Case studies   School of Marketing and Entrepreneurship

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Iontas.com: Marketing a Software Product

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IONTAS.COM
MARKETING A SOFTWARE PRODUCT[1]

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The year 2001 was a momentous one for most companies in the IT sector with dramatic drops in both profit and market sentiment. Few businesses in the sector were immune to the upheaval. Fortunes had been lost, at least on paper, and many dot.com businesses had folded. While telecoms businesses had been the hardest hit among established concerns, the gloom was widespread.

As he prepared to wind down for the Christmas break, Martin McCreesh, Chief Executive Officer (CEO) of Iontas and its sister company, Iontas Creative Solutions, mused that at least many of the sufferers had seen some days of heady excitement prior to the downturn. He and Iontas had not. Having been established in 2000 and had its software products ready to launch in 2001, Iontas had probably entered the market with the worst possible timing. Companies, which had considered that they had overspent on IT, had slashed budgets, or even prohibited any IT expenditure while they waited to see how business developed in the wake of the downturn and the events of September 11th. Already he and his fellow directors had revised their original strategy fundamentally at least once. Now they were reviewing strategy again, with further changes possible particularly in their approach to their markets. This was his young son's first Christmas and he was looking forward to the break. However, he suspected that much of the period would be spent in transatlantic conference calls with the company chairman and the other directors.

Iontas would have to generate substantial sales in 2002 and/or raise significant new capital. In the early days of the dot.com boom, the level of sales and raising investment were not so closely linked. Now, in a tougher environment, they were.

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[1] This case was developed as a basis for class discussion rather than to illustrate either effective or ineffective handling of a business situation.

THE ORIGINS OF IONTAS

The concept of Iontas was developed by Martin and his current Chairman Joe Stockton back in 1996 when both were employed in Ivron, based in Dublin, which produced both hardware and software video conferencing products. Martin was a programmer with the company and Joe was Chief Operations Manager and also Martin's boss. Both were electronics engineers. In their spare time, the pair began to develop PC monitoring software. This software would enable managers and supervisors to examine the pattern of usage of employees' PCs. There were some relatively simple products on the market, but they were cumbersome to use and typically involved a laborious trawl through records as might be done with a VCR tape, for example.

At that time, in the mid to late nineties it was not clear whether there was a market for such a product. It clearly had immediate "big brother" type connotations. Privacy issues appeared to be a major stumbling block to progress. Joe and Martin continued to work on the project in their spare time, more as a hobby than as a serious business proposition. They kept in contact even after Martin moved to Donegal Town in 1999. He had always intended settling in a smaller community and was offered a position in Viasec, a software development company backed by Eircom, the recently privatised telephone operator and based in Donegal Town. In a trawl for new ideas by Viasec, Martin mentioned the project and the Viasec owners were interested in purchasing the intellectual property (IP) associated with the project.

Martin and Joe were willing to sell but approached a financial advisor, Frank Blayney, for assistance on structuring a deal. Frank suggested that they might consider developing the product themselves and that he was confident that he could raise seed funding from private investors through the business expansion scheme (BES). This scheme allows individuals to invest up to €31,600 in any calendar year in a qualifying business for a minimum of 5 years. A rebate of the investor's marginal tax rate (typically 42%) is immediately available so the net cost to the investor falls to about €18,000. Most BES schemes have an exit mechanism after 5 years. However, in this case, the investors decided to fully opt in as long term

shareholders. Martin and Joe decided to establish a new business with Martin as CEO and Joe as part-time Chairman. Frank Blayney was appointed Chief Financial Officer, again on a part-time basis. The promoters waited until January 2000 to establish the company to avoid any potential problems with the millennium bug.

In fact, two companies were set up, as previously noted. They were Iontas and Iontas Creative Solutions. The two company structure with common shareholders, was chosen for two reasons. It was decided to establish a business to offer services such as web design and other forms of design such as packaging, exhibition material and other visual displays. This would generate cash flow enabling the software development company to recruit additional staff. BES funding was only secured by Iontas. Investors were not entitled to a tax rebate on the full investment as there was a limit of €317,000 which could be raised in this way. However, a total of €500,000 was raised in this round of funding.

