

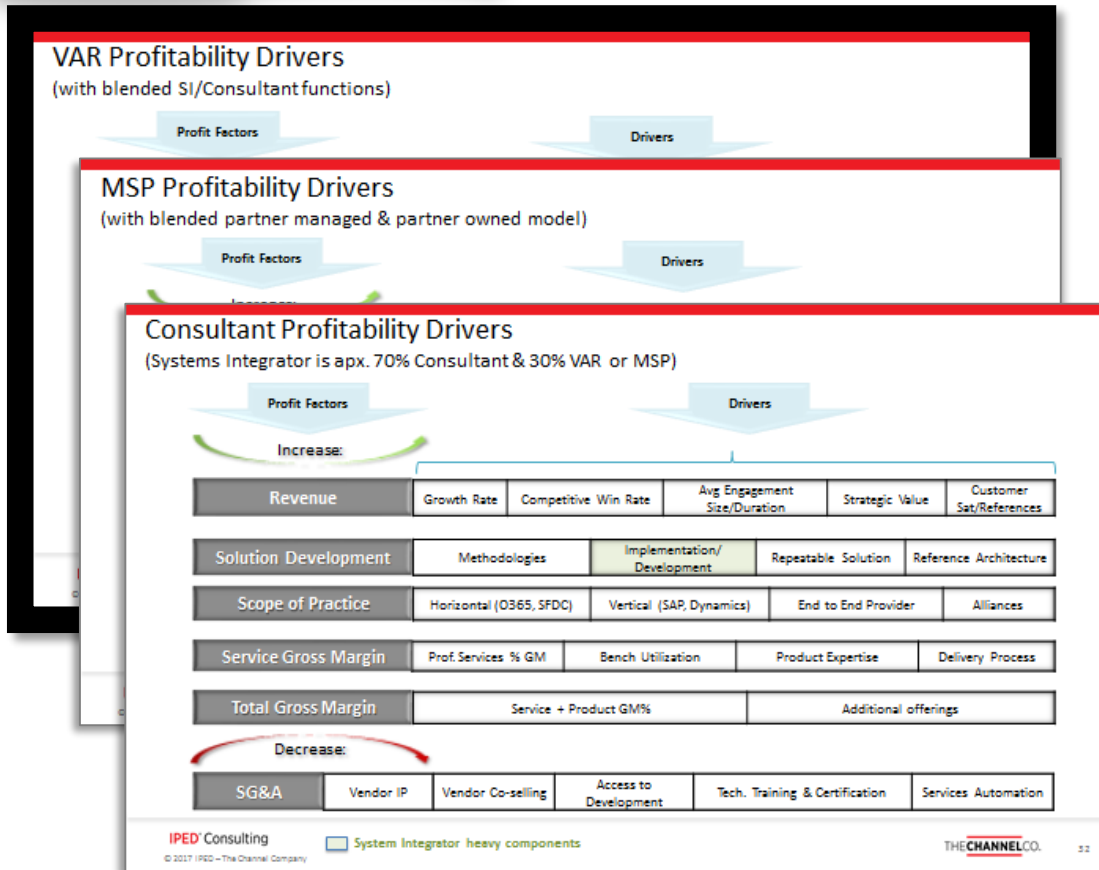
# The State of VAR Profitability

Research Review and Discussion

Continuing Education for IPED Channel Masters

# Three pure-play models from which you can have a granular view of profitability and benchmark your program

## Partner Profitability



## Vendor Support Needs

**Lever of Partner Profitability: VAR**

Partner P&L Levers	Type	Vendor Tools / Resources
	Increase Revenue	Stronger sales tools 23%

**Lever of Partner Profitability: MSP**

Partner P&L Levers	Type	Vendor Tools / Resources
	Increase Revenue	Offer utility based or consumption based pricing 53%
	Decrease SG&A	More marketing visibility as part of vendors MSP partner ecosystem 38%

