

Executive Insights

Understanding the Financial Benefits of Open Source

Raven Zachary, The 451 Group

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Agenda

- About
- Introduction
- Financial Analysis 101
- The Financial Elements
- The Calculator
- Best Practices
- Resources



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- An independent technology industry analyst company focused on the business of enterprise IT innovation
- Sector coverage - enterprise software, storage & systems, networks & media, and mobile software
- Clients include investment banks, VC firms, software vendors, and end users
- Offices in New York, San Francisco, London, and Boston
- 25+ analysts



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451 CAOS Research Service

- The Commercial Adoption of Open Source (CAOS) Research Service
- Bi-monthly research reports on enterprise open source topics
- Ongoing industry and community coverage
- Weekly insight service mailing
- Publicly-accessible blog
 - ✓ blogs.the451group.com



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Purpose

- "A practical guide for understanding and calculating the financial benefits of open source"
- Independent
 - ✓ Licensed by JBoss
 - ✓ Authored prior to joining The 451 Group
- Supports the business case
- Non-academic
- Educational
- Actionable!



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Position

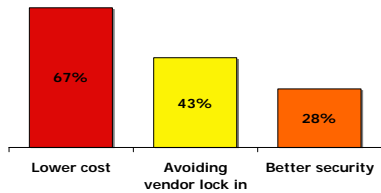
- The only position that the report takes is that financial benefits are *possible* with open source
- A bold position for a software vendor to support!



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CIO Insight Research Study

- November 2005
- Open Source Turns Strategic
- "What are the top three reasons your company uses open source systems, including Linux, rather than proprietary software?"

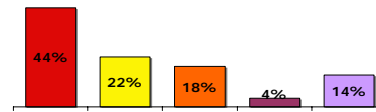


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Computer Economics Survey

- May 2005
- The Key Advantage of Open Source
- "What is the most important advantage in the use of open source?"



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End User Interviews

- Roughly half of the organizations said that financial benefits were the primary driver for open source adoption
- Other responses included greater control, avoidance of vendor lock-in, and ease of customization

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Financial Analysis 101

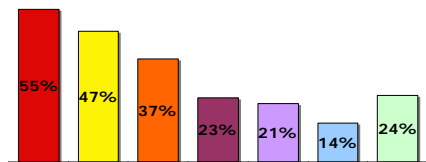
- Where do I start?
- How do I account for the unique aspects of my project and organization?
- What sources can I trust?
- What costs do I need to capture?
- What calculation method(s) should I use?
- How should I present the data?

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Baseline Magazine Survey

- May 2005
- Managing Projects Survey
- "If you've set financial goals, what methods are you using?"



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Why Financial Analysis is Important

- Points of comparison for multiple, competing projects
- IT budgets remain under cost pressure
- An exercise in planning
- Valuable knowledge for the future

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Financial Terms

TCO Fixed Costs Amortization

Sunk Costs NPV Cost Avoidance

ROI Capital Budgets

Opportunity Costs Cash Flow

Hard Costs Depreciation

IRR

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Financial Lessons Learned

- Each project and organization are unique
- Formal processes are not always in place
- Not every project has a financial benefit
- Cost savings are rarely "saved"
- Financial benefits studies often support a position

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The Financial Elements

- Hard Costs
 - ✓ Software Licenses
 - ✓ Hardware
 - ✓ Support
 - ✓ Development
 - ✓ Operations
 - ✓ ...

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The Financial Elements

- Soft Costs
 - ✓ Downtime
 - ✓ Planning
 - ✓ Productivity
 - ✓ Support Quality
 - ✓ License Management
 - ✓ ...

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The Financial Elements

- Internal Costs
 - ✓ Charge-backs
 - ✓ Depreciation
 - ✓ Taxes
 - ✓ Time / Internal Labor
 - ✓ Contingency
 - ✓ ...

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The Financial Elements

- Revenue
 - ✓ Finances are not just about costs, they are also about gains
 - ✓ If there is a revenue component to your project, it should be captured

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The Calculator

- A simple spreadsheet
- Multi-year analysis
- Side-by-side comparison
- Various financial elements
- Flexibility for customization

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The Calculator

	Initial Investment	Year 1	Year 2	Year 3	TOTALS
HARD COSTS	76,250	41,200	111,150	49,100	277,700
Software Licenses	-	-	-	-	-
Hardware	25,000	3,000	3,000	3,000	34,000
Support	-	25,000	30,000	35,000	90,000
Development	22,000	2,500	5,000	2,500	32,000
Professional Services	12,500	3,000	-	-	15,500
Training	7,500	-	-	-	7,500
Testing	3,000	3,000	3,000	3,000	12,000
Operations	2,500	500	500	500	4,000
Staffing	-	-	65,000	5,100	70,100
Maintenance Contracts	3,750	4,200	4,850	5,100	17,900
SOFT COSTS	-	-	-	-	-
INTERNAL COSTS	-	-	-	-	-
REVENUE	-	250,000	500,000	800,000	1,550,000
CASH FLOW	-	-	-	-	-
Period	(76,250)	208,800	388,850	790,900	
Cumulative (Payback)	(76,250)	132,550	521,400	1,272,300	
RATE OF RETURN	-	607%	450%	1629%	
PAYBACK PERIOD	-	-	-	-	-
NPV	954,643				
IRR	340%				
cost of capital %	12%				

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The Calculator

Side-by-side comparison

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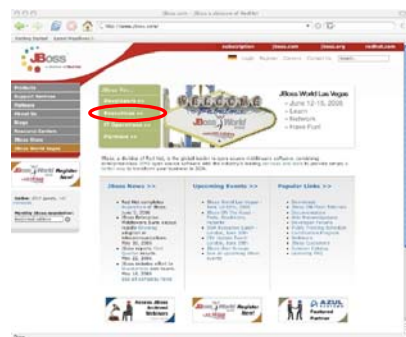
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Best Practices

- Be consistent
- Show your math
- Gather the right information
- Use a margin of error
- Recognize timing issues
- Review your contracts
- Build a business case

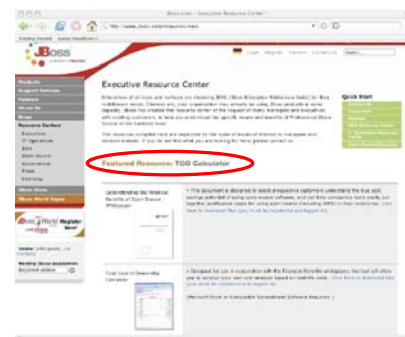
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The Report & Calculator



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The Report & Calculator



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Other Resources - Books



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Other Resources - Articles



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