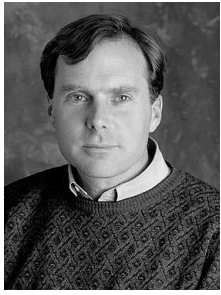


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CRM's Future: Humble Growth Through 2007

FORRESTER®



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After shrinking by more than \$2 billion in 2002, the CRM market will grow at more than 11% annually -- hitting \$73.8 billion in 2007. During this period, users will shift from integration to continuous optimization.

2 MARKET OVERVIEW

- The CRM market declines more than 5% in 2002.
- CRM applications grow from \$11.7 billion in 2002 to \$20.6 billion in 2007.
- Services represent 56.8% of the total market in 2007.

3 ANALYSIS

- Web services will lower both user lock-in and license fees.
- After mastering multichannel infrastructures, CRM users will wield analytics to tune their customer and channel mix.

8 WHAT IT MEANS

- Microsoft dominates the mass market for analytics.

9 RELATED MATERIAL

- Online spreadsheet for the CRM forecast featuring seven market drivers

10 GRAPEVINE

11 ENDNOTES

MARKET OVERVIEW

CRM GROWS TO \$70 BILLION IN 2007 -- MODERATELY

Where is the CRM market headed? To answer this question, Forrester dissected the overburdened CRM moniker into 10 component categories: applications, services, and infrastructure (see Figure 1). Based on our analysis of the dynamics of these segments and the overall economic environment, we project that CRM revenues will grow from \$42.8 billion in 2002 to \$73.8 billion in 2007 (see Figure 2).¹ After a drop of 5.4% in 2002, the market will experience a healthy, but modest, compound annual growth rate of 11.5% over the period of 2002 to 2007. Some highlights:

- **Services dominate revenues.** Professional service firms and outsourcers make up over half of the total CRM market. Growth at consulting firms like Accenture and Deloitte Consulting, contact center outsourcers like Convergys and TeleTech, and marketing services providers like Acxiom and Harte-Hanks will drive the CRM services segment to \$41.9 billion in 2007.
- **Apps revenue resurges in 2004.** Vendors like Siebel Systems, Onyx Software, and KANA Software stumbled through 2001 and early 2002. But the CRM apps category will regain its footing as annual growth jumps from 6.8% in 2003 to 14.0% in 2004. This expansion tapers to 12.5% by 2007 -- but CRM apps outpace the overall market average with CAGR of 11.9% over the period of 2002 to 2007.
- **Internet commerce drags down customer channel apps.** Despite gains made by eCRM vendors like eGain Communications, Primus Knowledge Solutions, and RightNow Technologies, customer-facing channel applications experience the slowest growth in the CRM market (see the July 2002 Forrester Report "Mastering Online Customer Service").² As eCommerce vendors like BroadVision and ATG scramble to morph from online commerce vendors into self-service vendors and interactive selling suites from Calico Commerce and Trilogy wilt, they will drag the annual growth rate of this segment down to 7.3%.
- **Marketing automation makes the most headway.** Marketing automation vendors like E.piphany and Unica put on a late-stage spurt to capture the title of fastest-growing CRM segment. While growth between 2002 and 2004 will hover around 14.5%, the segment expands at a 17% rate thereafter. The result: Marketing automation more than doubles -- hitting \$928 million in 2007.