**Lever of Partner Profitability: Consultant/Systems Integrator**

Partner P&L Levers	Type	Vendor Tools / Resources
<b>SOLUTION DEVELOPMENT</b>		
Intellectual Property	Increase REVENUE	More IP to help us Architect Next-Generation Services 34%
<b>DELIVERY EFFICIENCY</b>		
Service Delivery Tools	Decrease COGS	Better Access to Service Delivery Tools, Best Practices (Architectures, SOWs, Integration Guides) 30%
<b>STAFFING</b>		
Resources and Development	Decrease SG&A	Easier Access to Field SEs for Joint Engagement 43%
	Decrease COGS	Field Mentoring for Consultants 35%
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Sales Process Program	Decrease COGS	Help us Get Access to Certified Technical Talent to Expand our Bench 29%
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<b>COST OF SALES</b>		
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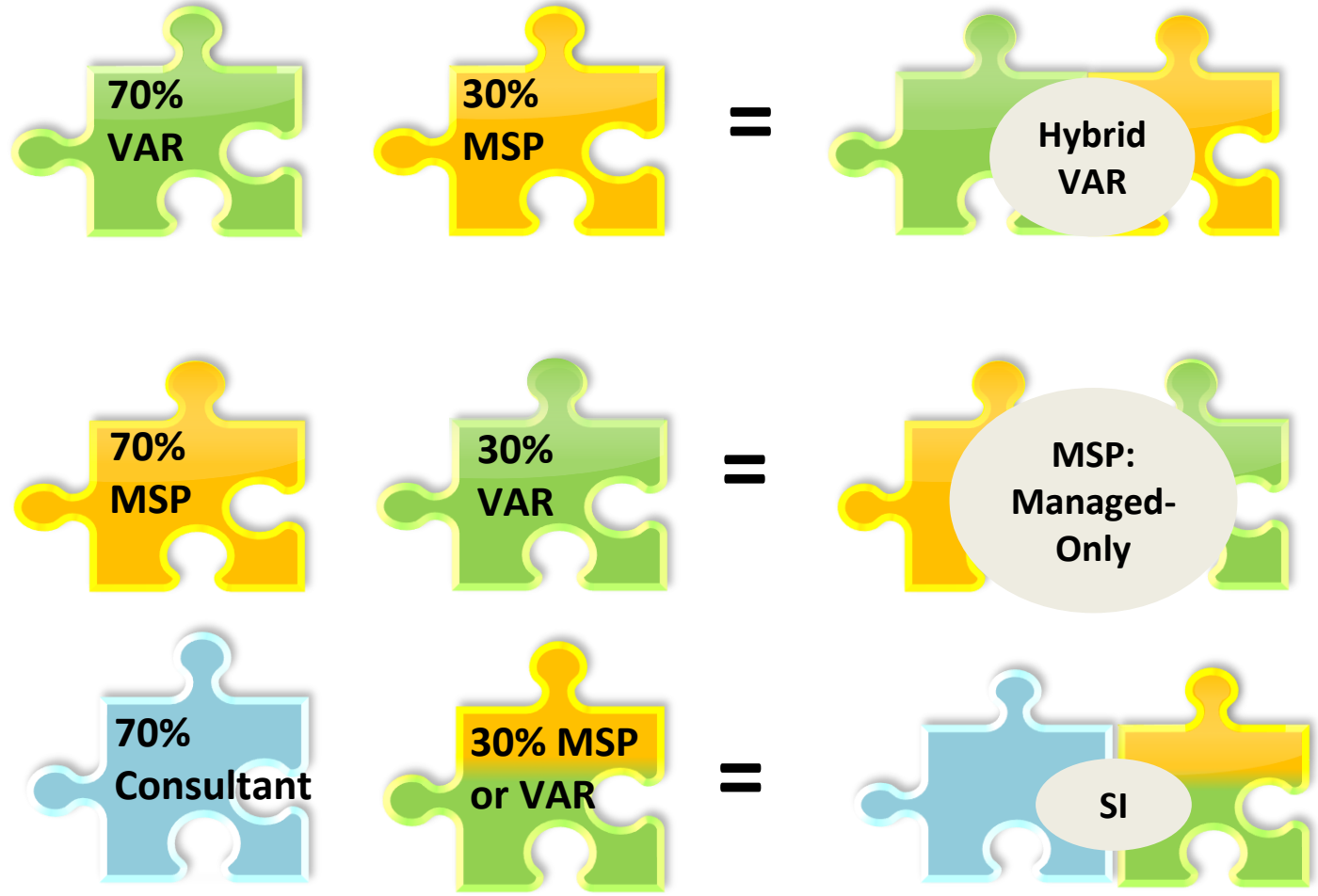
REVENUE  
C.O.G.S.  
SG&A

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# Why role-based programs matter: hybrid business models

## How to Use These Models:

- Dissect your ideal partner profile
- VAR, MSP and Consultant models are the 3 pureplay roles
- Factor in the correct percentage of the 3 pure models to achieve the hybrid mix of your ideal partner profile
- Then benchmark partner needs to your program



- Illustrative -

# IPED Consultant



**Jeff Hine**



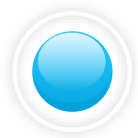
*IPED Consultant & Writer*

## **Perspectives On:**

- ✓ Partner business models & economics
- ✓ Consulting business dynamics
- ✓ Building & running a professional services practice

## **Professional History:**

- Consultant / Analyst – ESG Group
- Director, Partner Alliances - Glasshouse Tech.
- VP, Professional Services – Avamar Technologies
- Client Director – EMC
- Director of Marketing & Prof. Services – Articulent/Berkshire
- Product Marketing - Digital Equipment Corp.