Joe Stockton was originally from Moville, a small coastal town in North East Donegal on the Inishowen Peninsula, about 20 miles north of Derry City. A local development committee were keen to see the project established in Moville and provided accommodation in a renovated corn store in the town. While facilities in the town were limited, this was not a concern for Martin. Local broadband services were also limited. Potentially this offered a greater problem. However the demand for broadband was also limited in the area. Martin had calculated that he could probably employ up to 60 engineers/programmers before broadband width became a problem. Of greater concern was the cost of broadband facilities. Eircom was, effectively a monopoly provider and he considered that Iontas was paying over the odds. Otherwise the area was not badly served for infrastructure. Derry and Letterkenny were about 20/25 miles distant. Each had an active 3rd level institute with strong focus on IT, University of Ulster (Magee) in Derry and the Institute of Technology in Letterkenny. The airport in Derry, with connections to Dublin and various airports in England and Scotland, was 25 miles away while the two Belfast Airports were less than two hours drive away.

So in January 2000, the two companies opened their doors and began recruiting. The name selected for the company was Iontas. This is an Irish (Gaelic) word loosely translated as "amazement" or "wonder". Phonetically it is pronounced as *"een-thas"*. However from an early stage it became clear that the name caused pronunciation difficulties outside the immediate geographical area. As a result the pronunciation evolved to be pronounced as a 3-syllable word *"eye-own-thas"*. Iontas Creative Solutions, which had mostly developed a clientele in the north west of Ireland retained the original pronunciation.

Joe Stockton had continued to work full time in Ivron. Later in 2000 it was purchased by a US based company, Gentner Comms. As a shareholder, Joe was required to stay with Gentner for 2 years as part of an earn out agreement. He relocated to Austin, Texas, hence the transatlantic phone conferencing mentioned at the start of the case. This earn out period was due to end in September 2002 after which he would reassess his options. His current position was as Vice President, Business Development with Gentner. In passing, it might be noted that Viasec, Martin's previous employer closed down in 2001 when Eircom refused to provide additional funding and withdrew its support.

THE IONTAS PRODUCT OFFERING

Obviously it took time to develop a working and tested version of the Iontas product offering. Essentially it is a software tool which acts as a PC usage monitoring system.

Appendix 1 illustrates how the product works in practice. The appendix shows a user group report for Iontas' own staff in November 2001. This is normally reproduced in full colour codes on a monitor. Note how little use Martin made of his computer though he makes sure that we are all aware that he has been at his desk later than anybody else! It is possible to check on each element of everybody's use modules. So if a manager wished, for example, to know what Zal was using Internet Explorer for, click on the relevant colour coded bar and it produces a report as illustrated for Sasha in appendix 2. It can also present reports on specific activities. See appendix 3 for an example of this, where the use is games.

The system is web based and is suited to MS based systems. It does not have functionally on Mac, Linux or Unix based systems. It had been estimated that it would take at least 6 man months to adapt the Iontas suite of products to Linux. Unix would take the same. There was some evidence of a possible demand for Linux based products as some large potential customers used it as their operating system. There was no evidence of demand from Mac users. The product is patented in Europe, the Commonwealth and the US. Two separate, though related, products were developed. Agent Focus was specifically developed for call centres. The second product, branded PC Focus, was targeted more broadly at a range of businesses. Both fulfilled the same general purposes.

Essential features are as follows:

- It details desktop application usage and resource access
- It gives file and web access details
- It provides information on log on/off, idle time and alerts

Idle time is calculated from a point when, after a predetermined interval of, say 5 minutes, there is not active use of keyboard or mouse.

In introducing the product to potential users (and investors), the control features of the product invariably attract most attention. And it is true that management of company IT policy and internal security are key features of the product and that the system can be used to ensure that all employees adhere to company policy on PC usage. However, Iontas maintain that there are other significant benefits which the product conveys. They group these other benefits into three distinct areas; performance improvement, reducing the cost of ownership of software and time and project management. These benefits are outlined in more detail below:

- Performance improvement: In this instance it is claimed that employees can analyse their own PC usage with a view to improving their own performance and productivity.
- Reduce the cost of ownership of software: The system can indicate the extent to which different software packages are used. For example, in appendix 1, it should be

possible to see usage of TAS books, which is an accounting software system. Most such software has a price related to the number of users. If a company is paying a license for users who are not actually using the system, then it is clearly an inefficient use of resources. In those circumstances, the number and type of licenses can be reduced to the appropriate level.