Figure 1 Subsegments Of CRM Market

Category	Description	Representative vendors
Applications	Software licenses, maintenance, and services by application vendors	
Marketing automation	Campaign planning, list management, campaign execution suites	Teradata, Unica, Xchange, Revenio, MarketFirst, Aprimo Marketing
CRM suites	Integrated, multifunction applications that span online and offline marketing, sales, and/or service	Siebel, SAP, PeopleSoft, Oracle, E.piphany, Onyx, Pivotal
Analytics	Tools for customer segmentation, behavior, profitability modeling, reporting, and analysis	Quadstone, SAS, Marketswitch
Customer channel management	CRM application vendors addressing primarily Net-based channels (includes eCRM, commerce, configurators, knowledge bases, FAQs)	Kana, eGain, Divine, Trilogy, Blue Martini, BroadVision, Primus, ServiceWare, Banter
Field force automation	Software for field-based organizations including direct sales, channel management, and field service	Dendrite, UpShot, MarketSoft, Click Commerce, ChannelWave, Allegis, ViryaNet, FieldCentrix
Services	Outsourced business process and professional services related to contacts and data	
Contact center outsourcing	Outsourced inbound and outbound agent-assisted sales and service	Convergys, TeleTech, APAC, SYKES
Consulting	Professional services firms that provide strategy, implementation, and operational consulting	Accenture, Monday, Deloitte, IBM Global Services, KPMG, Akibia, eLoyalty
Marketing services	Outbound email, customer experience measurement, surveying, data deduping and augmentation	Experian, Acxiom, Group 1 Software
Infrastructure	Integration and routing technology for contacts and data	
Data integration	Middleware explicitly created to integrate customer data and provide a common data model across an organization	DWL, BEA, Siperian, Acta
Contact center infrastructure	Call routing and queuing, CTI, IVR/voice recognition, work-force management and training	Avaya, Alcatel, Witness Systems, Aspect, Blue Pumpkin

Source: Forrester Research, Inc.


ANALYSIS

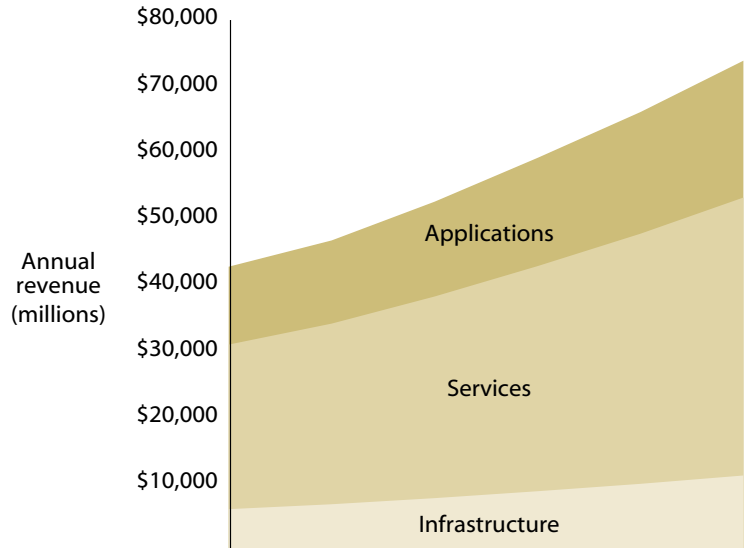
NEW FORCES RESHAPE THE CRM MARKET

What's in store for CRM's future of humble growth? Forrester identified seven key drivers that will reshape the overall industry (see Figure 3).

- 1) **Technology saturation.** During the late 1990s binge, firms purchased about 10% more technology than they needed. Coupled with corporate downsizing and general economic malaise, 2001 became a bitter winter for most tech vendors. While 2002 shows signs of economic stabilization, Forrester doesn't expect the impact of that glut to completely wear off until 2004 (see the March 19, 2002 Forrester Brief "Tech Recovery Update: Coming Off The Bottom").³

Figure 2 Forecast: Global CRM Sales, 2002 To 2007

 The spreadsheet detailing this forecast is available by clicking the online "Get Data" button above this figure.



	2002	2003	2004	2005	2006	2007	CAGR
Total	\$42,767	\$46,729	\$52,571	\$59,180	\$66,093	\$73,839	11.5%
Applications	\$11,746	\$12,543	\$14,299	\$16,325	\$18,348	\$20,639	11.9%
Marketing automation	\$439	\$487	\$575	\$678	\$793	\$928	16.2%
CRM suites	\$7,130	\$7,625	\$8,814	\$10,188	\$11,512	\$13,009	12.8%
Analytics	\$1,525	\$1,646	\$1,864	\$2,110	\$2,364	\$2,647	11.7%
Customer channel apps	\$2,185	\$2,264	\$2,440	\$2,641	\$2,859	\$3,103	7.3%
Field force automation	\$468	\$520	\$606	\$707	\$821	\$952	15.3%
Services	\$24,819	\$27,243	\$30,410	\$33,949	\$37,723	\$41,920	11.1%
Contact center outsourcing	\$10,015	\$11,346	\$12,781	\$14,397	\$16,125	\$18,060	12.5%
Consulting	\$12,740	\$13,594	\$14,994	\$16,537	\$18,191	\$20,010	9.5%
Marketing services	\$2,064	\$2,303	\$2,635	\$3,015	\$3,407	\$3,850	13.3%
Infrastructure	\$6,203	\$6,943	\$7,863	\$8,906	\$10,022	\$11,280	12.7%
Data integration	\$1,016	\$1,180	\$1,371	\$1,593	\$1,832	\$2,107	15.7%
Contact center infrastructure	\$5,187	\$5,763	\$6,492	\$7,312	\$8,190	\$9,173	12.1%

