Finding Success in the new Open Source Landscape

Lessons learnt from Jboss, Digium, Hyperic & Ringside

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A Tag Team Approach

- David Skok
  - Serial Entrepreneur for 25 years
    - Started 4 companies & performed on turnaround
    - 3 of those companies IPO-ed
  - Became a VC in 2001
    - 3 successful exits (AppIQ, JBoss, Tabblo)
    - Open Source investments: JBoss, Digium, Ringside
- Bob Bickel
  - Founder Bluestone Software (IPO, then sold to HP)
  - SVP of Strategy, JBoss
  - Active Board member, Hyperic
  - Founder, Ringside Networks

A Selection of Key Issues

- Suitability of Product Category for Open Source
- Building a Community and growing Downloads
- Strategies for Monetization
  - Converting Free Downloads to Paying Customers
  - Creating the Subscription Offering
- Building the Sales & Marketing Machine
  - Expanding Deal Size
- Building a Management Team
- Exits and Valuation

Suitability of Product Category for Open Source

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Key Characteristics

- JBoss
  - Java Application Server
    - Used to run Mission Critical applications
- Digium / Asterisk
  - PBX & Telephony Server
    - Company phone system is extremely mission critical
- Hyperic
  - Web Infrastructure Management Software
    - Large mission critical deployments fundamental to business (on-line business)
- Ringside
  - Social Application Server any web site to weave in Social Networking
    - Customer facing, mission critical
    - A key function for Marketing

Building a Community and Growing Downloads

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JBoss

- 1999 to 2003: over 5 million downloads
- Built without spending money
- Developers already have strong communities on the web
  - The ServerSide
  - SourceForge
  - SlashDot
  - Etc.
- Exceptional PR
  - Marc Fleury played role of industry bad-boy - the press loved to quote
  - Nathalie Fleury leveraged the Blogosphere very well
  - Worked hard to make boring technology sexy
- Created a wave of free press coverage

Digium

- 2000 - 2004: 2-3 million downloads
  - 2007: 1 million downloads
- Promoted by Tim O'Reilly, Jeff Pulver (VON show & magazine)
- Telephony Tradeshows
- Very strong PR
  - Mark Spencer provided a great public face
- Strong brand awareness
- Asterisk: Clear market leadership

Hyperic

- 2004-2006
  - Spun off from Covalent for $1
  - Trial Version via web
  - Foundation of JBoss Operations Network
- Summer 2006 – Open Source
  - Accel and Benchmark invested to make transition
- 2008
  - Focus on Web Infrastructure Management
  - 15,000+ Downloads per month, >4,000 Open Source deployments
  - Open Source Feedback – 432,000 MySQL Tables managed!
  - OEM deals with JBoss, MySQL, Spring, Mule, Iona
  - Large 2,000+ Server Customers – hi5, Cnet, Ask.com, eHarmony, Mosso (VMWare Hosting), Contegix

Ringside Networks

- Founded in 2008
  - Ex-Bluestone and JBoss team
  - Seed funding from Matrix Partners
- Social Application Server
  - Allows every website to weave in social applications
  - Facebook compatibility
  - Written in PHP
- Who is the target?
  - Website developers will get easy access and can add functionality
  - Marketing or the website business owner is the real buyer – how will this translate for large enterprises?
- Recent PR
  - Open source was mentioned in headline, but Social Networking is what got the press

Going Forward

- In the early days PR for Open Source was easy
- Question:
  - Has Open Source now become mainstream, making it much harder to get the press coverage that was so important to creating awareness at a low cost?

Strategies for Monetization

Turning Free downloads into Paying customers

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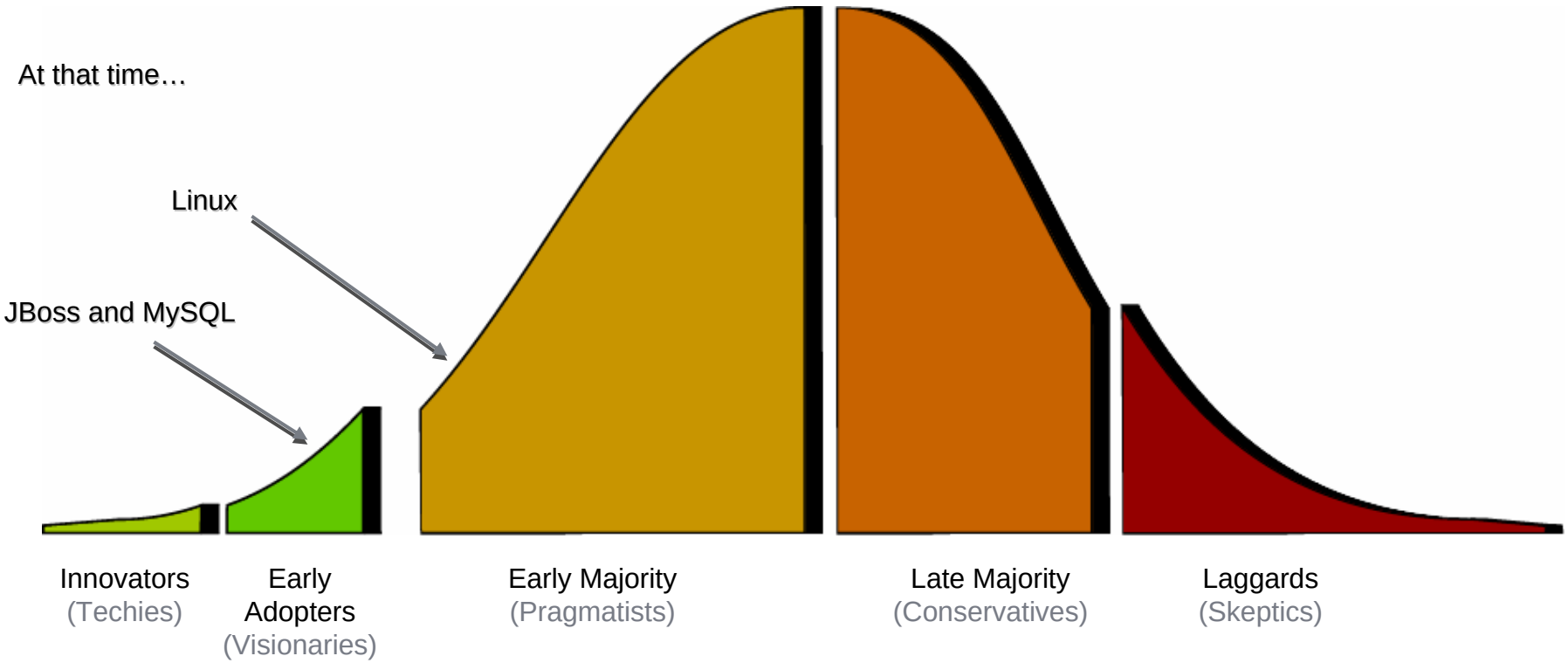
The thought process at JBoss