- Time and project management: This benefit, it is claimed, can operate at both the individual and corporate level. At the level of the individual, employees can see their own usage of the various tools available. At corporate level the system could act as a basis for automated project timesheeting and analysis. Assume, for example, that a draughtsperson is working on an assignment. By keying in job details, the system could calculate automatically how long the job took. This, of course, is provided that the PC usage equals job duration. If the draughtsperson was away from his or her PC, perhaps discussing the job with a colleague, it may not be recorded. In any event, it is likely that more dedicated systems for that purpose may offer better functionality though they may depend more on the active participation of the person being monitored. An example of such a system is where each employee has a smart card and when they move from one job to another, they swipe the card and key in a job number which automatically ends their involvement on the previous job and starts to book time to the new job.

WHO WOULD USE THE PRODUCT?

A key factor is obviously the level of PC usage in the organisation. If employees typically have a high level of usage, then monitoring that usage may be important. An example of such high usage is call or contact centres and, indeed, this is where the company started. The first product developed by Iontas was branded as Agent Focus and targeted specifically at call centre personnel or agents. Agreement was reached with Stream, a multinational operator of outsource call systems based in nearby Derry, and with up to 1000 agents employed, to trial the product. Essentially Stream provided a contract service for companies which required a long or short term call centre facility.

Other potential heavy users of PCs could be government departments, financial service organisations, educational institutes, and design organisations such as architects, engineers, and print design. Indeed, any organisation, as previously noted, with high PC usage, could potentially be a target.

THE DEVELOPMENT STAGE AT IONTAS

The two businesses Iontas and Iontas Creative Solutions (ICS) began operating in tandem. For Iontas, the key issue was the successful commercialisation of the PC monitoring software. For ICS, it sought out local contracts in areas such as web design. It recruited its own sales force. Otherwise technical staff were used interchangeably between the two companies. ICS was not seen as a strategic business unit in the long term. Its function was principally to generate cash flow to facilitate the development of the Iontas suite of software products. It can be said to have succeeded in that it achieved a turnover in excess of €300,000 in 2001 and broke even based on attributable costs. In the longer term, if Iontas is successful it may be spun off as a separate business, or sold off. As previously noted, Stream in Derry was the first customer of Iontas.

Stream agreed to trial the system. It was an ideal first customer for several reasons. It was close to Moville, operated in a sector that had extensive PC usage, was part of a multinational group, and, at 1000, had a substantial number of employees. That the trial was successful can be illustrated by the fact that Stream are still operating the system albeit at a discounted price which reflects the trial nature of the offering. Martin had naturally hoped that a successful sale to Stream in Derry would open other doors within the same organisation elsewhere but this had not happened. Stream had since been bought out by another operator of outsource call centres, Selectron.

The second major trial customer was Conduit Europe. Conduit was originally developed by Irish entrepreneurs. It operated in two ways. In Ireland, and a number of other European countries, it offered a phone based directory service with associated product offering. In Ireland its directory service was 11850. It also, similar to Stream, provided outsourcing call centres. Orange, the mobile phone operator,

was a client. The first major sale at commercial prices was to Esat, an Irish Telecoms operator since sold to BT and now floated off as a separate business and rebranded as 02.

Thus the initial focus was on direct sales to users. The customers were based in Ireland and could be readily serviced. They were also part of a product proving process so direct contact was vital. In addition, using an intermediary was seen as unnecessary in a local context. The typical intermediary in the software industry would expect a 40/50% discount on list prices.

By autumn of 2000, Martin was satisfied that the product was largely proven though some work remained to be done. Additional capital was now required to help realise the company's plans as the company was not yet generating substantial funds from sales. Its "burn rate", the term used to indicate the excess of cost over cash generated from sales was significant. A high burn rate was tolerable if the prospects were considered good. For example, the marginal revenue of a software product, once breakeven had been reached, was likely to be high. Investors were therefore gambling on an eventual high level of return once the company, in which they had invested, became profitable. An alternative method of return was the sale of the business, typically to a larger player either for cash or for shares. As previously mentioned, Ivron, where Joe Stockton worked, had been sold to Gentner in this manner.