(All dollar amounts are in millions and numbers have been rounded)

Source: Forrester Research, Inc.

Figure 3 Forces Reshaping CRM Market

Market drivers	Impact on CRM segments
Technology saturation	<ul style="list-style-type: none"> • Tech saturation worked off by 2004 • Gainers: None • Losers: All market segments except data integration
Customer contact channel integration	<ul style="list-style-type: none"> • A priority today; diminishes by 2005 as most firms achieve it • Gainers: All segments except Internet commerce • Losers: Internet commerce loses as efforts are consolidated
Vendor verticalization	<ul style="list-style-type: none"> • By end of 2004, most apps vendors have vertically tailored products • Gainers: CRM suites • Losers: Mild negative impact to pure consulting firms
Web services-enabled portals	<ul style="list-style-type: none"> • Low impact through 2003; full impact by 2005 • Gainers: Consulting; point technologies like PRM and self-service • Losers: CRM suites, as best-of-breed becomes a more viable alternative
More professional services by apps vendors	<ul style="list-style-type: none"> • Apps vendors steadily increase their consulting services revenues • Gainers: Apps vendors segments • Losers: Pure professional services firms
Apps vendors shift to subscription model	<ul style="list-style-type: none"> • Subscription model steadily gains importance over the next five years • Gainers: Field sales, service, marketing apps gain from broader adoption • Losers: CRM suites, as per-seat prices decline on enterprise deals
Offshore labor	<ul style="list-style-type: none"> • Offshore labor slowly, but steadily, becomes a factor over the next five years • Gainers: Contact center infrastructure, eCRM, and CRM suites • Losers: None

Source: Forrester Research, Inc.

- 2) **Channel integration.** Most firms will continue to assemble a complete view of their customer relationships by combining scattered data from an average of four customer channels through 2005. Consultants like Monday and Cap Gemini Ernst & Young, specialty data integration firms like DWL, and CRM suites vendors all benefit from this focus. By 2005, firms will master the basics of channel integration and will be looking for more sophisticated operational and analytical capabilities.
- 3) **Vendor verticalization.** ISVs like eGain and SAP are organizing themselves around industry lines -- an established practice at consultants like KPMG and Accenture. The slowdown in CRM suite license sales will continue to drive software vendors deeper into niches as they tailor once-horizontal products for specific industries -- placing them in direct competition with their consulting partners, as well as industry specialists like Dendrite in pharmaceuticals or Reynolds & Reynolds in automotive (see the June 18, 2002 Forrester Brief "CRM's Future: Verticals, Subscriptions, Services").⁴
- 4) **Web services-enabled portal architectures.** Siebel Version 7 represents an industry trend as vendors rearchitect their products around middle-tier business object servers that use Web services to connect with both browser-based and fat clients. The result is bittersweet for vendors. While this trend will improve CRM

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deployments, it will also enable alternative user interfaces through transactional portals -- deflating today's \$3,000 to 5,000 per-seat client/server cash cows (see the May 2002 Forrester Report "Web Services Erode CRM Barriers").⁵