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What Early Majority Buyers want

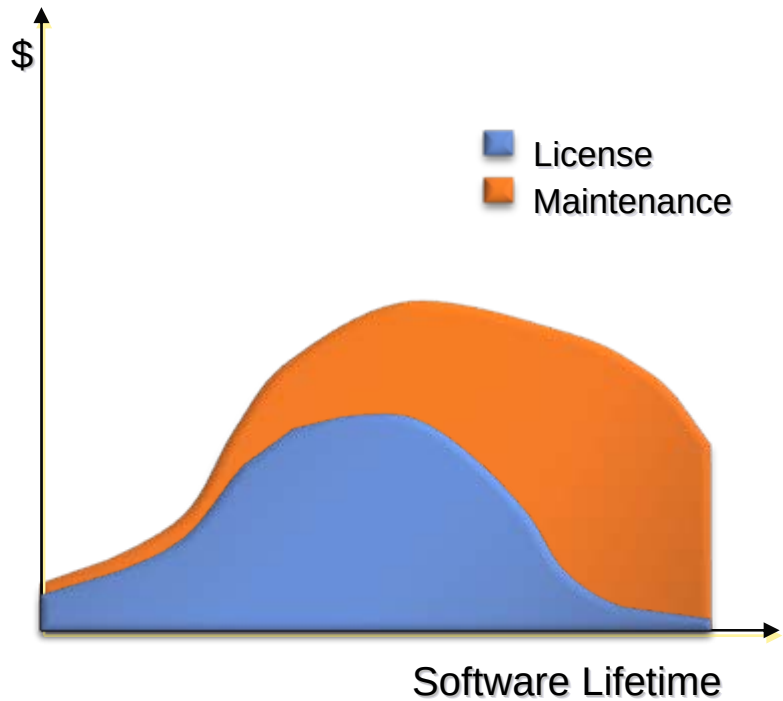
- A “throat to choke”
- Roadmap
- Indemnification
- Longevity

Value to the person with budget

- Understand that you cannot expect great service unless you pay for it

Maintenance Revenue and Subscriptions

- Maintenance is where all mature S/W companies make profits
  - Selling new licenses is very costly
- Subscription is highly valued
  - See multiples for RHAT, Salesforce.com, etc. versus traditional license software companies
    - Typically valued at 20-25x next year's free cash flow



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JBoss creates “Professional Open Source”

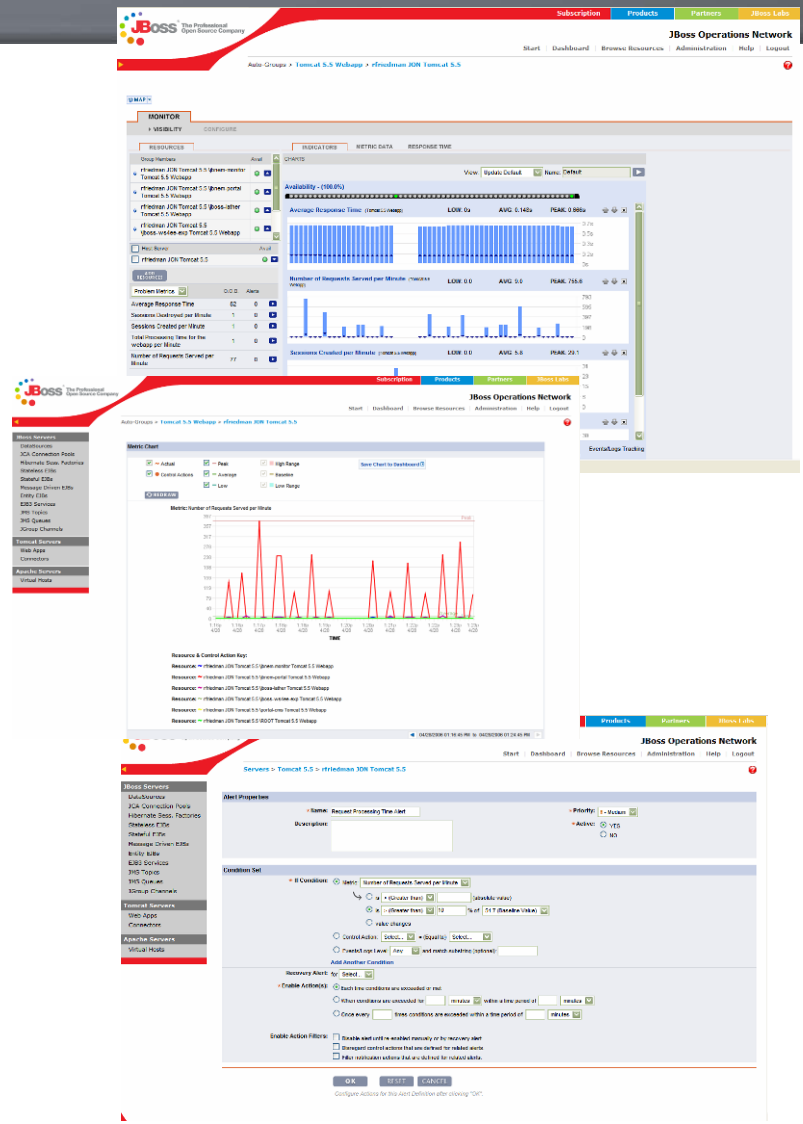
- The key elements of Professional Open Source
  - Open Source as a viable business model
  - Developers of Open Source get paid
    - Hired all the best JBoss contributors
  - Products remain Free and Open Source
    - Revenue comes from providing value-added services that the customer wants to pay for
- Sell Support Contracts
  - For 3 Applications in Production
    - $20,000 gets 24 hour response time
    - $40,000 gets 2 hour response time
- Far cheaper than BEA/IBM’s maintenance contracts

Creating a “Subscription” offering

- Support offering is not enough
- Subscription:
  - A bundle of several components that each provide value that the customer is willing to pay for
- Elements of the JBoss subscription
  - Hardened version of the software
  - Support
  - JBoss Operations Network
  - Improved self-service web support and knowledgebase
  - Etc.