So in autumn of 2000, Iontas sought additional funding. Existing shareholders were requested to provide new capital. However, the directors realised that other sources of investment would be required. After intensive negotiations a phase one funding package of just over €1 million was agreed. The new investors were Enterprise Ireland and Enterprise Equity. Despite the similarity of name, the two organisations were not in any way related. Enterprise Ireland is the Irish Government's indigenous industry development authority. Enterprise Equity is the venture capital arm of the International Fund for Ireland (IFI). It invests in manufacturing and internationally traded services businesses in Northern Ireland and in the six border counties, south of the border. Donegal was one of the counties. IFI had originally been set up and funded by the US, Canadian, Australian and New

Zealand governments to promote peace in Northern Ireland through aiding economic development on both sides of the border. The European Union had subsequently become involved in the funding of IFI and was now the largest contributor.

Negotiating the phase one investment took over 6 months and was not concluded until April 2001. While this was not unusual, it did have two major consequences for Iontas. Firstly, Martin McCreesh was the only full-time senior executive in Iontas and much of his time was taken up with the negotiations. Secondly, by the time they were complete, a worldwide downturn in the IT sector had begun in earnest. It is difficult to pinpoint exactly how and why things changed. A number of reasons might be offered. They include:

- Many major telecoms players had paid very high prices for acquisitions and for 3G (third generation) mobile phone licenses. In the UK alone, the auction of licenses by the British government had raised in excess of Stg £20 billion. Associated with this was a growing concern that the market for 3G mobile products would not be as lucrative as expected. WAP systems, (regarded as 2½ G) had not been widely accepted or used by consumers.
- The dot.com bubble had well and truly burst. Companies returning to the market for additional funding were finding the market much less receptive. Many were folding. Investors were becoming much more discriminating as they realised that the new economy was developing more slowly and in a more patchy way. An early straw in the wind was seen in the American Football Superbowl. Regarded as the world's biggest TV advertising event, it had attracted 20 dot.com advertisers in January 2001. In January 2002 this had fallen to 5.
- Investment in IT infrastructure had been moving at a rapid pace in areas such as cable and broadband. This had led to a glut of offerings not matched by take up.
- The US economy, was finally showing signs of slowing down after an unprecedented boom period of 7 years.

The effects of the slowdown were immediately noticeable in the telecoms sector. Companies such as Nortel, Ericsson and Motorola shed thousands of staff. More importantly, many

large organisations put a blanket ban on all IT and subcontracted purchases until the position stabilised. This was particularly difficult for a company such as Iontas which was seeking to develop a completely new customer base through direct selling to end users of a product which they, the customers, had managed to do without to date.

In addition, the delay in completing the new investment package had meant that it would not stretch as far as had been anticipated. In particular, the proposed strategy of setting up a direct sales force in key markets such as the US was becoming more like a risky gamble. As a result, Iontas began to look towards resellers as a possible route to market.

EXAMINING THE RESELLER ROUTE TO MARKET

Iontas personnel had attended a number of trade fairs and had attracted considerable interest from a variety of resellers of software products. Early in 2001, it began to investigate some of these opportunities. They offered no guarantees of successful sales. However, they were likely to be closer to their customers and also in a better position to introduce a new product to existing customers. Resellers were selected based on their existing business levels and contacts. The objective was to develop a critical mass of business quickly. A total of eight resellers were selected. Two were located in Ireland, two in Spain and one each in Turkey, Australia, Germany and the UK.

The results were distinctly unimpressive. Each had indicated a potential for a minimum of €100,000 in sales per annum. None delivered anything like that figure. An example was the Turkish reseller whose overall turnover fell from $8m in 2000 to $1m in 2001. The UK reseller closed. Only one of the resellers generated some business and that was one of the Irish companies. Even that was limited but was showing some potential at the end of 2001.

Through the contacts developed with the resellers, another problem began to emerge, particularly in continental Europe. It became apparent that the business culture in Europe was less favourable to the concept of PC usage monitoring. Initial indications were that, before an organisation could install the software on a PC, it would have to seek the permission of each staff member affected. In Germany, in particular, all

organisations were required by law to have works councils, which represented employee interests. These councils would have to agree to the installation of the software. All indications were that this would not be approved.

However, in anglophone markets such as Ireland, UK, US and Canada, the business culture simply required that employees be informed of the use of the software.