- 5) **Services ascendant.** CRM implementation survivors face an even larger challenge: getting people to use apps. Operational change specialists like Deloitte Consulting, Seurat, and Extraprise Group will help firms redesign processes and incentives that encourage users to capture and maintain quality data. Vendors like Quixi that provide data entry services for mobile sales reps, voice recognition firms like Datria Systems and Nuance Communications, and data vendors like Ascential Software and D&B will win as they piggyback on these efforts.
- 6) **A shift to subscriptions.** As software vendors seek to build a revenue backlog to smooth quarterly results, they will increasingly turn to subscription-based apps. Oracle's Larry Ellison declared that one-third of his firm's revenue will come from hosted applications by 2005.⁶ Vendors like Salesforce.com, UpShot, and Salesnet already serve a small but growing installed base.⁷
- 7) **Low-cost offshore labor.** Global 3,500 firms spend an average of \$8 million on offshore development services today but don't follow suit with CRM-related services (see the September 2001 Forrester Report "The Coming Offshore Services Crunch").⁸ As firms like Symantec and Amazon.com have discovered, chat and email services from providers like Daksh eServices in India and PeopleSupport in the Philippines can save firms 40% over Stateside prices (see the March 20, 2002 Forrester Brief "A Contact Center In India? Daksh Explains Why").⁹

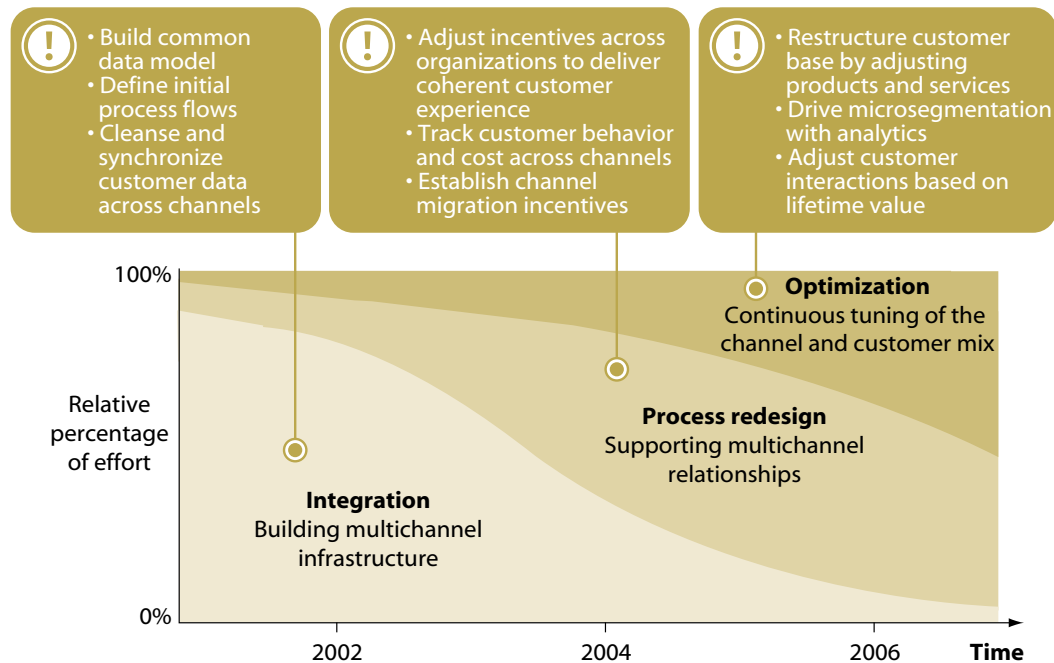
CRM PREPARES FOR THE NEXT WAVE

The days of unfettered CRM growth are over. Firms hoping that CRM apps would provide customer relationship magic face the stark reality of languishing apps, lousy data, and dysfunctional organizations. But the CRM disappointment won't last. Just as manufacturers evolved from a 1900s scrap-and-rework approach to today's design-for-manufacturability process control, firms will extract value from their CRM investments by evolving through three phases of maturity (see Figure 4 and see the June 2000 Forrester Report "The Customer Conversation").¹⁰

- **Phase 1: Channel integration.** Forty-four percent of online shoppers use two or more channels; 79% of financial transactors are multichannel (see the June 2002 Forrester Report "Right-Channeling Financial Transactions").¹¹ Yet firms still struggle with cleaning and synchronizing data and leading consumers to the best channel for a transaction: Many firms can't provide basic capabilities like central change of address or help with online transactions from their call centers. So firms start their CRM journey by cleaning up data across both online and offline channels.

Figure 4 Evolution Of CRM Activity At Typical Global 3,500 Firms

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Source: Forrester Research, Inc.