The JBoss Operations Network

- Modeled after Red Hat Network
- Provide more clear value add to the customer
  - Beyond just support
- Monitoring and Management were key elements



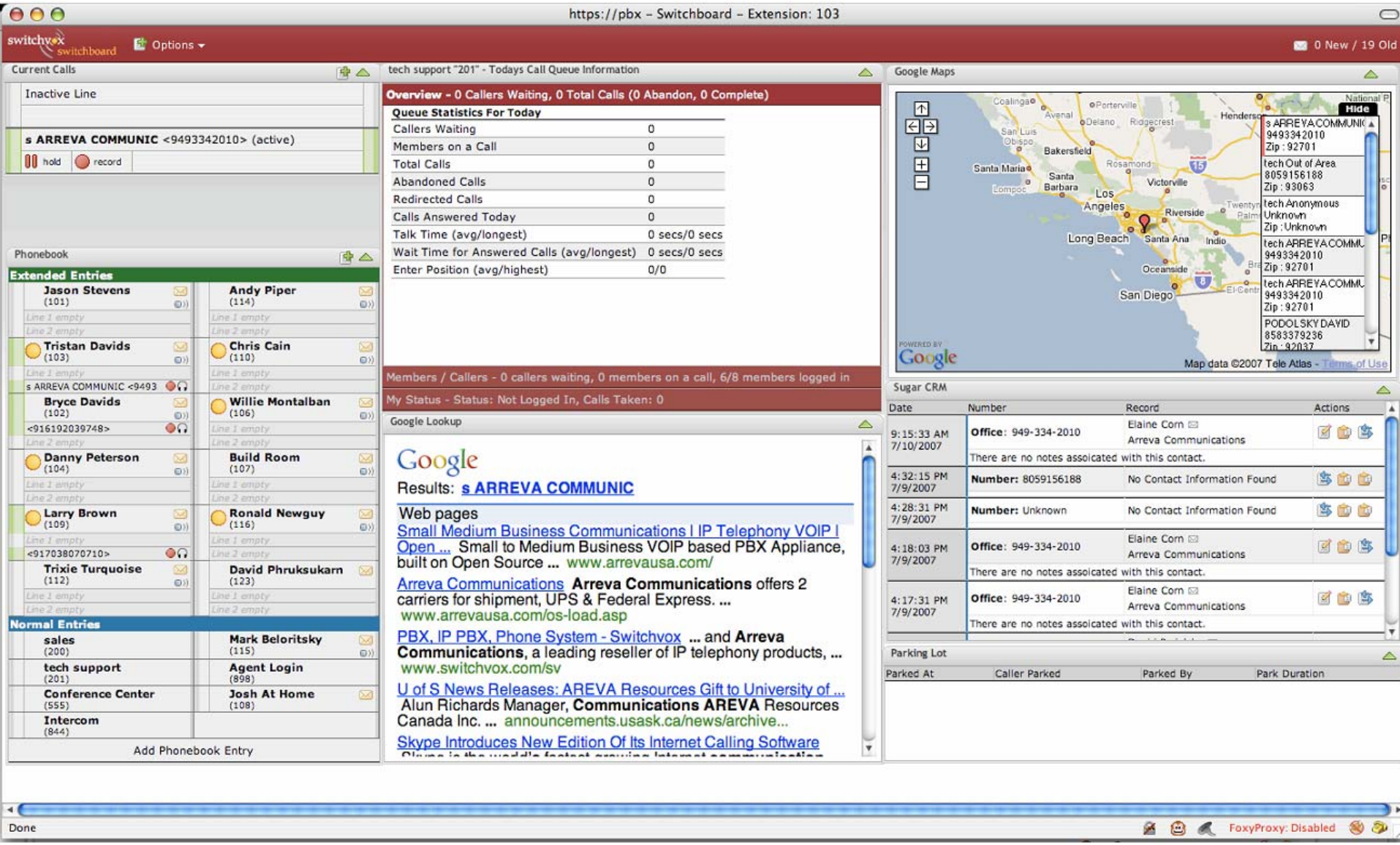
Evolution towards a Subscription

- Subscription is a marketing bundle
  - Hardened version
  - Indemnification
  - Support
  - JBoss Operations Network
- This changed the whole value proposition for the salesforce
- At Red Hat moved JBoss totally to Fedora/RHEL Model
  - Only way to get production version is to buy it.

The Digium Story

- Started by making money from telephony boards
  - Extremely successful: 50% EBITDA
- Recent Evolution
  - Acquired Switchvox:
    - Highly featured PBX built on top of Asterisk
    - Free and for-pay SMB versions
      - Early adopter customers like free software
      - Early majority customers don't feel comfortable with a free phone system
  - Sell Appliances (bundled servers and software)
  - Subscription offering similar to JBoss

Switchvox Screenshot



Hyperic

- Initial flip to Open Source Model
  - Put most of functionality into the open source version
  - Struggled with which features to put in Enterprise Version – not as clear as JBoss' Middleware vs. Management
  - Sales frustrated there was not more differentiation
- Long term goal is arriving
  - Have learned which parts to be in OS and EE
  - Clear value in OS version, and now monetizing 2-3% - similar to JBoss.
  - Similar growth rates to JBoss

Ringside

- Just launched and everything is in Open Source
- Clear delineation of what is open source and what will be subscription and other monetization
  - Open Source – The Platform
  - Subscription – Social Graph Analytics, Specialized Social Applications
  - Other Monetization – Payment Services and Advertising Services

Building a Sales and Marketing Machine

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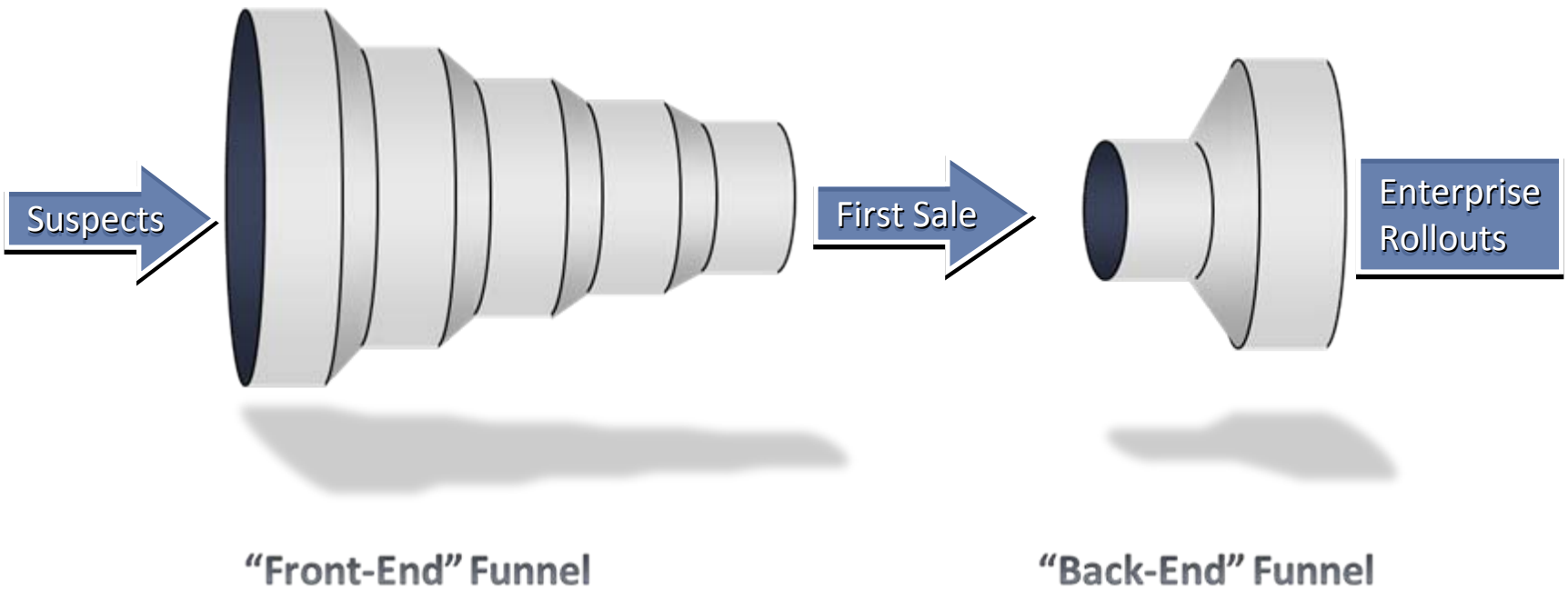
It's about lowering sales costs

