Understanding Total Cost of Ownership (TCO)

| MAXIMIZER CRM

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One of the biggest concerns associated with cloud CRM is the long-term total cost of ownership. Use this guide to calculate and set your budget.

Why look at the TCO for CRM systems?

As cloud computing has emerged as a growing preference over the last couple of years, for businesses of all sizes implementing or upgrading a CRM system, most companies think they have a pretty clear grasp of the facts when it comes to deciding between a cloud and an on-premise system. However, you have to do the legwork if you want to do what's right for your business. So how do you approach a comparison between the two?

When deciding which CRM system is best for your business, it is a great idea to evaluate the Total Cost of Ownership (TCO) of the options available, estimating the total costs incurred over a set period of time across the different offers being proposed. CRM solutions have a much larger total cost than just the purchase or rental of the software and so a business looking at upgrading or implementing CRM for the first time should look beyond the base cost of the software for a given number of users and factor in elements such as the level of customization, the system complexity, the cost of deployment, the potential for reduced IT resources and the expected system lifespan.

"With the continual rise of cloud computing, doing a TCO has proven to be incredibly useful for businesses selecting CRM systems."

Typically, a TCO analysis will show a significant difference between the initial price of something and its wider long-term cost, by taking into account factors such as staff, space, equipment and other extra expenses. With the continual rise of cloud computing, doing a TCO has proven to be incredibly useful for businesses selecting CRM systems - it has meant that there was a real alternative for companies wary of the commitment and up-front investment necessary with an on-premise solution.

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Thus the emerging choice in CRM over the last few years has been between two options: a total cloud solution, where the data is hosted and the CRM software is used on subscription basis (otherwise known as Software as a Service or SaaS) or a fully-owned on-premise model, with the business acquiring a number of licences and most aspects being fully managed in-house by an IT team. For businesses of all sizes, adopting cloud-based applications has become an increasingly attractive proposition, particularly for Small and Medium Enterprises (SMEs), which are often looking for scalability, flexibility and value for investment in their quest to boost productivity and drive revenues, without the associated expensive hardware, operating system and database purchase.

However, as Web-based technology has developed, the comparison is no longer simply between a traditional cloud and on-premise model. CRM vendors have become a lot more flexible, offering a selection of solutions that provide elements of both on-premise and cloud to suit the exact needs of your company. Companies can now have the option of a subscription-based CRM solution still storing the data on-premise for added security, or they can purchase the CRM software while storing the data on the cloud for added flexibility. It depends on the needs of the business.

The costs of each of these can be gauged with a TCO analysis. By providing a realistic measurement of the long-term costs for each of your preferred options, a TCO analysis allows businesses to quickly see which solution will fit their budget best and supply the expected Return on Investment (ROI).

The battle between cloud and on-premise

The competition between cloud and onpremise enterprise solutions has seen the cloud side of the equation steadily rise in recent years. The latest Gartner figures show that 41% of CRM systems are now SaaS-based[1], up from 35% in 2012[2], and that figure is expected to grow to more than 50% in 2015[3].

Conventional wisdom is that the long-term cost of cloud exceeds that of on-premise, but most businesses don't just want to rely on popular belief – they want numbers.

[1] Louis Columbus, Gartner CRM Market Share Update: 41% of CRM Systems Are SaaS-based, Forbes, 6 May 2014

[2] Louis Columbus, Gartner Hype Cycle for CRM Sales, 2012: Sales Turns to the Cloud for Quick Relief, Forbes, 27 July 2012

[3] Louis Columbus, Gartner Predicts by 2015, More Than 50% of CRM Will Be Deployed as SaaS, Forbes 28 May 2015

The good news is somebody has in fact run the basic numbers. It has been a few years since The Yankee Group carried out its landmark TCO study on hosted CRM systems versus on-premise solutions for SMEs, but it still sheds valuable light on the debate over cloud versus on-premise and even shatters a few myths[4]. The 2005 study concluded that on-premise CRM solutions were considerably more expensive over the course of a five-year period than cloud-based alternatives.

"On-premise CRM solutions were considerably more expensive over the course of a five-year period."

Contrary to prevailing sentiment, on-premise systems were also shown to be more expensive to operate annually than their cloud-based counterpart. Generally, the operating costs of servers and infrastructure are shared in a cloud environment across multiple customers. In an on-premise world, the equipment is purchased by a company, although an asset is also in effect a liability, –as equipment needs regular maintenance in terms of hardware as well as operating system, anti-virus, malware and third party tools.

