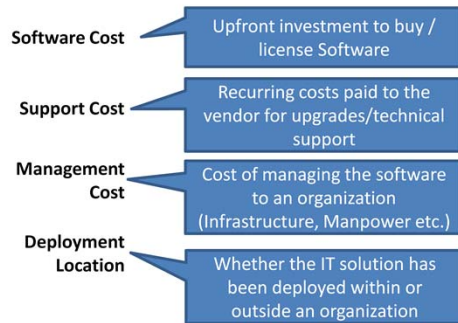# Evolution of the IT Business Model

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Let's now take a closer look at how the Software business model has evolved over the years.

The cost of IT for businesses is many-fold; It includes software costs, software support costs, management costs. In addition, we consider where a solution has been deployed.

Software cost is the upfront investment that is paid to the vendor and is used to purchase or license a particular software solution. Support costs refer to the recurring costs paid to an IT vendor for software support, updates, patches etc. Management cost denotes the cost of running a particular IT solution to an organization, such as the IT infrastructure costs, and costs in IT personnel.

Let's now look at a few software service models and typical costs associated with each.

First we have the traditional model where proprietary software is created and licensed to organizations, for example ERP or CRM software solutions that are created from scratch. For our example, let us assume that such software may cost in the range of 4000 US dollars per user as a one-time software purchase fee. It is also typical for vendors to charge an annual support fee, which in this example can be about 800 US$ per year. However, the management costs are invisible in this case as it's the clients responsibility to take care of them, which includes the infrastructure and the personnel required to keep the software running year after year. Some studies have shown management costs can be up to 4 times the cost of software. And of course, the solution we are talking about here is typically deployed at the clients' side.

Software Service Models

	Traditional	Open Source
Software Cost	$4000 /user (one-time)	$0 /user
Support Cost	$800 /user /year	$1600 /user /year
Management Cost	Up to 4x the cost of Software!	
Deployment Location	Client Side	

There has been a major trend among various organizations to invest in open-source software solutions of late, however many companies are not willing to take the risk of investing in such solutions without software support. Thus in the open source model, the cost of software and licensing is typically free or at a small cost, but an open source software vendor will charge the client a support cost, which may be higher than the traditional model. This model has been popularized by companies such as Red Hat. The open source model reduces the visible cost of the software, but the management cost remains the same, which is still a major chunk of the overall cost of the solution.

The next model is the outsourcing model, which can be used to reduce the cost of IT by delegating the management of software to companies based in India or China, for example. The savings incurred in this model is by reducing the cost of manpower, and transferring management responsibilities to such companies. For this discussion, we can apply the outsourcing model over a traditional software solution, which means that the software and support costs are the same as the traditional one, however, since the management of the software has been outsourced to a company, they can quote a flat, per-user fee to manage the software, (say, less than 1300 US dollars per user per month). In the outsourcing model, the IT solution maybe deployed at the client side, in which case the outsourcing company manages the software remotely, or it can be located at the provider's side.

Software Service Models

	Traditional	Open Source	Outsourcing	Hybrid	Hybrid+
Software Cost	$4000 /user (one-time)	$0 /user	$4000 /user (one-time)	$4000 /user (one-time)	
Support Cost	$800 /user /year	$1600 /user /year	$800 /user /year	$800 /user /year	$300 / user month
Management Cost	Up to 4x the cost of Software!		< 1300 /user /month	$150 /user /month	
Deployment Location	Client Side		Client or Provider Side		

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The hybrid model is an interesting model followed by large software vendors that sell software that are fairly standardized such as ERP/Financials/CRM etc. In this model, the software vendor creates a version of the software which is rapidly customized and deployed to clients and the vendor can automate support through remote access. Thus the company can substantially reduce costs to manage software by paying lower management fees. A more advanced form of this model is Hybrid+ where all the costs are combined into a flat monthly fee.

Software Service Models

	Traditional	Open Source	Outsourcing	Hybrid	Hybrid+	Cloud Computing
Software Cost	$4000 /user (one-time)	$0 /user	$4000 /user (one-time)	$4000 /user (one-time)		
Support Cost	$800 /user /year	$1600 /user /year	$800 /user /year	$800 /user /year	$300 / user month	< $100 /user /month
Management Cost	Up to 4x the cost of Software!		< 1300 /user /month	$150 /user /month		
Deployment Location	Client Side		Client or Provider Side			Provider Side

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With Cloud computing, and in particular, web-based IT solutions for businesses, a company develops one web-based version of the software and offers it to clients over the internet, thereby eliminating deployment costs. Since vendors can offer the same software to many clients the cost of the software comes down dramatically, even to the order or less than 100 USD per user per month.