-  **Strategic Backdrop for Profitability**
-  **Dissecting VAR Profit and Expenses**
-  **Refining the Value Proposition Around Profitability**

# Start with your relative position ....

## Strategic

We are generating a significant amount of revenue with these technology suppliers and are highly involved with them at the sales, marketing and technical levels

## Tactical

We generate a significant amount of revenue with these technology suppliers, but product alternatives exist and we are not strategically invested in these lines

## Opportunistic

We infrequently buy small amount of products from these technology suppliers, and re-actively based on our customers' demands



# The impact of profitability: then and now

# S U C C E S S

## THEN – “Profitable”

- Gross margins
- New customers
- Professional Services growth
- Solvency

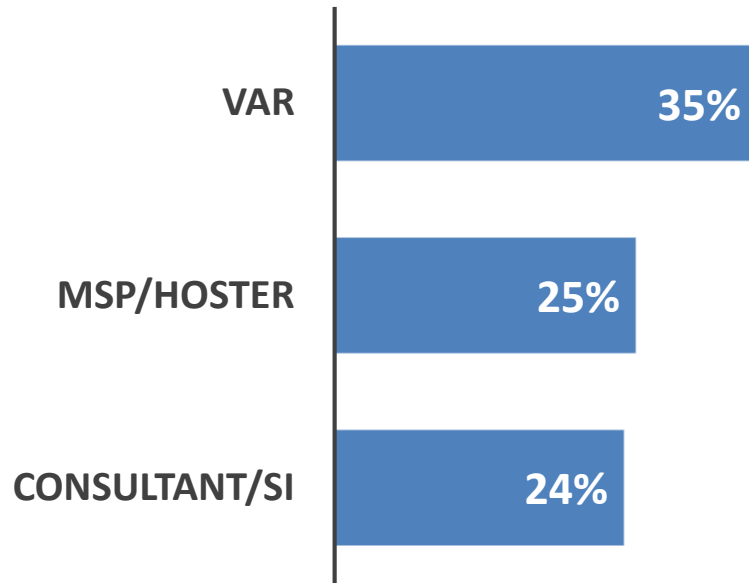


## NOW – “Valuable”

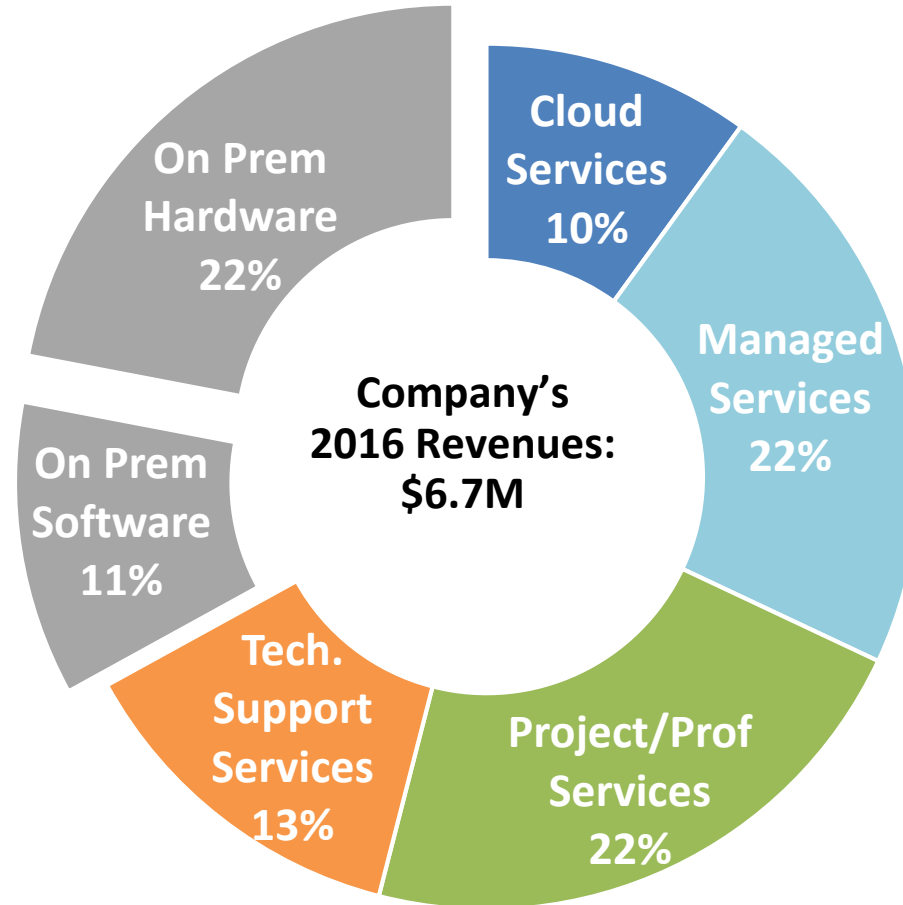
- Intellectual property
- Monthly recurring revenues
- Customer retention and expansion rates
- Vertical insights and LOB relationships
- Services diversity

# Respondents are hybrid VARs and MSP/Consultants leading with professional and managed services, then on-premise hardware

