

Cisco SaaS-es Microsoft, Hits On-Demand Highway with \$3.2 Billion Acquisition of WebEx

Abstract

On March 15, 2007, Cisco Systems, the world's #2 network equipment manufacturer—which was relegated to second place in that department after the merger between fellow heavyweights Alcatel and Lucent in 2006—announced it would acquire WebEx, the market leader in on-demand collaboration applications. WebEx's network-based solution for delivering business-to-business collaboration extends Cisco's vision for offering the market a unified communications portfolio, particularly within the small-to-medium business (SMB) segment. More broadly, it also addresses two mega-trends among some of the world's large communications companies: [1] away from “paving the highway” toward driving lucrative applications and services over that highway, and [2] providing software as a service (SaaS).

Event

With 2.2 million registered users, WebEx is the global leader in on-demand applications for collaborative business on the web, which it delivers over its global Media Tone Network. Cisco has commenced a cash tender offer to purchase all outstanding shares of WebEx for \$57 per share and will assume outstanding share-based awards for an aggregate purchase price of approximately \$3.2 billion, or about \$2.9 billion net of WebEx's existing cash balance. WebEx was founded in 1995, launched its IPO in July 2000 and at the time of this acquisition has nearly 2,200 employees. For FY2006 ended December 31, 2006, WebEx reported revenues of \$380 million. The companies expect the transaction to close in the fourth quarter of Cisco's FY2007, and following the close WebEx will become a part of Cisco's Development Organization.

Context

Cisco launched its own videoconferencing offer, TelePresence, in 2006, but WebEx is the gold standard for videoconferencing, having transformed it into an online service that allows anyone connected to the Web to hold secure conference calls. Beyond Web conferencing, WebEx also brings other goodies to the table. WebEx's Media Tone Network (MTN) is a global platform specifically designed for secure delivery of on-demand applications. WebEx Connect lets users integrate data from multiple applications and create a customized collaborative workspace that can integrate with local workflow and business processes. WebOffice provides document

sharing, calendars, databases and Web meetings over the MTN. WebEx AOL/AIM Pro Business Edition offers group chat, VoIP capabilities, centralized administration, secure file transfers and integration with Microsoft Outlook as well as WebEx Connect.

Microsoft is launching competitive offerings based on its Office Communications Server 2007, Office Communicator and Outlook, and its Office Live solution specifically is targeted at WebOffice.

Other competitors include Klir Analytics, which offers on-demand monitoring and analytics solutions; RightNow's application/workflow/collaboration solutions via both licensed and on-demand models; Salesforce.com's on-demand collaborative workspace focused on sales processes; and Google, which is launching a comprehensive suite of online, on-demand applications.

Key Ramifications

Takes Cisco not “into the software market,” but into SaaS. In the wake of the Cisco-WebEx announcement many in the media and analyst spheres have been crowing, “Cisco is not just in hardware anymore, now it's in software, too.” Those proclamations are about a decade too late. In 1998 the company launched its Cisco Provisioning Center (CPC), a service activation system that provisions Layer 2/Layer 3 across Cisco networks for frame relay, VPN and other network services. CPC is an OEM of NetProvision Activator, the flagship product of Syndesis (which was recently acquired by revenue assurance provider Subex Azure). Today Cisco's large and growing software portfolio includes CiscoWorks, Broadband Management, IP Solution Center, the extensive IOS product line, and more than 50 other products and product families. Cisco also holds investment stakes in a number of software companies, some of which were members of its Cisco Ecosystem alliance program in the operations/business support systems (OSS/BSS) market. So while its acquisition of WebEx certainly takes Cisco in a new direction, it is not Cisco's first substantive foray into the software market. What makes this acquisition most relevant is that it marks Cisco's entry into the software as a service (SaaS) market.

Goes head-to-head with Microsoft, Google, RightNow, Salesforce.com, Klir and anyone offering on-demand applications. With this acquisition Cisco gains instant entrée into the growing market for integrated videoconferencing,

With Cisco's entry into the software as a service (SaaS) sweepstakes, this is an appropriate forum to present a list of the top 10 reasons to consider SaaS:

1. **Rapid implementation.** There is no faster way to get started with a new software application than to take advantage of a professionally run service. Even complex business process-oriented applications can be ready to go in less than 30 days.
2. **Lower capex.** Implementation costs are significantly lower than developing custom solutions or purchasing and installing proprietary software and hardware.
3. **Lower opex.** The SaaS model spreads infrastructure, development, maintenance and future innovation costs across a broad base of users.
4. **Reliable cost forecasting.** Subscription fees are predictable, allowing you to forecast your IT costs over several years. (Reliable sales forecasting for suppliers too, through the recurring revenues associated with subscription services as opposed to the bumpier revenue cycles associated with outright software license sales.)
5. **Ease of access.** Implementations are based on Internet access with browser-based interfaces, making it easy for staff to access the service from anywhere.
6. **24x7 support.** Support staff who specialize in the given application and are available 24x7 can mean significant improvement in end-user assistance over on-premise implementations where the support function is spread across internal IT staff and remote vendor support for software-related issues.
7. **Increased reliability.** The infrastructure behind most SaaS offerings consists of professionally run data centers with full system and database redundancy, load balancing and failover, which leads to better availability and performance.
8. **Increased security.** Physical and data security are generally greater than most companies will put in place for on-premise implementations.
9. **Future-proof IT.** Planning and managing upgrades is someone else's problem. You get the benefit of frequent upgrades without the hassle of testing, managing change control or converting data.
10. **Reduced risk.** Low upfront cost, little or no staff time to get going, and an already up and running environment avoids most of the risks of selecting and implementing new software. The project will be on-time, there will be no hardware costs or other infrastructure surprises, and if it's not the right software you won't be walking away from a big investment if you choose to make a switch.

on-demand applications, collaborative workspaces and multi-mode messaging. Better still, rather than "starting small and working its way up the ladder," Cisco has bought the acknowledged videoconferencing and collaboration market leader—whose company name has nearly joined the ranks of product names such as Kleenex that fell into generic use because the products were so widely used that they became synonymous with the service itself.

Does indeed open a potentially lucrative new revenue stream beyond its equipment revenue base. The maturing market for routers and switches flies in the face of Cisco's ambitious annual 10-15% revenue growth targets, and it's a smart strategic move to seek out other markets that offer more

upside. The burgeoning market for integrated videoconferencing, on-demand apps, online collaboration and messaging fits the bill, and should enable Cisco to leverage its equipment in emerging markets.

EMA's Perspective

For the better part of the past two decades Cisco has been relatively comfortable in its skin as a network equipment manufacturer (NEM) whose Cisco Powered Networks now "power the Internet," and an active software provider from CPC to IOS. In recent years it reigned as the #1 NEM and John Chambers joined fellow industry luminaries Bill Gates and Larry Ellison as three of the market's top opinion leaders (the fourth being Scott McNealy). Two things changed for Cisco in recent years: first its equipment sales (and to be fair, those of most other NEMs) slowed, reflecting overbuilt capacity, particularly IP networks, as demand for IP-based services has yet to catch up. Then in 2006 the trans-Atlantic merger of Alcatel and Lucent toppled Cisco from the NEM top spot. A perhaps wizened, perhaps merely pragmatic Cisco now views the network as a platform for communications and collaboration. Combining WebEx's technology and services portfolio with Cisco's own Call Manager, Unified Presence Server and MeetingPlace products—plus WebEx's subscription-based service model—complements Cisco's Unified Communications strategy to bundle mobile, Internet and other services into a single system. The acquisition also gives Cisco an effective new way to expand beyond (below?) its normal sales profile among large enterprises to now crack the SMB market.

EMA believes this move is both an announcement of Cisco's entry into and a high-profile validation of software as a service (SaaS), a model of software delivery where customers access network-based software that has variously been known as hosted software, service bureau (in the 1980s) and ASP (in the 1990s) and is now referred to as on-demand software. Other current SaaS offerings include SalesForce.com and SalesNet for CRM, analytics and monitoring from Klir, Google's productivity and communications suite or any of the free online e-mail systems like YahooMail or Gmail. They also include the lineup of Office applications and delivery frameworks Microsoft is currently crafting into a coherent entry in this market. While Microsoft is still assembling its offering, with a stroke of the pen Cisco has gone to the head of the class. Yet making the grade will hinge on three factors over the next 18 months:

The network is the medium. Microsoft may be the end user business applications king, but Cisco's vast experience delivering integrated hardware + software solutions is ideal preparation for creating the right combination of Cisco and WebEx software and network components to deliver

integrated communications services. Cisco is accustomed to helping service providers deliver the venerable “five 9s of reliability” to their own end customers; Microsoft’s reputation has been earned more through innovation and ubiquitous application availability and less due to stellar reliability. ADVANTAGE: Cisco

Hearts and minds of users. Shout-from-the-rooftops anti-Microsoft zealots—or anyone who has ever had Windows crash for no apparent reason—may find this hard to believe, but Microsoft is and may always be a user-driven company to which the intricacies of the GUI and the total user experience are second nature. Cisco is and may always be a denizen of the network, one step removed from where users live and breathe. Yet its acquisition of WebEx may put it in squarely in the sweet spot of where those total user experiences are headed. ADVANTAGE: push

Documents may dictate. Microsoft Office is the most widely-used suite of business and personal productivity solutions in the world, and at most companies when talk turns to on-demand applications it most commonly centers on Microsoft Office applications. As further proof, one promising sector of the enterprise asset management market is currently owned by companies whose systems dynamically allocate and reallocate a limited pool of software licenses (most commonly Microsoft licenses) across the corporation based on frequency and immediacy of usage. In short, Microsoft may own the SaaS space by virtue of owning the software that the majority of users want to access as a service. ADVANTAGE: Microsoft



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