- **Phase 2: Process redesign.** With the basic interaction infrastructure in place, firms face an even tougher task: changing employee and customer behavior to match revised business rules and process flows. These people- and process-centric efforts run smack into tough issues like “that’s my territory” and “we’ve always done it that way.” Firms in this more advanced stage will design metrics and offers that span organizational boundaries. Some examples: Merrill Lynch offering incentives to field reps who yield low-net-worth clients to lower-cost phone reps or EMC offering its storage network customers discounted firmware upgrades if they are done remotely rather than by a technician dispatched to the customer site.
- **Phase 3: Continuous optimization.** Manufacturers like 3M and Ford Motor Company have used statistical experimental design to control quality for decades -- now it’s the front office’s turn. Firms that reach the third phase will view their businesses as a constantly updated portfolio of products and customers. Credit card giant Capital One Services provides a nascent example of a third-phase activity: It conducts its business as 40,000 designed experiments per year. The majority of these efforts fail, but the firm can quickly triage the new products and customer segments worth keeping -- and the ones to jettison.

WHAT IT MEANS

- !** **The glory days of love-'em-and-leave-'em app sales are over.**
Mounting pressure for software warranties, class-action lawsuits, and the SEC rummaging through vendors' books for revenue recognition snafus will morph most ISVs into hybrid businesses. Vendors like E.piphany and PeopleSoft will offer lease-to-buy or subscription-based licensing, a choice of hosted or on-site products, and a professional services segment that approaches 50% of revenue.
- !** **Microsoft will democratize marketing analytics.**
As CRM users get past the process redesign stage, they'll reach out for practical analytical tools. Which vendor will meet these needs? Microsoft. SAS and SPSS will appeal to the statistical elite, but Microsoft will run away with the mass market. Redmond will dominate the fast-growing marketing automation category through its broad Microsoft Office user base, .NET-enabled product portfolio, and user interface skills.
- !** **ISVs continue to blend supply- and demand-side apps.**
Consolidation pressure from declining ISV valuations and user-pendulum swings toward one-stop shopping will drive suite vendors like Siebel to seek new sources of license revenue. Siebel's vertical functionality will push the vendor farther into the supply chain -- in the automotive vertical for example -- toward order fulfillment and availability checks with suppliers. Expect Siebel to pick up a collaborative design vendor like Alventive, a supply chain visibility app like Viewlocity, or contract management from struggling diCarta.

RELATED MATERIAL

Online Resources

The underlying spreadsheet detailing the forecast in Figure 2 is available by clicking the online “Get Data” button above the figure.

Forecast Methodology

The model underlying this forecast was created based on 2001 revenue data from 447 CRM-related software, service, and infrastructure vendors. This revenue data came from several sources: 1) public filings; 2) OneSource Information Service (used for private company data); 3) briefings with Forrester analysts; and 4) an online survey of 49 vendors. The companies were grouped into 10 market segments, which roll up to three major categories.

Forrester made estimations to allocate revenue across market segments. Siebel, for example, reports its revenues in only two categories -- licenses and services -- but participates in many of the market segments. We generally did not split revenue for large vendors across segments unless there was concrete evidence on which to do this. Instead, we created categories that lend themselves to easy classification of vendors -- for example, CRM suites or customer channel applications.

While we believe that all significant vendors were accounted for in each segment, we did not attempt to track every vendor that claims to have some CRM revenues. As a result, the forecast will slightly underrepresent the overall market.

Related Research

July 2002 Forrester Report “Mastering Online Customer Service”

June 18, 2002 Forrester Brief “CRM’s Future: Verticals, Subscriptions, Services”

June 2002 Forrester Report “Right-Channeling Financial Transactions”

May 2002 Forrester Report “Apps Market, Interrupted”

May 2002 Forrester Report “Web Services Erode CRM Barriers”

GRAPEVINE

Rube Goldberg writes a business plan.

Remember Rube Goldberg's wacky contraptions, typically something like: Dog chases cat on treadmill to wind string to ring bell and wake sleeping father? We encountered the equivalent in a business model: European automotive paint vendor gets into auto insurance business so it can influence consumer selection of a body shop that uses automotive paint products that consume its paint. That's Akzo Nobel's Car Refinishes business unit's plan, according to Adam Honig, CEO at Akibia Consulting, the integrator providing systems for Akzo. Now that's managing your demand chain.