Primary Business Models



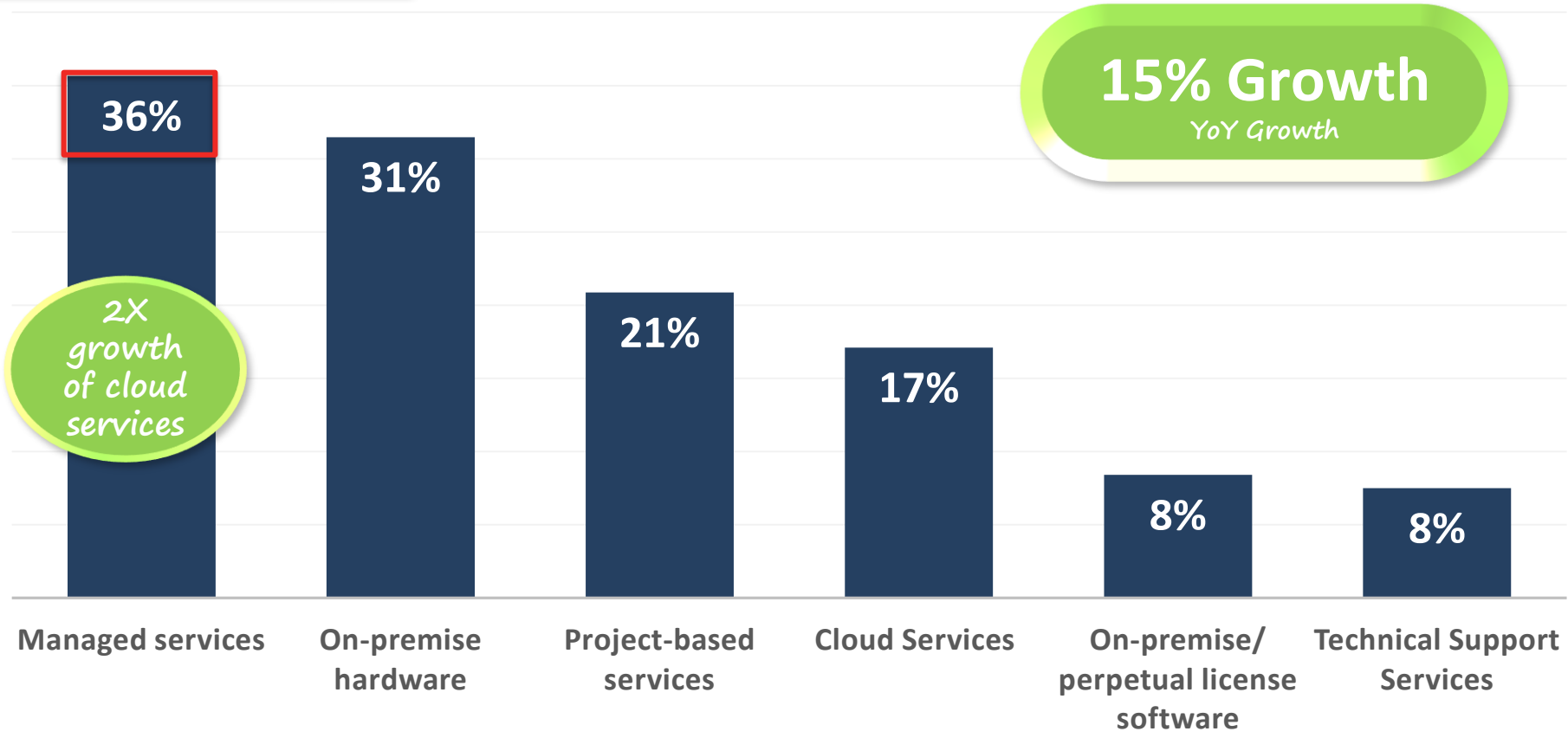
Revenue





# Respondents grew 15% in topline sales; plan to drive topline growth from MSP services and on-premise hardware sales

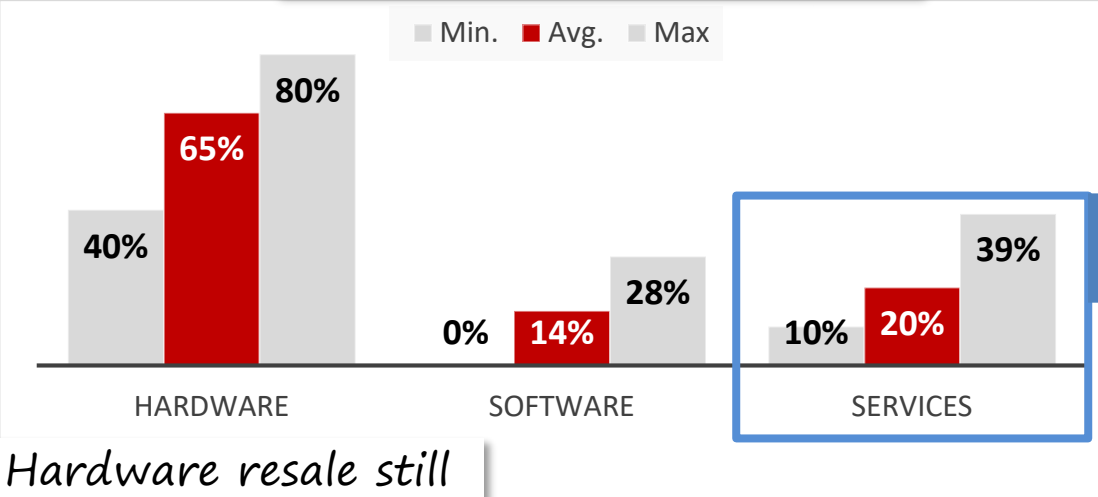
## Growth Impact Ranking



Q: From which categories do you expect to gain the majority of your topline sales growth in 2017? (Please rank in order of source of growth)

