of the above changes were felt only in the last quarter of calendar year 2000, where that quarter's recorded revenue was reduced by about \$500 million. In addition to the effect of CA's difficulties in closing major new contracts (especially in their mainframe business) earlier in the year, this means that CA's recorded revenue was down from calendar year 1999 by about 26%. The new revenue recognition methodology accounted for nearly half of this drop.

The Effect on Calendar 2001 Results

For the last quarter of calendar year 2000 and the four quarters of calendar 2001, the new revenue recognition method continued to create revenue that was substantially below comparable quarters in the previous year when measured the old way (see Table A1).

As the net residual value held in reserve increases, the drawdown of this pool will start to add considerable additional revenue each quarter. When that happens, reported revenue will recover.

Table A1
Computer Associates Quarterly Revenue Comparisons, 2000–2001 (\$M)

Quarter Ending	Revenue Using Old Method	Revenue Using New Method	Change Due to Accounting Change (%)	New Deferred Revenue for Quarter	Net Residual Value Reserve
December 31, 2000	1,404	783	-44	–	629
March 31, 2001	1,441	733	-49	1,305	1,875
June 30, 2001	1,440	713	-50	502	2,237
September 30, 2001	1,442	734	-49	466	2,535
December 31, 2001	1,452	749	-48	554	2,850

Source: Computer Associates, 2002

The Effect on the Market Data

This change in accounting treatment would have the same effect on any software vendor (and BMC Software has moved toward a similar treatment), but as CA is a strong force (and in some cases has been a market leader) in many software markets, the impact of this accounting change has been to reduce the market revenue reported by IDC in calendar 2001 by an amount that will sometimes be significant. IDC has always tracked vendor revenue in such a way as to match the publicly stated revenue of the software vendors (where available). For this reason, IDC's market figures in some markets show a decline from 1999 to 2001 and a projected decline or reduced growth in many markets that is largely the result of CA's new method of revenue recognition and not truly representative of the market's potential. Conversely, it is quite likely that in the future CA's recognition of previously deferred revenue will tend to increase

growth in some markets and may also positively affect CA's market share and position in some markets.

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