The events of September 11th 2001 had also altered the landscape considerably. Prior to that, personal privacy had dominated considerations of such software. However, that focus on privacy was already beginning to shift with some case law beginning to indicate that employers could be held liable for material sourced or used by employees. With the rapid growth of the internet, all parties, including lawmakers and regulators, were learning in a new environment which was not easily managed at national level. The events of September 11th placed a major new emphasis on security over privacy. Nowhere was this more evident that in USA. Though daunted by the cost, Iontas began to look more towards that market. It had always been seen as the prize market. Martin had hoped to enter that market through first targeting Irish based subsidiaries of US multinationals. He was aware that this had been the market entry model selected by other software developers. Now it was clear that it required a more direct approach.

A prerequisite of the new strategy would be the establishment of an office in the US. It was already apparent that potential customers demanded a local presence to support a product. Iontas dipped its toe in the water by taking space in a serviced office complex operated by Enterprise Ireland in Boston.

Martin had also recruited a business development manager for the North American market. From London, Zal Hassan had already worked in the US, marketing video editing software. She had left the US when her visa had expired and had come to live in North Donegal. She had spent the past few months on desk research and had lined up a number of potentially interested partners in the US.

Martin and Zal had visited several potential partners and customers in the US in recent weeks. The response had been

encouraging though most businesses in the sector were still suffering because of the general downturn and the events of September 11th. However, it was also clear that those events had placed a greater emphasis on security issues. In particular, the authorities were targeting electronic methods of communication and funds transfer in their efforts to pursue those responsible and their associates. It was not clear whether this emphasis on security would continue to last when, as seemed likely, enquiries would drag on for several years. In passing, it was clear to Martin that the availability of a Boston address had greatly increased the credibility of Iontas as a potential supplier in the US market. However, it was also evident that a more active presence in the market would be of benefit. The previous decision that direct sales to end users was not the route for Iontas was also borne out. It was clearly beyond the resources of Iontas to gain direct access to users. The product was not of sufficient value or central to customers' activities to gain access easily. Therefore it seemed certain that the products should be sold through resellers.

Three possible categories of resellers had been identified. The first of these involved businesses which might act as distributors on an exclusive or non-exclusive basis, possibly also selling through a further channel level such as a peripherals supplier or retailer. This approach was common in a variety of other industries but was less common in the software sector. It appeared to be confined to small ticket items and /or software which did not require high levels of support. Examples might be anti-virus software, accounting systems, payroll systems or CAD software. Given that the decision to install Iontas products, Agent Focus or PC Focus, was likely to be made at a relatively senior level in an organisation, this channel was unlikely to be appropriate.

The second channel identified was that of technology partner. In this instance the technology partner typically had an existing suite of products incorporating software and possible hardware designed for a specific purpose. Good examples of this were systems designed for call centres, an industry of considerable interest to Iontas. Here the technology partner might supply a complete turnkey system for a call centre or the operating software to manage/upgrade

a call centre. This might involve routing calls to free operators, monitoring call answering and recording calls. In this instance, the Iontas product would be incorporated into the technology partner's offering and Iontas would receive income based on the number of users of its software. So the Iontas products would become a small part of a more comprehensive product offering.

The third type of channel under consideration was that of managed service providers (MSPs). While there was some overlap with technology partners, essentially MSPs managed all or part of the IT function in their clients. These clients were typically large organisations in both public and private sectors such as government departments or other public services (Iontas had recently undertaken a pilot project for the Irish Law Courts Service), local authorities, banks and other financial institutions and manufacturing businesses.

A key advantage of the MSP route was that MSPs had a portfolio of existing clients to whom the PC usage monitoring systems could be sold. MSPs would clearly be more inclined to encourage the adoption of the system if they were being rewarded for doing so.

There were, however, some implications for Iontas of selecting the reseller route. Its brand and subbrands, Agent Focus and PC Focus might quickly disappear from view, subsumed into the overall offering. Direct connection was also lost with the end user which might limit the company's scope in enhancing or further developing the product suite.