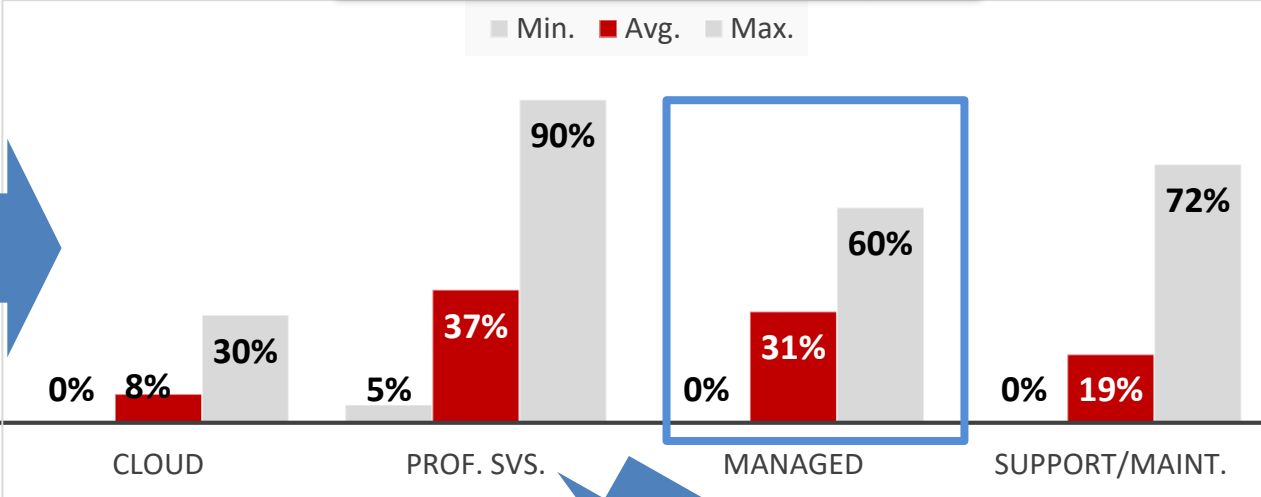
# Revenue Mix: VARs

## MIX OF TOTAL REVENUES



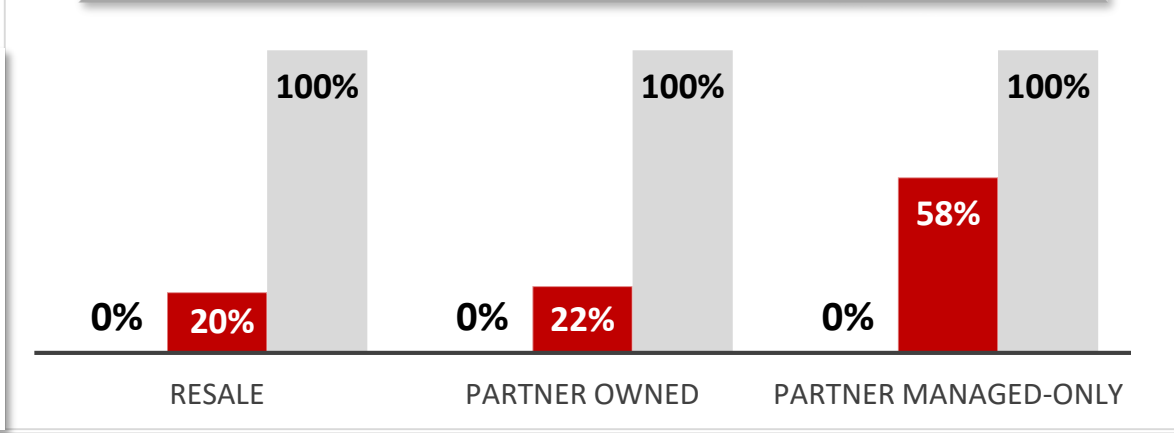
Hardware resale still dominate revenues

## SERVICES MIX - % of REVENUE



Professional services remains leading services element, with managed services close behind

## MANAGED SERVICES REVENUE by DELIVERY TYPE



Reselling managed services alone yields insufficient margins.