- Myth: Open Source is about lowering Development costs
  - Wrong
  - May lower QA costs
  - Peer review will produce higher quality software
- But the real value to Open Source is **lower Sales and Marketing costs**
  - GE email example
- **Note**: This only works if the community forms with very low investment

Building a Sales & Marketing Machine

- A concept that I had been working on for many years as an entrepreneur
- Provide a scientific process for designing and evaluating sales and marketing programs
- Defining “Machine”:
  - A scalable process that can be cranked up when needed
  - Requiring minimal manual intervention
  - Clear understanding of costs and returns
  - Dashboard providing Key Performance Indicators

Unified Sales & Marketing



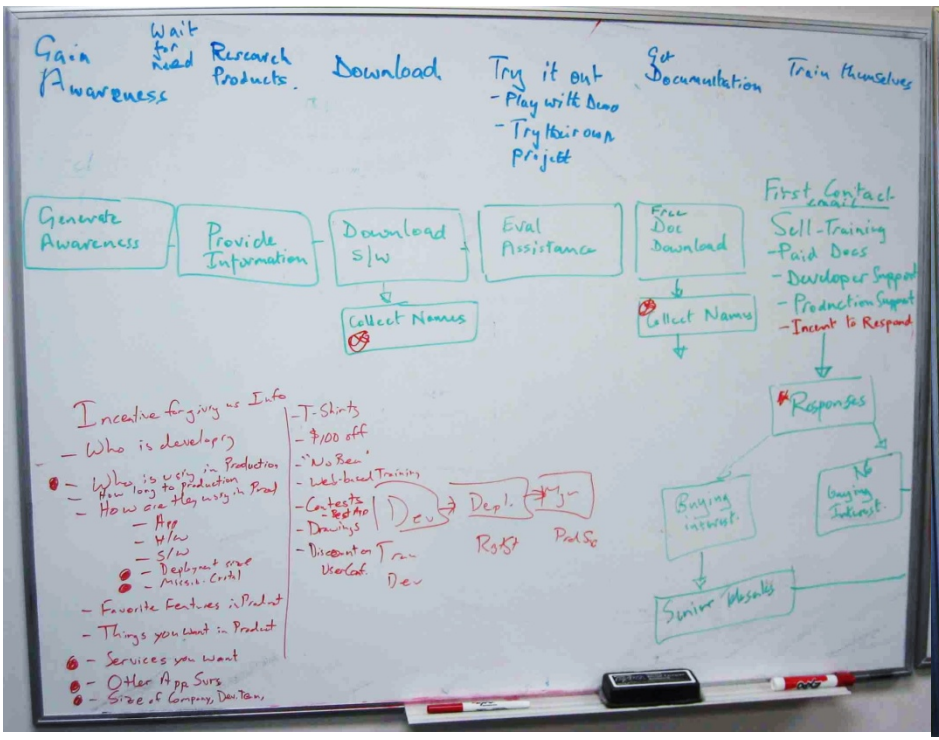
Sales & Marketing Machine Concept addresses the following issues

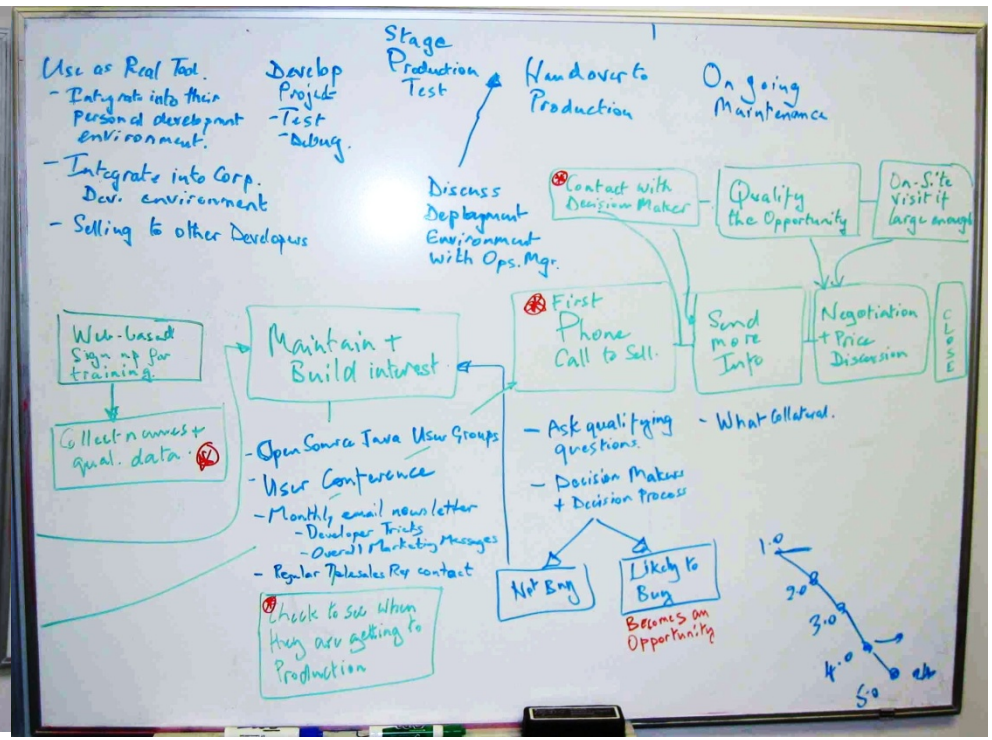
- Clear linkage of every marketing action to process of closing a sale
  - True integration of Marketing with Sales
- Solve the age old problem: not enough **qualified** leads
- Eliminate manual steps
  - Particularly critical in Open Source as the volumes of leads are very high
- Identify and eliminate blockage points
  - Reduce the sales cycle
  - Increase close rates
  - Lower customer acquisition costs

