Market Roundup

March 5, 2004

IBM Pursues Vertical Lift

By Charles King

IBM has announced the Partnerworld Industry Networks for ISVs (PWIN), a new initiative that realigns the company's ISV programs to facilitate the delivery of solutions for specific vertical industries. As part of the initiative, IBM announced new middleware solutions designed to help customers in the financial, healthcare, life sciences, and retail industries integrate, manage, and automate business processes. These new offerings follow similar IBM solutions for the banking and insurance industries, and all contain core middleware technologies from IBM's WebSphere, DB2, Tivoli, Lotus, and Rational brands. Overall, IBM said PWIN would provide ISVs, which the company identified as the fastest growing segment of its $29 billion business partner ecosystem, with a single source for technologies that will help them improve business process performance and develop open, industry specific solutions for multiple computing platforms. Early entrants of PWIN include ISVs in the banking, financial markets, retail, healthcare life sciences, and telecommunications industries such as Apama, DWL, Exstream Software, PureEdge Solutions, Leapstone, Rocksteady Networks, jNETx, Accelrys, Scimagix, CoreMedia, Evant, Yantra, and Cerylion.

The pursuit or creation of market opportunities is a continually evolving exercise for vendors. For IBM, that effort has changed substantially since the company announced some four years ago that it would exit the applications business, leaving the point solutions market to ISVs. That announcement was greeted with initial skepticism both by IBM's competitors and among ISVs, but IBM held to its word and has reaped substantial benefits as a result. What sorts of benefits? First, the decision allowed IBM to focus company efforts on its core hardware and services capabilities, areas where IBM has historically excelled. Second, it provided the impetus and structure for IBM to promote its middleware offerings as logical alternatives to competitors' development environments. But most importantly, the decision helped IBM deepen and strengthen its partner relationships, especially among ISVs who have felt increasing competitive pressure from other platform cum solutions developers such as Microsoft and Oracle.

So how does PWIN fit into the greater IBM universe? First, creating IT markets depends in large part on finding pools of associated businesses so that solutions can be leveraged across multiple sales opportunities. Specific industries provide natural targets for such efforts, as IBM has proved with its vertically-oriented grid computing solutions. Second, by focusing its middleware efforts on such pools of potential customers, IBM is creating opportunities both for its own hardware and service offerings, as well as for its ISV partners' value-adding products. Synergy, an interaction of two forces wherein their combined effort is greater than the sum of their parts, is often portrayed as the happy result of chance encounters. Overall, we believe that IBM's ongoing efforts at building relationships with and opportunities for ISVs stand as an example of how synergies can be created by design. In that scenario, PWIN stands as yet another building block IBM can use to build its own and its partners' future success.

The Sageza Group, Inc.
32108 Alvarado Blvd #354
Union City, CA 94587
650·390·0700 fax 650·649·2302
London +44 (0) 20·7900·2819
Milan +39 02·9544·1646

Internet Sales Tax Redux

By Jim Balderston

Some twenty states are including lines on state income tax forms that ask taxpayers to reveal how much they spent on out-of-state purchases, including those made over the Internet. The amount each taxpayer declares would then be used to calculate the amount of sales tax revenue that is owed the particular state. New York and California are the latest states to ask for such information on their tax forms. New York officials estimate that the new line in the tax form will generate $2.5 million in additional revenue; California officials believe they will reap an additional $13 million. State officials from across the country believe that there is some $35 billion in uncollected sales taxes. Some major online retailers already collect sales taxes voluntarily.

With the amount of money at stake, and the ongoing budget deficits many states are facing, it would seem to us that some sort of national sales tax clearinghouse is only a matter of time and urgency. Under such a system, purchases made through catalogs or Internet sites would be recorded for the purpose of assessing sales taxes. Such a system would do away with the present “honor system” now in effect in most states, and provide state governments with the means to track those purchases more precisely.