PRICING THE IONTAS PRODUCTS

As with most software products, a variety of pricing models are available. It is particularly problematic to price a relatively new to the market product. Marginal costs per unit are low and offer no guideline. Iontas had sought to develop a "what the market will bear" strategy but even this was a very inexact science. Its chosen model was based on the number of users in any customer. It was not interested in small orders as these were likely to prove expensive to install and maintain. The chosen model involved an initial capital cost of €100 per user dropping to €50 per user where there were more than 1000 users in any site. Reseller margins would vary from 30% for

small orders to 50% for larger ones. Iontas would also charge an annual maintenance cost of 15% of the original capital cost. Thus, for a 1000 user site, the end user would pay €50,000 for the initial license and €7,500 per annum thereafter. The reseller would receive €25,000 of this or 50% of the initial payment. Other pricing models had been considered and, in one case, used. This involved an annual license of €30 per user. This reduced the upfront commitment and enabled the end user to trial the product.

A further pricing model might apply in the event of a very large order for incorporation into a high volume product. Suppose, for example, MS Office were considering incorporating the system into their product? While Martin was looking forward to Christmas, he did not expect to find a gift like that in his stocking!
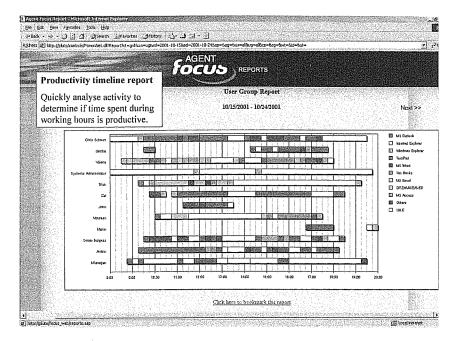
LOOKING FORWARD TO 2002

As he prepared for the Christmas break, Martin was still confident that 2002 would see a major breakthrough for Iontas. He was convinced of the value of the product and that it would sell as market conditions normalized. There was no doubt that 2002 would be a make or break year. At the present rate of "burn" he expected to require further capital investment before the end of 2002. The investors were aware of this and the phase 1 investment had been made on the assumption that a further phase of funding would be required. There was substantial interest emerging from resellers. However, this would only be translated into sales if and when the resellers became committed to the product and obtained orders from their clients. Competition was emerging both in a direct and indirect sense. Direct competitors also offering PC usage monitoring included Trysys, Bardon Data Systems and Harddrive Software. Other indirect competitors offered software metering or internet monitoring focusing on only one of the benefits claimed for the Iontas products. Competitive products appeared to be similarly priced. He was satisfied that the Iontas product was still ahead of competition though he recognized that this was no guarantee of success. In his business plan he had projected €250,000 turnover in 2001. Actual turnover would be half that. He was looking to reach
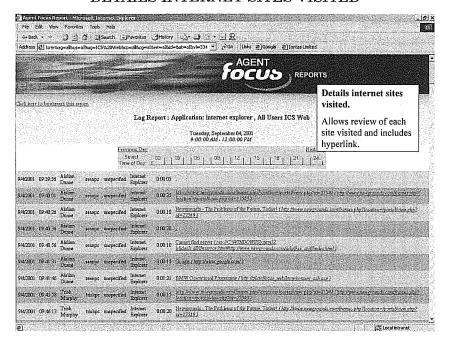
€1.5m in 2002 and €6m in 2003. Given that the sales cycle was 3 to 6 months he recognised that he was already behind his forecast for 2002. It was a paradox that a major advantage of the product – that it was easy to trial – also tended to slow the sales cycle as potential customers took time to evaluate it. He and Joe had already discussed increasing their presence in the US market but this would increase the burn rate. He, himself, was contemplating spending 50% of his time there, though he recognised that he also had to manage the overall business at Moville.

Out of the blue, perhaps there was a solution. He had been aware for some time that Joe Stockton had been under pressure from Gentner to relocate within the US. He also knew that Joe was resisting this. Knowing where he was to be relocated, Martin had great sympathy with Joe! Now he had just put the phone down after a call from Joe to tell him that he had been released from his earn out agreement and would be available in January. It would make sense to use Joe on the ground in the US. He would need the support of Zal and two of the existing technical staff. Martin estimated that , roughly this would double the burn rate to €100,000 per month. He would have to sell this to the investors. Truly, there would be plenty of food for thought over Christmas.

PRODUCTIVITY TIMELINE REPORT

DETAILS INTERNET SITES VISITED

GAMES USAGE REPORT