The Starting Point

- 5 million downloads
- **BUT**…
  - No contact information had been captured
  - Only a few names from training courses
- The company was selling documentation
  - $27k in revenues per month

The Original Brainstorming Session



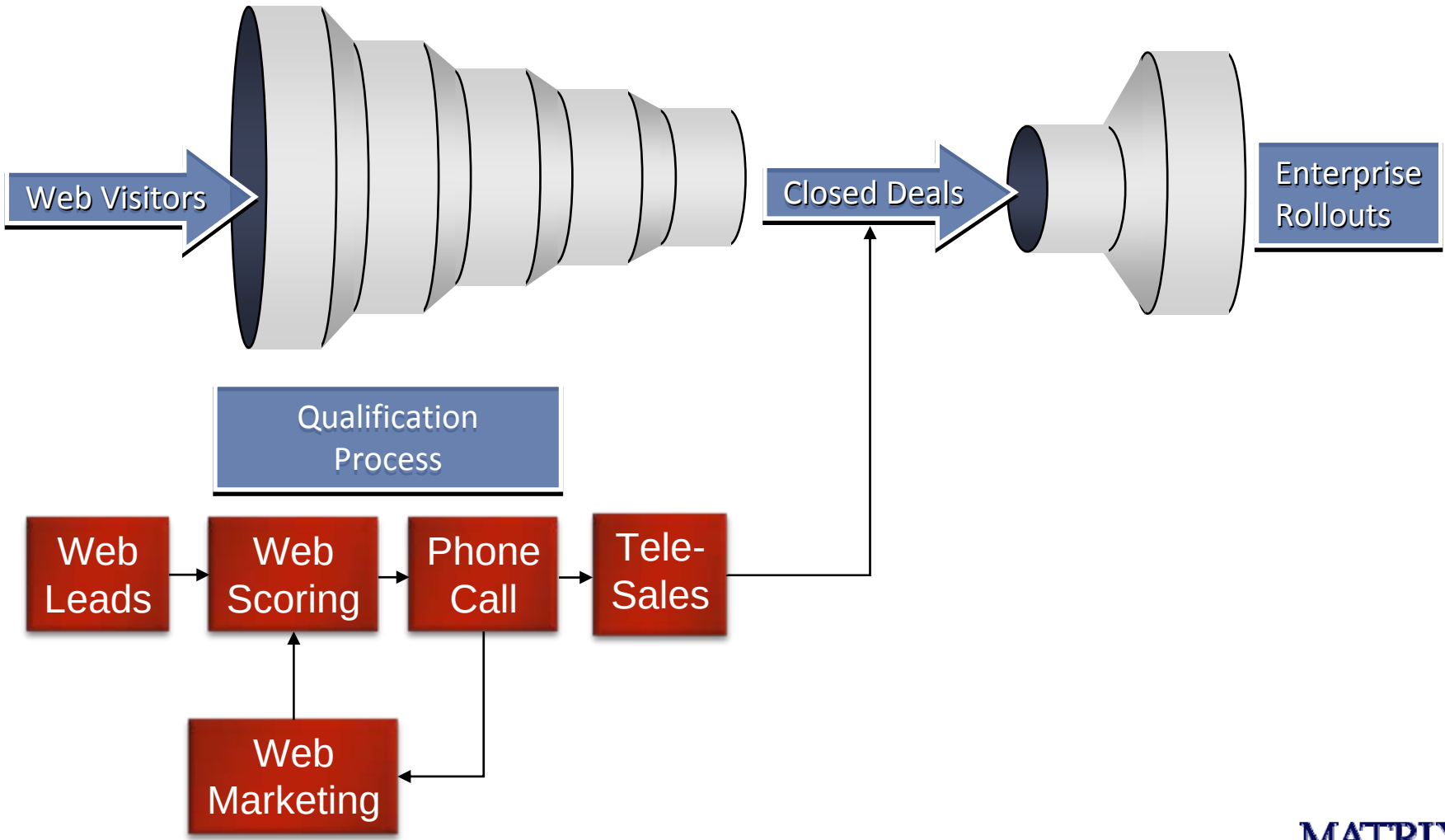


Rapid Success …

- 14,000 leads per month
- 3,500 people viewing Webinars every month

- But 14,000 leads is actually a big problem…
  - Try asking a sales person to phone 14,000 leads in one month

The Finished Process - (key elements only)