Some idea of how complex this problem could become can be seen in the European experience collecting VAT. Most European Web ecommerce sites have multiple versions for each market and restrict credit card use to customers in that market. This provides a one-to-one relationship between where someone lives and where the VAT gets paid. Now consider that state and local sales taxes in the U.S. comprise some 7,000 separate jurisdictions. Such a system would require a sizable investment in technology, not only for its bare bones operational needs but for such things as security and reliability. Whether such a system would be hardwired to retailers’ check-out lines or would somehow gather its data from credit card companies, the ability to purchase goods online would become a much more public affair, at least to tax officials. Such a data warehouse comes fraught with reasonable concerns about not only data and system integrity, but data privacy. These requirements will tax (pun intended) the best efforts of any IT vendor undertaking such a task, and will be given close scrutiny by both members of the public and various legislative officials on both the state and federal levels. Any vendor undertaking such a assignment would do well to remember the scrutiny and outcry surrounding many electronic voting machines, which in many cases were not only insecure and prone to tampering, but also unable to provide a paper audit trail to ensure that votes were counted correctly. When one considers the public issues raised by the tallying of the public’s votes, one can only assume that such scrutiny will be orders of magnitude higher when tallying the public’s tax liability.

SCO Announces Linux License and Lawsuits

By Charles King

SCO has announced that EV1Servers.net, a Houston-based Web hosting company, had agreed to sign a SCO Linux user license to cover most of the company’s roughly 20,000 servers. The financial details of the agreement were not revealed by either party. According to news reports, SCO’s CFO Bob Bench also confirmed that Computer Associates, Questar, and Leggett & Platt have also signed Linux licenses with SCO. In unrelated announcements, SCO said hit has filed its first lawsuits alleging UNIX copyright violations against AutoZone, an automobile parts retailer, and automaker DaimlerChrysler. The suits seek undetermined damages. Finally, SCO announced its Q1 2004 earnings results. After paying dividends on preferred shares, the company lost $2.25 million, or 16 cents per share, with revenues falling 16% to $11.4 million from $13.5 million the previous quarter. SCO lost $724,000, or 6 cents a share, in the same quarter last year.

Like Wonderland, SCO’s Linux adventures are becoming curiouser and curiouser. The company’s efforts to sell licenses for Linux distribution have finally found a few apparently willing takers, but just what those licenses mean and exactly what they are worth remains unclear. SCO’s Linux IP claims began with the company’s $1 billion (since grown like Topsy to $5 billion) suit against IBM for supposed UNIX copyright violations. SCO’s logic for this and other legal proceeding follows a somewhat tortured path; since the company purchased UNIX IP from

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Novell, any stray bits of UNIX code which might have been incorporated into Linux variants constitute copyright violations which have hugely injured SCO. The problem is that SCO has been either reticent or unable to provide much in the way of evidence for its claims. In December, the Utah judge hearing the case against IBM ordered SCO to deliver samples of the pilfered code, and reiterated the order this week. So what is the sum of all this sound and fury? Nothing, which will remain the case until when (and if) the suit is heard, a jury decides, and the principals live with or appeal the judgment. In other words, since SCO has not legally proved its claims against any UNIX or Linux vendors, its proposed licenses for Linux users are essentially worthless.

If that is the case, why would EV1, CA, Questar, and Leggett & Platt sign on? For EV1, we suspect that the company simply decided that the ongoing media noise from the suit constituted more of a threat against its business (which consists of leasing and hosting specific Linux-based servers to ebusiness clients) than simply buying the license. The other companies, especially CA, are harder to parse out, but we expect that SCO offered at least a modicum of elasticity in its $699 per single CPU licensing fee as a means of putting some public wins on the board. However, SCO's suits against AutoZone and DaimlerChrysler represent a markedly larger gamble, since both companies have the money and legal wherewithal to wrap up SCO in additional court proceedings even as the company remains embroiled with IBM, as well as in suits and countersuits with Novell and Red Hat. Given this, SCO's latest earnings statement sounds a particular warning. The company, which has never been glowingly profitable, is standing in a field heavily pockmarked by legal money pits, most of them self-constructed. Without the assistance of a deep-pocketed suitor or pal, any slip could prove potentially fatal. While the existence of such a benefactor (such as Microsoft, which for months has been rumored to be bankrolling SCO) could add some longevity to the company's efforts, unless SCO makes notable progress in court the sale of vaporous software licenses will provide little comfort and even less salvation.