Here are the key advantages for a cloud solution, found by The Yankee Report:

- Faster implementation and ramp-up time to productive use of applications
- Lower upfront and ongoing costs
- No additional IT infrastructure for servers, networks, storage and IT resources to support them
- No additional IT application support staff
- Guaranteed service-level agreements (SLAs)
- Vendors provide an enterprise-class infrastructure with appropriate servers, networking and storage systems; plus, they are responsible for frequent upgrade application with each new version release, regular customer data backups and required restores, as well as meeting the latest security and compliance requirements.

The Yankee Group analyzed the TCO for a cloud and on-premise solution over a five-year period, looking at both 20 users and 100 users (see graph).

Percentage of CRM systems that are cloud (source: Gartner and Forbes)
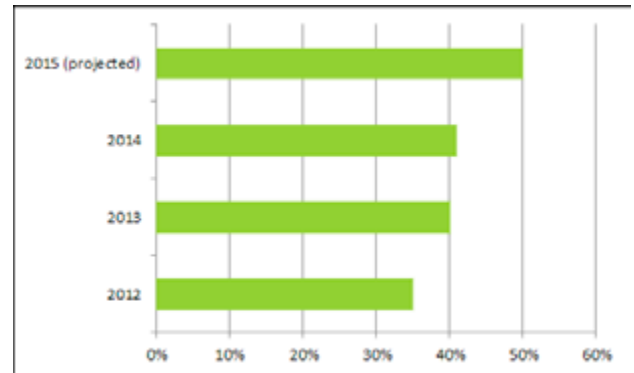
TCO (USD) over a five-year period (source: The Yankee Group)
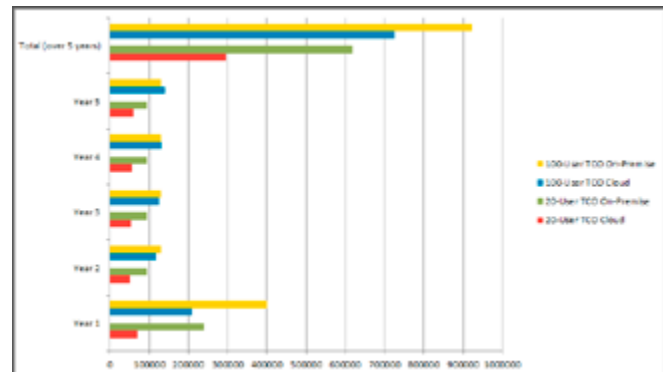
[4] Sangeev Aggarwal, TCO of On-Demand Applications Is Significantly Better for DMBs and Mid-Market Enterprises, The Yankee Group Decision Note, 1 June 2005

On-premise CRM is not without its advantages, but The Yankee Group did not see TCO as one of them – at least for SMEs. The main draw for on-premise is that it gives users full control over software and hardware, with their own staff maintaining the system and taking responsibility for the security and backups – not to mention guarding against and handling service disruptions. Having an on-premise system can be easier to integrate with other in-house software, which can be a major benefit for some businesses.

However, the biggest drawback for an on-premise system is without a doubt the initial start-up cost. With this type of system, the costs do not stop once it has been paid for, installed and configured. Ongoing costs begin to mount and support and staff need to be taken into account. IT departments for smaller businesses are more likely to have limited resources than those of a cloud vendor and, therefore, can be less secure with a more fractured reliability than the cloud alternative.

"Cloud offered a substantial TCO advantage over a four year period."

A more recent study carried out by consulting, market research and analyst firm, Hurwitz & Associates[5], corroborated the The Yankeee Group findings, confirming that cloud offered a substantial TCO advantage over a four-year period. The research firm's analysis for a business with 100 users revealed that cloud CRM costs were still less on an annual basis than an on-premise solution, even after the first year.

The report looked at the comparative TCOs for three different sizes of user groups and found significant savings for a whole range of SMEs (see graphs on pages 6 and 7).

Overall, TCO for a cloud-based integrated solution suite was shown to be significantly lower than the comparable on-premise solution:

For a company with 100 users, the total cost for the cloud-based system amounted to $697,656, while the total cost for the on-premise solution was a staggering $1,400,570 over the four-year period, with more factors to take into account and IT resources taking up a large chunk of the outlay.

5   Sangeev Aggarwal and Laurie McCabe, The Compelling TCO Case for Cloud Computing in SMB and Mid-Market Enterprises, A Hurwitz White Paper, 2009

Hurwitz & Associates also calculated the cost percentage for both systems (see graphs below).

The research also showed that as the number of users increased, the TCO advantage of cloud reduced – from 55% for 52 users, to 50% for 100 users, to 35% for 200 users – however, a 200 user company could still make substantial savings with a cloud based system (see graph on page 7).