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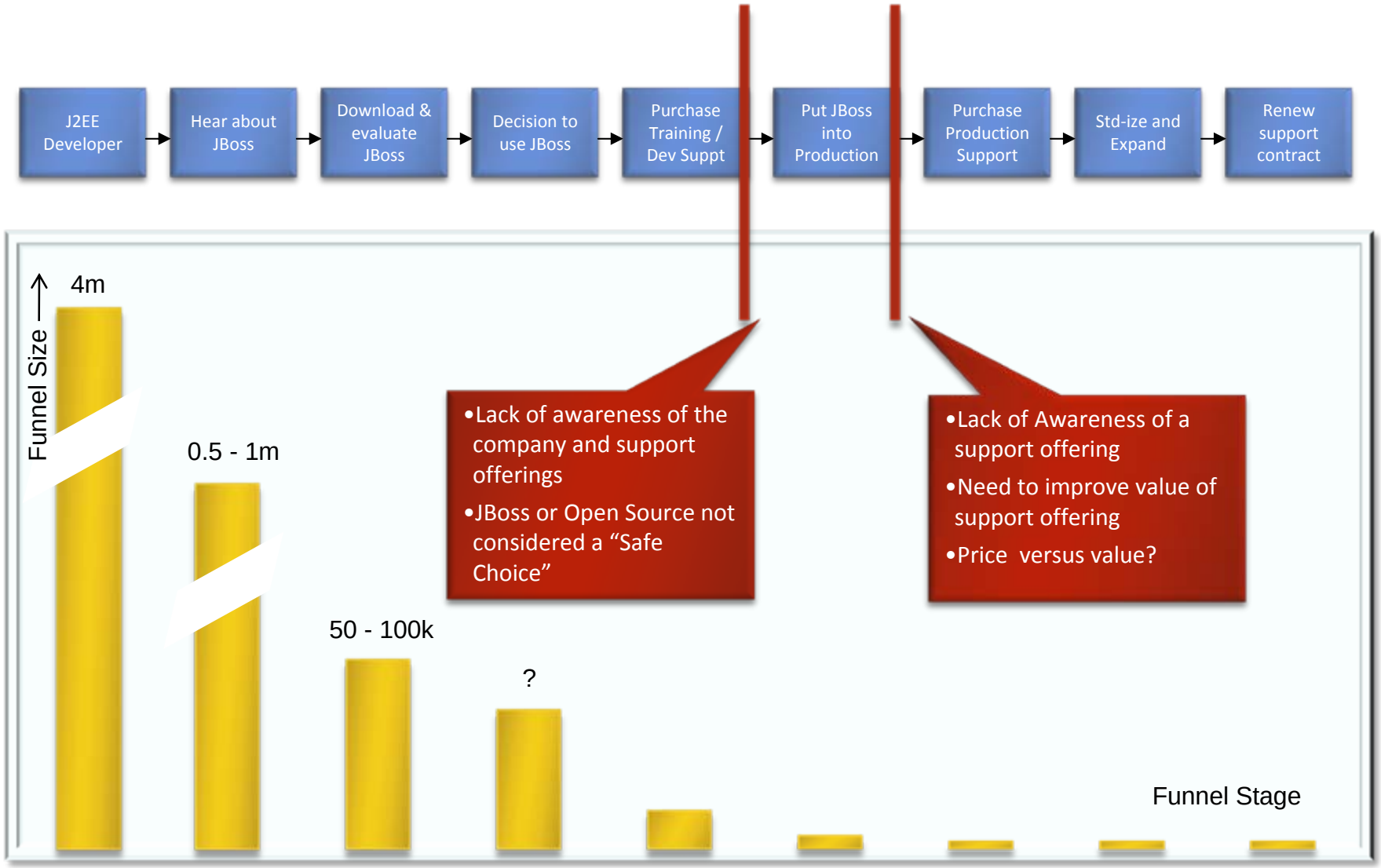
Using the model to work backwards

- To do $4m in the quarter:
  - If Average Deal Size is $10k
  - Need $4m divided by $10k deals to reach target = 400 deals
  - Means 1,200 deals being worked in telesales (400x4)
    - Know that each rep can work 60 deals at a time, means 20 reps
  - Means 3,600 telemarketing calls (1,200x3)
  - Means 14,400 Raw Leads (3,600x4)

Closed Loop Marketing

Key Blockage Points with Reasons



5 Dimensions for Growth

- Add Sales coverage to leverage the huge leadflow
  - 16,000 leads per month
    - Growing rapidly due to Open Source crossing the chasm
  - Leverage partners
  - Expand geographically
- Convert more of the non-paying users to paying
  - Only 3-5% of the user base was paying
  - JBoss ON introduced truly compelling features
- Convert more departmental customers to Enterprise
  - Increase ASP, lower M&S for renewals
- Expand the product line to a full middleware offering
  - JBoss labs to create a pipeline of new projects
- Build out the Partner Ecosystem
  - Provide value to eco-system, and collect % of $10Bn ecosystem

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Pricing matrix

- Evolved a sophisticated multi-dimensional pricing matrix
  - No of Servers in production
  - No of Products suppored (JEMS)
  - No of named support individuals
  - Etc.

Building a Management Team

Building a Management Team

- Vision is easy - Execution is far harder
- JBoss: The key hires
  - Bob Bickel, VP of Strategy (PT 10/02, FT 9/03)
  - David Skok, VC (12/03)
  - Tom Leonard, VP Business Development (1/04)
  - Cary Smith, CFO (2/04)
  - Joe McGonnell, Dir. of Marketing (2/04)
  - Rob Bearden, SVP Sales & Marketing (5/04)
  - Brad Murdoch, VP of Customer Services (8/04)
- What made JBoss was exceptional execution
- Exceptionally talented management team = Good execution

Exits and Valuations

A Personal Philosophy on Exits

- Focusing on exits leads to poorly built companies
  - Customers see it
  - Potential employees see it
  - Potential acquirers see it
- The best companies:
  - Built by people that are passionate about their product
  - Focus on creating value for their customers
  - Look after their employees
- Don’t focus on Exits, and they will come to you

Valuing an Open Source company (M&A)

- Ultimately companies are valued on future cash flows
  - Simple Discounted Cash Flow analysis
  - Recurring revenue models mean highly predictable future cash flows
- In that model, growth is very highly valued
- Parameters that change the valuation…
  - Strategic value of asset
  - Synergies
  - Competing bidders

Summary

- Suitability of Product Category for Open Source
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The JBoss Spirit: Batman Villains

The JBoss Spirit

Backup Slides - Not Used

The VC Funding

A Fundamental Catalyst of Change

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JBoss Pre-Funding

- Company of 11 people
  - Some extremely smart and entrepreneurial individuals
- Offices with 2 rooms
- Revenues of $750k per quarter
  - Mostly Training
  - Documentation
  - Consulting
- No experienced management
  - But … Bob Bickel was starting to get involved

Marc and Ben Sabrin

Why JBoss raised capital

- JBoss did not need the cash
- The real reason for raising the money was to get all the “Soft Services”

"Matrix Partners has been instrumental in JBoss' success. David Skok's industry expertise, extensive network of relationships and continual support were vital in helping to build the JBoss management, sales and marketing teams. He has been a mentor to me personally, and played a key role in working with our strategic partners. We relied upon Skok's guidance and advice every step of the way from creating a successful company through the M&A process. He has truly been an asset to our organization."

— Marc Fleury

Post Funding Priorities

- Building a Management Team
- Building a Sales and Marketing Machine
- Building a range of Services offerings
  - That offered high value to customers
  - To attract non-paying customers into paying
- Business Development
  - Create and leverage key partnerships such as HP

JBoss Marketshare Analysis

QUESTION 7. Which Java application servers are currently in use at your company (or at the companies to whom you consult)?

