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INVESTMENT TRENDS

Selling software as subscription

So-called SaaS idea has a future, says money manager

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Forget buying a box of software at your local retailer. The emerging way to obtain it is by subscription over the Internet.

From TurboTax and Photoshop to Salesforce.com and NetSuite, more and more software-makers are moving to the Software as a Service, or SaaS, model.

"To us, the companies that sell this type of service are attractive," said Dave Hackfort, vice president and portfolio manager at North Star Asset Management Inc. in Menasha. "They've got some unique characteristics that should help them grow over time."

Under a SaaS model, customers pay a monthly fee to access the software, which is housed on outside servers rather than on the user's computer. When customers log in, they know they'll have the most up-to-date version of their software, Hackfort said.

Business customers also have the advantage of being able to pay for software over time, rather than in big, up-front payments when it's installed.

"It takes a lot of cost out of the system by moving to an SaaS approach," Hackfort said.

From an investor's perspective, the SaaS model gives companies a much more consistent and predictable base of recurring revenue that weathers nearly any economic environment, he said. Customer retention rates tend to be higher, too, because users store their data on software-makers' servers, making switches to competing services costly and time-consuming, he said.

Hackfort

"That leads to pricing flexibility. Small price increases over time won't deter customers," Hackfort said.

Many companies are adopting the SaaS model:

Adobe Systems Inc. (ADBE, $71.60) is moving its software that creates and measures the effectiveness of advertising to an SaaS model. VeriFone Systems Inc. (PAY, $36.56) is starting to sell services rather than credit card payment terminals for checkout. Intuit Inc. (INTU, $88.81) is transitioning its QuickBooks and TurboTax products to subscription offerings rather than boxes of software. ACI Worldwide Inc. (ACIW, $18.52) is beginning to offer its electronic payments-enabling software as a service.

Bottomline Technologies Inc. (EPAY, $25.20), Portsmouth, N.H., automates financial processes such as invoicing and payments for customers worldwide.

ABOUT THIS

The Journal Sentinel focuses on one Wisconsin money manager or analyst in this weekly feature, looking at a trend that helps investment pros make their decisions.

A staggering 90% of all business-to-business invoicing and payments are still being done through the postal service, so the company has ample opportunity to grow, Hackfort said.

Bottomline has a strong balance sheet with more cash than debt, and its valuation is in line with that of the overall market, he said.

Bottomline's stock pulled back late last month after the company said it would invest in research and development and a sales force for three new products, a move that will hold back margins for a year or two, Hackfort said. But the products will drive growth over time, he added.

"So we think it's an attractive time to buy," Hackfort said.

The biggest risk to Bottomline is the possibility that the company could fail to execute a successful launch of its new products and fail to ramp up sales for them, he said.

Bottomline shares have a 52-week trading range of $24.17 to $37.41. They could trade as high as $31 over the next 12 months, Hackfort said.