Recommendations for an effective TCO model

When considering a TCO model, the pioneering landmark study on TCO for CRM systems by The Yankee Group states it is important to evaluate the cost over a three-year to five-year period. The main factors to consider, according to The Yankee Group, are:

- Licence – subscription costs versus licence costs for an equivalent number of users

- Installation and implementation – costs for design and configuration; initial customization costs need to be taken into account

- Staff – if you plan on installing and running your CRM within your own IT environment, don't forget the additional IT costs for skilled staff; admin training and user training are ongoing costs that a cloud system can eradicate

- Maintenance and support – in terms of value, the ongoing support and maintenance from a cloud vendor is often underestimated; software can malfunction and vendors can enhance data security and maintain backups.

- IT infrastructure – hardware, software, support, power and energy; cloud-based CRM systems do not incur these costs as vendors take control of this.

On-premise must take into account operating systems, backup software, security and maintenance; server storage space can also add to the cost.
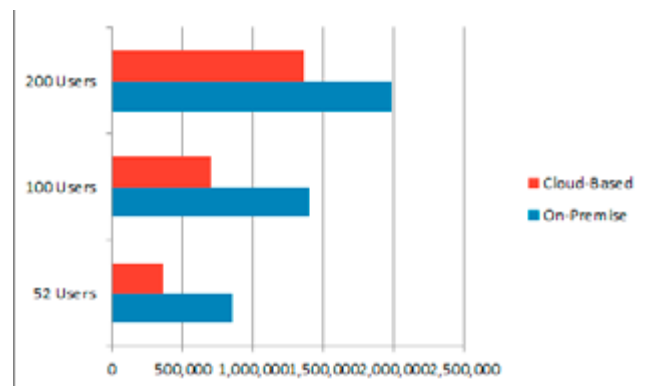
TCO calculation for an on-premise solution over a four-year period (source: Hurwitz & Associates)
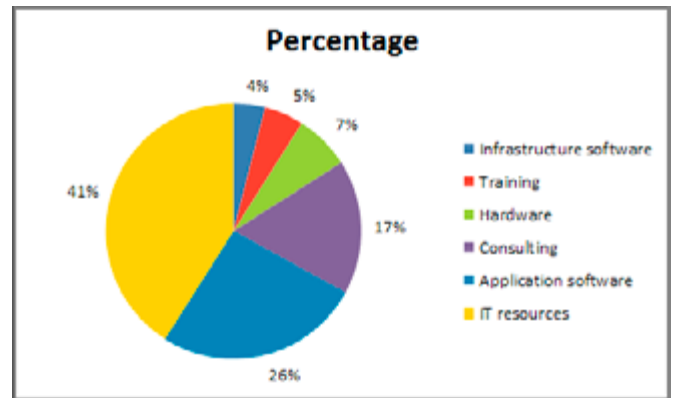
TCO calculation for a cloud-based solution over a four-year period (source: Hurwitz & Associates)
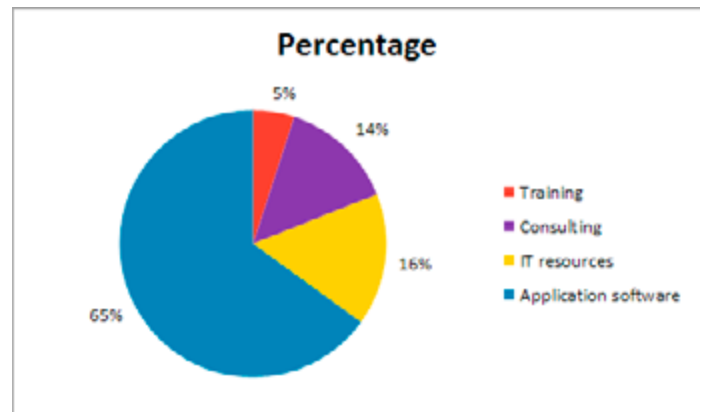
TCO comparison in ($) for 52-user, 100-user and 200-user companies over four-year period (source: Hurwitz & Associates)

## Other factors to consider when making an informed decision

Once you've looked at TCO, you then need to take a look at the big picture, thinking about your business, its size and the strategic planning. Here are some of the key points other than TCO to consider, that could be evident in both cloud and on-premise CRM solutions, depending on the product:

- Scalability – the ability to scale up and down is invaluable as businesses respond to the changes in the marketplace and to other economic factors. SMEs can respond to growth quickly and maintain profitability whilst doing so
- Reliability – the reliability of the vendor must be researched if choosing a cloud-based server: users want a highly accessible and reliable system at all times
- Mobility – being able to access your CRM remotely, via smartphone, tablet, laptop etc. enables users to interact with customer data, whenever and wherever they are
- Functionality – businesses need to review their current internal processes and practices and select a CRM system with the functionality to enhance and drive effeciencies
- Contract terms – service level agreements (SLA) and the length of a contract are important factors to consider
- Data security – any concerns should be addressed upfront and a security SLA also agreed upon.