	Aug. 2002	Nov. 2003	Nov. 2004
JBoss' Application Server	13.9%	26.9%	34.8%
IBM's WebSphere App Server	29.0%	40.1%	33.9%
BEA's WebLogic	24.5%	34.6%	28.7%
Oracle's 8iAS, 9iAS, 10gAS	20.8%	29.1%	22.0%

Java Use and Awareness Study © BZ Research November 2004

http://sdtimes.com/article/story-20050101-05.html

Gartner Magic Quadrant Leader

Enterprise Application Server Leaders are

JBoss, IBM, BEA, Oracle, and Microsoft

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IPO or Sell

- Designed the business to do an IPO
- Events put the company in play
  - 4 interested buyers
- Comparison of IPO versus Acquisition…
  - Led to decision to sell

Looking back…

- Early 2004 – venture round closes
- Revenue Growth:
  - 2004 $11m
  - 2005 $26m
  - 2006 on plan to do $65m

JBoss: What worked

- Large and vibrant community, built at very low cost
- Exceptional Brand awareness
- Mission critical application platform
  - Customers needing support, and willing to pay for it
- Outstanding Management Team
  - Vision was extremely good
  - Execution was exceptionally good
- Helped create a press wave of attention on Open Source
  - …and rode that wave very well

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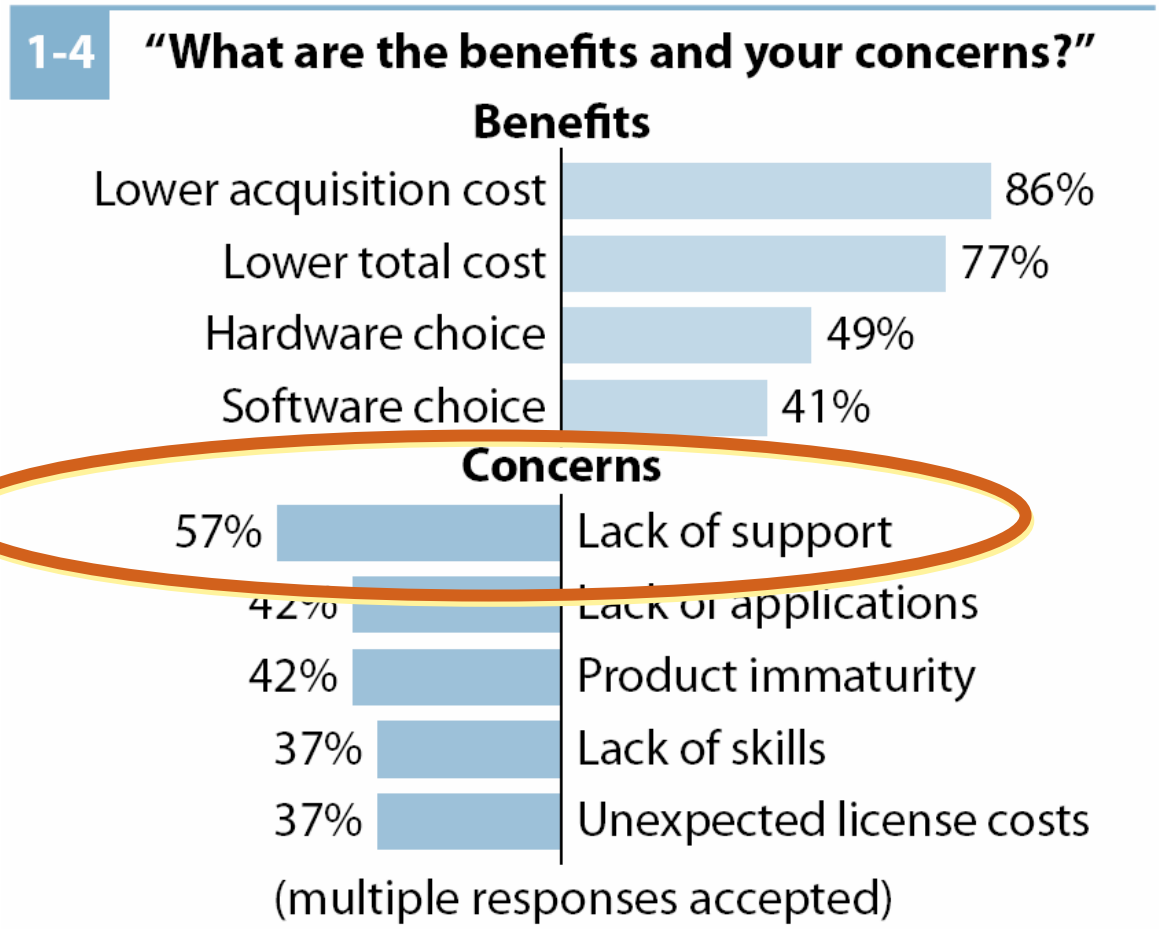
Forrester Research



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Primary Initial Service Offering

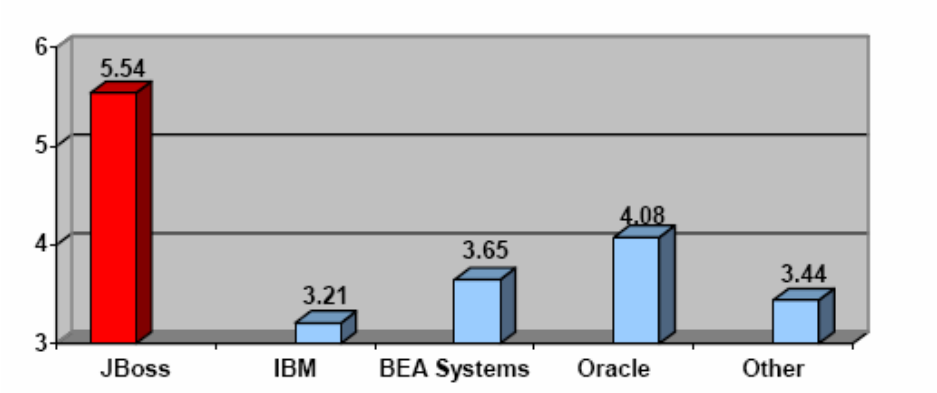
- Production Support Contract
- More like an Insurance policy
  - Hope not to have to use it, but when it's needed it can be critically important
- High margin
  - Since it is not used very frequently

Renewal Rate

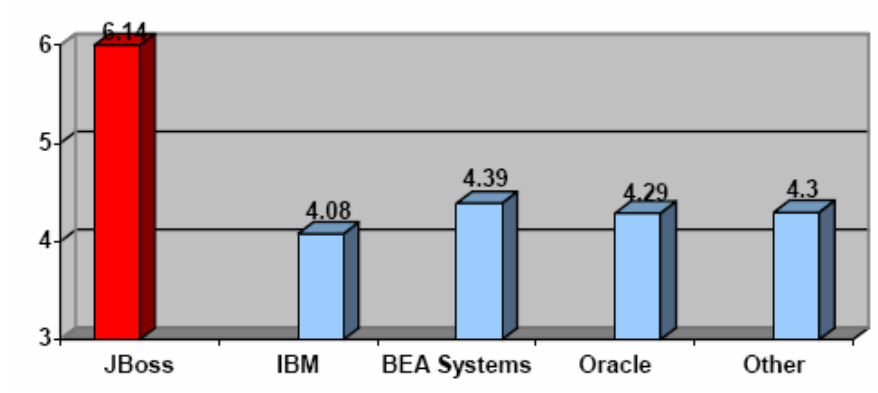
- In a recurring revenue model, Renewal Rate is a key statistic
- JBoss achieved an 85% renewal rate
- Maniacal focus on customer satisfaction