VARs don't frequently own hosting infrastructure

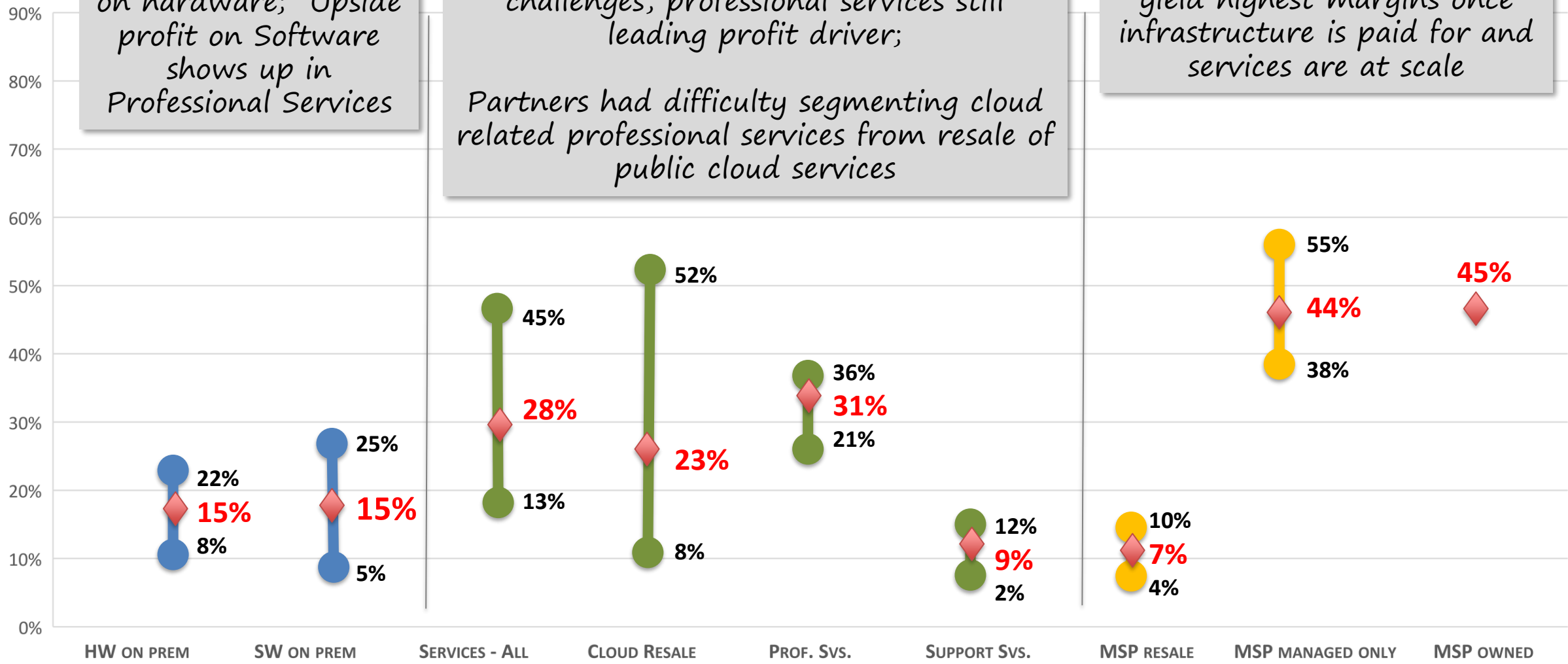
# Gross Margin Ranges: VARs



Wide range of profits on hardware; Upside profit on Software shows up in Professional Services

Despite scalability and utilization challenges, professional services still leading profit driver; Partners had difficulty segmenting cloud related professional services from resale of public cloud services

MSP owned services only yield highest margins once infrastructure is paid for and services are at scale



# MSP portion of VAR business is focused largely on Partner-Managed Services

**MSP**

*“Our revenue mix used to be 25% recurring and 75% project services mix; but it’s got to be at least 30% plus recurring. This allows me to cover costs with recurring revenues.”*

% of MRR revenues

**21%**

**Resale**

- Resold another supplier or service providers’ managed services

**25% GM** 

**61%**

**Partner Managed-Only**

- Partner manages customer’s asset (*on customer premise, at someone else’s datacenter or on a public cloud*)

**50% GM** 

**18%**

**Partner Owned**

- Offered your own hosting services on your own data center and managed for a customer

**50-60% GM** 

*Q: Thinking specifically about your Managed Services business in 2015, what % of your total managed services revenue came from each of the following types of services? (n=207)*











# VAR: Top Revenue Producing Product Categories



## Takeaways:

- Client security software overtakes client hardware devices - common segue to building out an MSP practice
- PCs and client devices still a staple of many solutions, but VARs continue to see margin pressure on volume hardware
- Flash technologies have bolstered sales momentum around NAS storage solutions
- Many VARs have refocused their efforts on server virtualization






## Top 5

		<u>GM Trend</u>
1.	 Client security software (firewall, anti-SPAM, anti-virus)	
2.	 PC's/Notebooks/Mobile Computers	
3.	 Enterprise Networking Infrastructure	
4.	 Enterprise Network Storage	
5.	 Mid-Range Servers	