Other options

As highlighted earlier in this document, there are a multitude of options now available. Some companies feel restricted by compliance rules or the security requirements of clients or partner
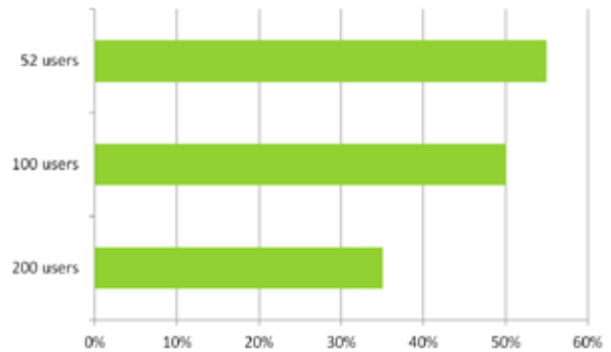
companies and may initially look only at an on-premise solution. However, even a company with very strict security rules can tap into the cloud's benefits through the 'private cloud' – where your company has a dedicated server that can even actually be on-premise, but is maintained by a cloud provider – and other options that give you the best of both worlds.

There are a number of combinations beyond basic cloud and on-premise solutions. You can have web-based CRM applications that are deployed in-house on a monthly subscription basis, so that the data is on-premise, but you still save on the up-front investment in software, maintaining full online accessibility. Another option is the up-front purchase of the CRM software, which can then be deployed in your own dedicated hosted environment or private cloud – meaning you still get web accessibility, but with added flexibility, where you can deploy other business applications alongside your CRM in an exclusive hosting environment. You can also subscribe to software on a SaaS basis from the vendor – with all the advantages of upgrades, flexibility, etc. – while a geographically local partner company actually

hosts the data, which is particularly useful in operations where local regulations require the data be held in-country. This solution also enables your firm to store other cloud software on the same hosted server.

It has to be noted that using public cloud is not associated with a higher degree of data risk, but some companies feel more secure handling sensitive information within a virtual private network. Some even opt for a combination of hosted and proprietary database solutions to build in further redundancy and contingency planning.

Conclusion

A good CRM system takes very little time to update, has the features and functions your company needs to grow and be more productive and, most importantly, generate a healthy ROI – at a low total cost over the long term. Understanding TCO and doing your own analysis is critical to understanding which type of system fits those criteria. Although one size does not fit all, for many companies cloud computing CRM solutions can help organizations to achieve these requirements and provide added flexibility to scale up or down as and when business demands require – a key for many SMEs looking to leave themselves open to rapid and unexpected growth, while protecting their business from economic shocks and other sudden crises.

Budgeting Tool

On premise 5 year costs

	Year 1	Year 2	Year 3	Year 4	Year 5	Total Cost over 5 years
Purchase costs						
Implementation, Customisation and Integration						
Application Support and Maintenance (from vendor)						
Host Server Computers and Maintenance						
IT Infrastructre (including Internet access)						
End-User Support and Administration						
User Training						
Cloud TCO Per Year						
Cumulative TCO						

Cloud-based solution 5 year costs

	Year 1	Year 2	Year 3	Year 4	Year 5	Total Cost over 5 years
Purchase costs						
Implementation, Customisation and Integration						
Application Support and Maintenance (from vendor)						
Host Server Computers and Maintenance						
IT Infrastructre (including internet access)						
End-User Support and Administration						
User Training						
Cloud TCO Per Year						
Cumulative TCO						

About Maximizer

Maximizer CRM is fueling the growth of businesses around the world.

Our CRM solutions come fully loaded with the core Sales, Marketing and Service functionality companies need to optimize sales productivity, accelerate marketing and improve customer service. With flexible on-premise, our cloud and your cloud deployment options, tailored-to-fit flexibility, state-of-the art security infrastructure, industry-specific editions and anywhere/anytime mobile access, Maximizer is the affordable CRM solution of choice.

From offices in North America, Europe, Middle East, Africa and AsiaPac, and a worldwide network of certified business partners, Maximizer has shipped over one million licenses to more than 120,000 customers worldwide.

MAXIMIZERCRM

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