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Upgrade pace slows for Siebel.

On a quarterly earnings call Tom Siebel once boasted that 90% of his customers upgrade to a newest version within a year of its release. He's going to have a tough time hitting that mark if our intelligence is correct: In a recent conversation with one of his systems integration partners, the CEO intimated that none of its 50-plus Siebel 6 customers has taken the leap to version 7 yet. No one's going to hold Tom to this track record in the current economy. But Forrester expects that we'll never see rapid-fire upgrades again -- witness SAP's recent decision to extend the life of R/3 4.6C when customers balked at SAP's announced retirement of support for the product.

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Delta's passive-aggressive profitability preference.

On a recent Delta Air Lines trip, we overheard a ticketing agent tell a customer who was using a ticket purchased with frequent-flyer miles that she was bumped off a rescheduled flight because the customer was not "a revenue customer." Maybe not this trip -- and maybe never again if Delta doesn't suppress its urge to thump customers exercising their hard-earned loyalty rewards.

ENDNOTES

- 1 The model underlying this forecast was created based on the 2001 revenues for 447 CRM-related software, service, and infrastructure vendors. We generally did not split revenue for large vendors across segments; instead we created categories that lend themselves to easy classification of vendors -- for example, CRM suites or field force automation. We did not attempt to track down every last vendor, so the forecast slightly underweights the contribution of myriad small companies.
- 2 Forty-five percent of companies are actively considering or piloting interactive knowledge bases, and 50% of firms expect to increase eService spending in 2004 as firms expect online self-service to absorb 23% of their incoming call volume over the next two years.
- 3 Forrester believes that there was a 12% overspend in technology in 2000 -- representing a \$62 billion bubble.
- 4 Thirty-eight of 45 CRM software and services providers surveyed expect their efforts to build industry-specific processes and knowledge into their apps to increase "substantially" or "moderately" by 2004.
- 5 Web services, even in their nascent state, plug the gap between doing nothing and building a robust -- but complex -- EAI technology. Because of this practicality, Forrester believes that firms will embrace Web services organically to: 1) Share data and status about demand, opportunities, orders, and service requests; 2) centralize key services for common customer IDs, pricing, and configuration; and 3) build role-based transactional portals to foster data and functionality sharing.
- 6 Ellison made this claim in his keynote at Oracle Apps Week, Oracle's user group meeting, in April 2002.
- 7 Collectively, Salesforce.com, Upshot, and Salesnet booked about \$40 million in revenue in 2001; we expect this figure to top \$75 million in 2002.
- 8 While the typical firm with more than 5,000 employees spends almost \$8 million on offshore service providers today, we estimate that the average budget will reach \$26 million by 2005.
- 9 Daksh loses less than 25% of its employees annually -- half of typical US turnover rates -- and pays its employees \$3,000 to \$5,000 per year. This more than offsets the 50% higher communications charges incurred for offshore facilities.
- 10 Firms that manage customer relationships from within channel and function stovepipes can't deliver the consistent experience that's expected by Net-aware customers. To meet these expectations, firms must evolve their CRM efforts to treat customer relationships as conversations.
- 11 Disparate CRM and channel integration efforts won't change how consumers use delivery channels or fix disjointed cross-channel customer experiences. Firms must get consumers to use the right channels for the right transactions.

Forrester's WholeView™ Research provides clients with unified guidance on customer trends, business strategy, and technology investments through Technographics®, TechStrategy™, and TechRankings™. WholeView Research drills down into the most important details of an issue while maintaining a holistic perspective of the impact of technology change on business.

Forrester also offers Events and Strategic Services that further enhance the WholeView. Each Event provides new ideas, clear direction, and innovative strategies with a WholeView perspective. Strategic Services deliver custom guidance for the complex business decisions that drive your company's success.

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Consumer Relationship Management

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Enterprise Applications

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Forrester Events

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Register by August 1, 2002, and qualify for an early registration discount (Forrester clients: \$1,200; Nonclients: \$1,350).

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London
October 7-8, 2002