# VAR: Top Gross Margin Producing Product Categories

Est. GM%

## Top 5

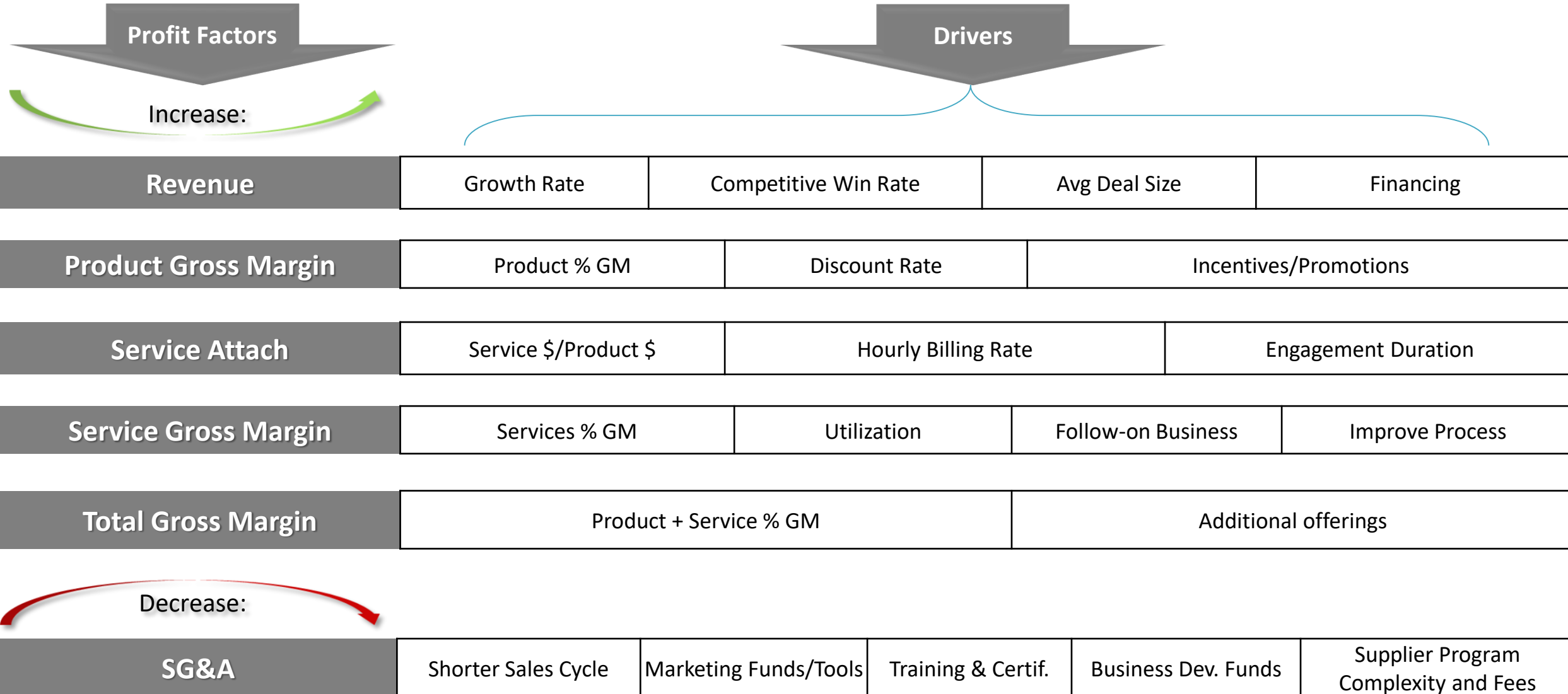
1.		Business Analytics	30%
2.		Client Security Software	22%
3.		Collaboration Software	22%
4.		Network Security Appliances	22%
5.		Converged Infrastructure Systems	21%



### Takeaways:

- Business analytic solutions carry the highest gross margins; on par with professional services margins
- Highest margin product categories all in software group
- Volume compute devices carry the lowest gross margins

# VAR Profitability Drivers



# VAR Profitability Drivers: Key Trends

Increase:

## Revenue

- **Revenue volume up, margins down, overall profitability healthy but not keeping up with financial growth**
- More qualified pre-sales staff and consultants result in better services scoping = higher profits

## Product Gross Margin

- **Continued margin pressure on volume hardware**
- Highest gross margin product categories are analytics, security, collaboration SW and networking appliances
- Product with fastest declining gross margins are PCs/notebooks, volume servers and processors

## Service Attach

- **Professional Services increasingly priced as stand-alone for pre-sales design/assessment; resale must be bundled with professional services to make meaningful profit**
- Despite staffing challenges, Residency Services is a common offering; trying to evolve to a managed service

## Service Gross Margin

- **Cloud (public) resale margins alone insufficient to sustain practice; must broker, add professional services**
- With large professional services deals margins are down due to the number of people required to staff the deal

Decrease:

## SG&A

- **Services bench utilization still plays large role in realizing services profitability; vendor IP sharing & mentoring can ease this cost burden**
- Cost of facilities remains significant factor, esp. as expanding sales staff and considering DC build-out
- Tighter MDF usage rules are increasing staffing expense; non-MDF opex investment remains low