Customer Satisfaction

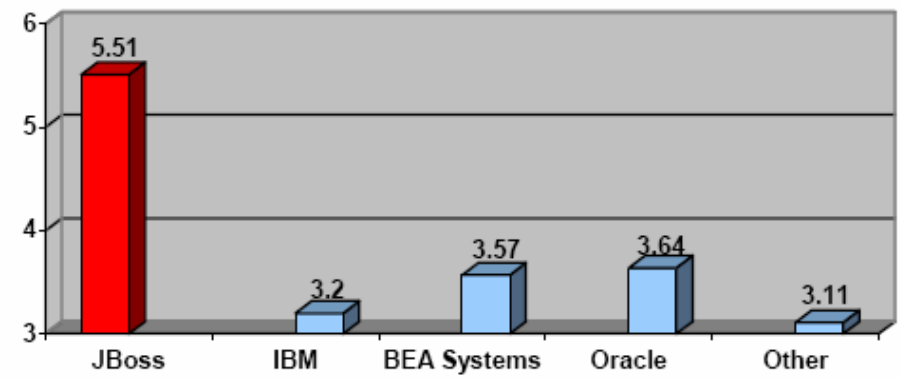
The Vendor provides excellent value for my support services investment.



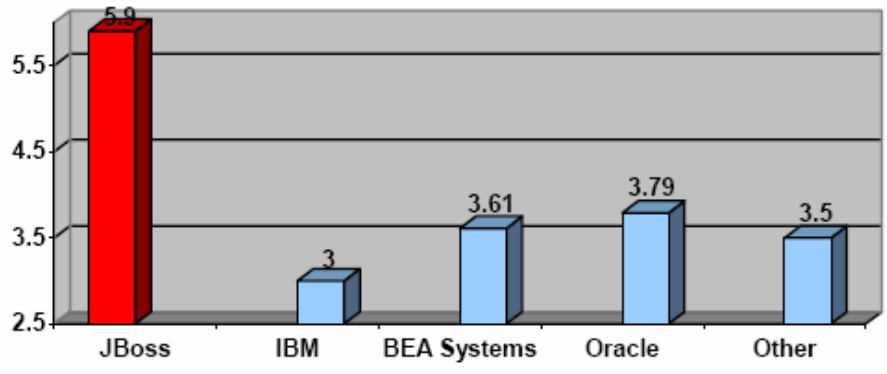
The Vendor's support staff knows their product(s) well.



I can easily get access to key people at the Vendor.



It is very likely that I would recommend the Vendor to others.



JBoss Support Survey, November 2004 – Velociti Partners.
Respondents using more than one application server vendor.
184 Customer responses for JBoss, 84 BEA, 28 IBM, 14 Oracle, 14 Other
Full report available at http://www.jboss.com/pdf/supportsurvey.pdf

Evolving Customer Buying Patterns

- Pre-Internet
  - Information about products hard to find
  - Reliance on your local sales rep for information
- Post Internet and Google
  - Use Google search to find any information
  - Full access to competitive info and pricing data
  - Technically smart buyers (developers & IT) prefer self-service to sales reps
    - Prefer to Download and try it

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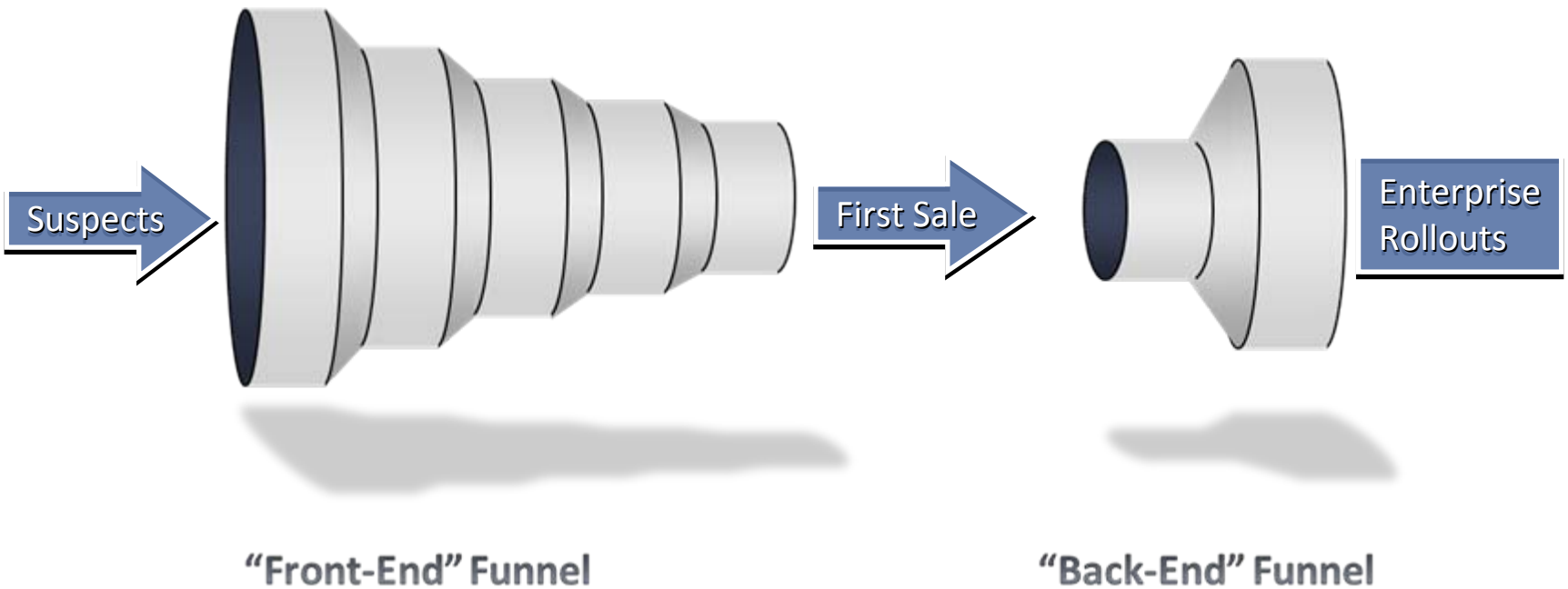
Unified Sales & Marketing



Metrics: The End Goal

Selling Open Source

- Very different sale to licensed software
- Not selling the product
  - Everyone we were selling to already had the product
  - Had to convince them they need support / services