

Searching for the next Salesforce - June 24, 2005

By Alorie Gilbert

Is there room for more than one Salesforce.com?

Michael Gregoire sure hopes so, and he's not alone. Gregoire, a former PeopleSoft executive, recently took the helm at San Francisco start-up Taleo. It's one of a few dozen software start-ups emulating Salesforce, which is shaking up the \$10 billion market for customer relationship management, or CRM, software and threatening industry leader Siebel Systems with a groundbreaking business model.

Salesforce's software programs require no installation because the company delivers them as Web pages over the Internet. Salesforce also charges monthly subscription fees for its service instead of requiring traditional licensing agreements that include big starting fees--agreements businesses find increasingly cumbersome.

But analysts say up-and-comers such as Taleo, which is taking the same no-fuss "on-demand" model to the much smaller market for corporate hiring and recruiting software, may have a tough time reaching Salesforce's heights.

"We'll see if one of these guys can break out as the quote-unquote next Salesforce.com," said Peter Coleman, securities analyst at Think Equity Partners. "A lot of it's a matter of timing."

Salesforce had impeccable timing, Coleman said. It was not the first company to introduce business software by subscription or "as a service." Many dot-com-era start-ups tried it first and then flamed out as the high-tech scene unraveled. Salesforce was a relative latecomer, but by the time it introduced its on-demand customer information system, in 1999, many businesses had become disenchanted with other applications software that didn't live up to expectations. Customers of Siebel Systems were a particularly unhappy bunch, and Salesforce went right after them.



Michael Gregoire
CEO, Taleo

Salesforce had a few other things going for it too. Siebel had already convinced thousands of businesses that they needed customer relationship management software, creating a huge market with lots and lots of potential users. It also helps that Salesforce is led by master salesman Marc Benioff.

The conditions created the perfect storm that launched Salesforce as the big success story of the subscription-software market, analysts said. A much anticipated initial public stock offering last year and a ninefold increase in first-quarter profits this year--all amid a lackluster market for business software--are proof of that.

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Such conditions are hard to replicate, yet the list of start-ups aspiring to be the next Salesforce seems to grow by the week. In addition to Taleo, it includes Rearden Commerce, which specializes in on-demand software for ordering business supplies and services, and BlueRoads, which makes applications for facilitating communication between businesses and their distribution partners. Enviance develops programs for ensuring compliance with environmental, health and safety (EH&S) regulations, while

Employee provides human resources applications. NetSuite, an Oracle-backed venture, and Intacct both specialize in accounting systems.

Taleo, formerly known as Recruitsoft, is hoping to break out of the pack with an initial public offering this year. The San Francisco company recently amended its IPO registration forms and expects to pull the trigger later this year.

Gregoire claims Taleo is among the top subscription-software "pure plays" behind Salesforce, though it's just a third of Salesforce's size. Salesforce reported \$176 million in revenue last year while Taleo revenue was about \$60 million, according to AMR Research estimates. That makes Taleo just about the size of RightNow Technologies, an on-demand player that went public last year.

Gregoire, one of several ex-PeopleSoft executives to join the company recently, was probably a wise hire. He was the head of PeopleSoft's \$1 billion services business until Oracle took over the company earlier this year. So his Rolodex is surely filled with names of hundreds of PeopleSoft customers--companies who are natural candidates for Taleo's service.

And he appears passionate about Taleo's prospects.

"We're the category leader in talent management," Gregoire said. "Believe me, it's hot."

Hot or not?

Talent management is a small but growing niche of the \$14 billion human resources software market. The programs help companies with recruiting and hiring tasks by storing, sorting and ranking resumes, creating a searchable database of job candidates. They can also automate routine tasks, such as adding new hires to payroll, and incorporate online psychological screenings of job candidates.

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*Peter Coleman, analyst
Think Equity Partners*

The software has helped companies fill positions more quickly and reduced paperwork, according to IT researcher AMR Research. Lowering employee turnover and reducing payouts to executive search firms are other potential benefits of the technology. The fledgling market generated about \$156 million in license revenue last year, by AMR's estimates.

Such niche markets, by virtue of their size, are more limited today than the market for CRM software, where Salesforce thrives. Yet these fringe markets are the best opportunity for subscription-software start-ups building viable businesses, analysts say.

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Many analysts believe these pioneering companies are just the early wave in a major transformation of the business software market. That transformation will see most software delivered as a service over the Web but will take many, many years to complete.

"It's way past the experimental stage, and the doubters have been proven wrong," said Jason Maynard, a securities analyst at Credit Suisse First Boston. "It's become real, and now it's just a question of how far and fast does it go."

Worldwide spending on subscription software grew by almost 40 percent last year, hitting \$4.2 billion, according to researcher IDC. The growth will continue at a rate of 21 percent a year over the next five years, IDC predicts, climbing to more than \$10 billion by 2009.

On a quest to keep pace, Taleo has made several acquisitions and expanded the scope of its products over the past year. It's now able to handle recruiting for salaried, hourly and contract workers and offers a lower-cost product for small businesses. The company also recently formed a partnership with LinkedIn, an online community of professionals, giving Taleo customers quick access to tools for finding references and referrals.

Taleo has assembled a list of 250 customers that even Salesforce would envy. It includes Dow Chemical, Gillette, Hewlett-Packard, Hyatt hotels, Procter & Gamble, Starbucks and Toyota. Its software stores almost 24 million resumes collectively for those companies.

Prices for its flagship product, Taleo Enterprise Edition, are based on the size of customers' staff. For a company with 10,000 employees, Taleo charges between \$75,000 and \$125,000 a year for the service--a premium compared with prices charged by most competitors. A scaled-down version of the product, for small and midsize businesses, starts at \$99 a month per licensed user, which falls within the range of most competitors' prices, Gregoire said.

Taleo's rivals include start-ups BrassRing, Deploy, Hire.com (recently acquired by Authoria), PeopleClick, Softscape and Webhire. All offer software by subscription, but Taleo claims to be the leader, with twice the revenue of its nearest competitor, BrassRing.

SAP and Oracle--among the world's largest applications companies--also are competitors. But Taleo has advantages over them, Gregoire said. SAP doesn't generally offer software by subscription, and Oracle is distracted by a monumental software redesign following its acquisition of PeopleSoft, he said. "They have really got other fish to fry right now," he added.

However, Taleo and its start-up rivals should brace themselves, analysts said. SAP and Oracle have a way of nudging in on interesting new markets. "It's sort of an on-demand feeding frenzy," Joshua Greenbaum of Enterprise Resource Planning said. "And like all good feeding frenzies, there's bound to be some blood in the water."