The Last Mile... Revisited

By Jim Balderston

The District of Columbia Circuit Court of Appeals ruled 3–0 this week that the FCC lacks the authority to give individual states the power to set the rates which local independent phone operators pay to lease lines from the Regional Bell Operating Companies. The ruling — which will go into effect in sixty days unless stopped by further legal action — was lauded by the RBOCs and criticized by companies like AT&T and Sprint, which said the ruling would diminish customers' choices in selecting local phone service. The ruling reverses a 1996 FCC regulation that allowed state public utility commissions to set the rates that the RBOCs could charge competitors. One aspect of this week's ruling left the status quo in place for broadband providers, who will not be required to share their networks with competitors. FCC chairman Michael Powell supported the ruling but three of his fellow FCC commissioners said they would take the matter to the U.S. Supreme Court if possible.

While it is unclear what the final determination of this case will be, and the distinct possibility exists that it will not be settled for at least a few years while it makes its way to the Supreme Court docket, it is also conceivable that the corner has been turned on how the RBOCs will be regulated and that they will be allowed to determine if and at what cost competitors will be allowed to access their last mile connection to the consumer. For long distance carriers like AT&T and Sprint, which are trying to build out local phone service, their days in these markets could be numbered as a result of this ruling. This ruling also undercuts the central purpose of the Telecommunications Act of 1996 which was supposed to open up local phone services to real competition. Such are the vagaries of operating businesses that are prone to having their markets upended by three judges (or perhaps nine, if the matter makes it to the Supreme Court).

If this ruling does stand, the emergence of the RBOCs as more than a mere shadow of Ma Bell will be realized, with major regional players assuming all the power of Ma Bell within their coverage areas. Further consolidation of the RBOCs may be in the making as well. But while the RBOCs may have gotten some relief from the likes of AT&T, MCI, and Sprint, we suspect that they will see more competition coming forth from those other providers of last mile connectivity, the cable companies. With things like Internet phone service gaining popularity and a built-in loyal subscriber base of Cable TV and high-speed internet access customers, the leap to phone service as a

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part of a bundled communication package seems well within the realm of possibilities. Of course, any such efforts by the broadband providers will require sizable infrastructure upgrades, but ones that given the nation's thirst for connectivity could become prudent investments in the long run. For IT vendors of all stripes, a huge opportunity could be in the offing as a result.

IBM Entices Partners to Play with SMBs, SMBs Offered Pretty New Things

By Joyce Tompsett Becknell

At IBM's Partnerworld in Las Vegas, IBM announced new resources and initiatives for its business partner community designed to help them grow their presence in SMB with industry-specific solutions tailored to SMB needs. The offerings, part of the IBM SMB Advantage initiative, will be available to all business partners, including resellers, ISVs, and SIs, and will be driven through the IBM Express portfolio of products. The program includes a $500 million investment in demand generation, education, teaming, and sales incentives with the Solution Builder Express. The solutions will be targeted to six areas including business integration, business intelligence, content management, ecommerce, infrastructure, and portal/workplace. They will also be sorted by industry vertical, including automotive, banking, electronics, finance, insurance, retail, wholesale, and the consumer and packaged goods industries.

Like most high-tech vendors, IBM is fascinated with the untapped potential of the small and medium business segments. It is consistently viewed as one of the more lucrative markets and yet it is the trickiest for vendors to approach. As a rule, SMBs do not purchase directly, which means that IBM must rely on its partners to provide the right solutions. When it works well, it is a win for all involved, but the consistency of quality of delivery has been difficult to achieve across such a diverse population. The problem with those pesky SMBs is that although they are lumped together as such by the vendors, the companies do not perceive themselves as SMBs. They persist in seeing themselves as specialists in their individual markets. This means that they want solutions targeted to the needs of their vertical space the same as really big companies do. A lot of SMB marketing in high tech has offered a one-size-fits-all approach, and it has succeeded only where that one size truly fits. By taking the time to target specific markets at price points and sizes that match SMB appetites, IBM and its partners can bring truly credible solutions that should make SMBs take notice.

The other half of this announcement of course revolves around the business partners. Like all businesses, the partners have longed for the big contracts with high price tags and higher margins which has led them to pursue larger companies. IBM, on the other hand, would like the partners to focus on the SMBs, where it has less likelihood of channel conflict and stands to gain more new business. Rather predictably, the partners will not oblige IBM unless they have real value-added solutions, allowing them to grow a substantial customer base and make money off it. In the end, this investment should provide the requisite solution building blocks partners need to confidently pursue SMB markets and extend IBM's reach across more enterprises.

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