# Levers Of Partner Profitability – VARs: Vendor Support Requirements

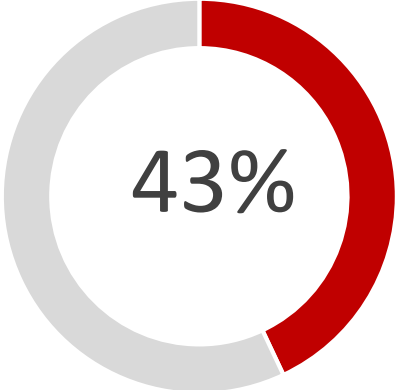
**REVENUE**

**C.O.G.S.**

**SG&A**

Partner P&L Levers	Type	Vendor Tools / Resources
Sales Velocity	Increase Revenue	Stronger sales tools <b>23%</b>
	Increase Revenue	Ability to sell renewals of support contracts <b>22%</b>
	Increase Revenue	Extended financing for our customers <b>18%</b>
Buying Power	Decrease COGS	Ways to earn higher discounts on resale <b>34%</b>
	Decrease COGS	More lucrative front-end incentives for deal registrations <b>75%</b>
	Decrease COGS	More lucrative performance based back-end rebates <b>19%</b>
Service Delivery Capabilities	Decrease SG&A	More IP to help us build next generation services <b>13%</b>
	Decrease SG&A	Field based co-selling resources <b>7%</b>
Vendor Enablement and Transaction Support (Program)	Decrease SG&A	Make training and certification more affordable <b>56%</b>
	Decrease SG&A	Reduce/Eliminate Channel/Alliance Program Fees <b>45%</b>
	Decrease SG&A	<ul style="list-style-type: none"> <li>Automate more of the core channel processes <b>26%</b></li> <li>Make programs less complex &amp; time-consuming to administer <b>23%</b></li> <li>Make quoting, pricing and transactional process less complex <b>23%</b></li> </ul>
	Decrease SG&A	<ul style="list-style-type: none"> <li>Make marketing funds easier to get access to <b>20%</b></li> </ul>

# All major SG&A expenses up



Say **longer selling cycles** have increased their selling costs most

- Different decision makers
- Unpredictable customer demand

## All 11 Major SG&A Expense Lines INCREASED

(71 – 92% response)

**Top 4  
Greatest  
Changes**

**1**

Technical staff



**3**

Business offices



**2**

Sales staffing



**4**

Back-office staff

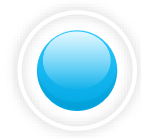


# Solution providers feel only ½ of vendor CAMs understand their profitability



**15%** say

CAM's **fully understand** all the elements of profits and costs



**29%** say

CAM's **understand most of** the margin and cost factors



**21%** say

Say CAM's understanding is **limited to transactional gross margins**



**19%** say

Say CAM's have a **very limited understanding** of both real margins and sales expenses



*Q: To what degree do you feel the channel reps who support you from your top IT vendors understand how you make money with their product line(s)? (n=318)*

# VAR Profitability:



## Key Vendor Takeaways

Know your “Vintage” VARs and understand the impact to regional coverage if they don’t evolve

Reselling *enables growth* in other core solution provider functions; growth of managed and professional services

VARs with local *vertical specialties* will continue to be more profitable and are first-movers for building cloud and MSP capabilities beyond resale

*Software platform*, analytics or app. dev. skills are critical for VARs to cultivate to differentiate and boost profits

*Complexity = cost*; VARs have the least buffer to net margins when programs impact SG&A expense (e.g., FE margin incentives)

*To ease investment hurdle* on building managed services and/or doing more marketing, vendor licensing and MDF process complexity must change

# Refining the value proposition around profitability



1. Map your *target partner profile* to hybrid business model & profitability drivers
2. Understand the *complete channel economic picture* for your products
3. Tailor your *value proposition* to speak to profitability impact first
4. Continue to *evolve your partner managers* into business managers, with a keen sense of profit & cost drivers

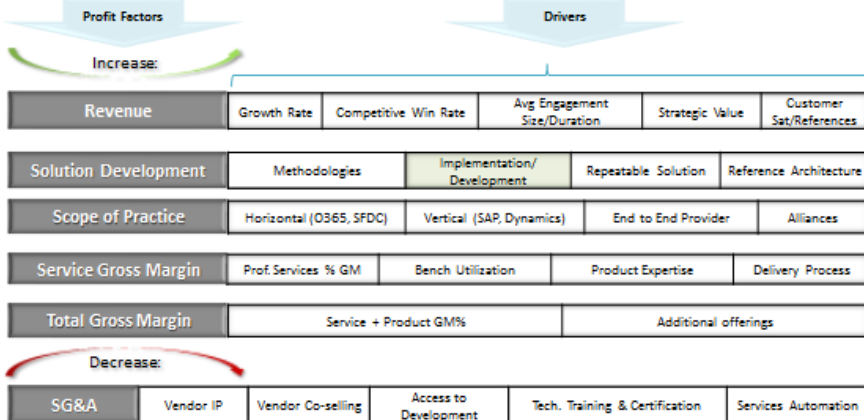
# Three pure-play models from which you can have a granular view of profitability and benchmark your program

## Partner Profitability

VAR Profitability Drivers  
(with blended SI/Consultant functions)

MSP Profitability Drivers  
(with blended partner managed & partner owned model)

Consultant Profitability Drivers  
(Systems Integrator is apx. 70% Consultant & 30% VAR or MSP)



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## Vendor Support Needs

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# Thank You



For More Information Contact:

**Lisa Sabourin**

Director of Engagements

C 561.339.5517

[lsabourin@thechannelco.com](mailto:lsabourin@thechannelco.com)

The Channel Company

[thechannelco.com](http://thechannelco.com)