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Houston Neal

2010 Manufacturing Software State of the Industry Roundtable - Part Two

Posted on May 6, 2010 at 2:11 pm | 1 Comment

This is the second installment in our Expert Roundtable Series covering the state of the manufacturing software industry. In part one, we reported buying activity, spending patterns by business size and industry, and primary motivations behind current buying activity. Here in part two we'll review activity in the software as a service (SaaS) market, how vendors are adjusting prices to compensate for the economy, how offshoring influences spending and whether manufacturers are implementing integrated enterprise resource planning (ERP) systems or best-of-breed applications. First, we'd like to introduce our experts.

About the Experts

Jonathan Gross is Vice President at Pemeco, an independent and impartial IT advisory firm. He provides the following services: IT-business alignment, systems selection and systems implementation. He is an IT/ERP columnist for Manufacturing AUTOMATION, an expert at Focus Research and a blogger at IT-Toolbox.

Ned Lilly co-founded xTuple, originally called OpenMFG, in October 2001, with the aim of bringing open source and ERP software together to solve the unmet needs of small to midsized manufacturers. Before that he was a co-founder of Great Bridge, an early attempt to build a business around the PostgreSQL open source database. PostgreSQL is the core technology that xTuple uses today. Ned is also well known for his ERP Graveyard blog.

Nancy Phillippi is the senior sales consultant at Custom Information Services (CIS). She has 13 years experience in helping Process Manufacturers, Distributors and companies that have complex accounting or manufacturing processes. You can read her articles on manufacturing on the CIS website or on the ERP Software Blog. Randy Smith is the CEO and co-founder of Vicinity Manufacturing. Vicinity was founded in 2002 with the goal of building a manufacturing system written specifically for formula-based manufacturers.



Manufacturing Software Trend Summary

Software as a Service



Manufacturing ERP Software Pricing



Integration Across Plants and Supply Chain



Best-of-Breed Applications



Integrated ERP Suites



Software as a Service (SaaS) Solutions Popular Among Small and Medium Enterprises

SaaS solutions are gaining momentum, especially among small- and medium-sized enterprises (SMEs). The primary driver is the low barrier to implementation. Many resource-constrained SMEs do not have the same level of IT sophistication or infrastructure that their larger counterparts do.

Jonathan Gross: SaaS solutions are gaining momentum, particularly among the SME segment. One of the primary drivers is the fact that end-users are not required to support and maintain the software. The provider does this work. This relieves pressure on overly stretched or unsophisticated IT departments. Another key driver is that no supporting infrastructure (databases, networks, etc.) is required. In contrast, on-premise ERP systems often require expensive supporting infrastructure.

Despite increased adoption, many buyers are still circumspect in their evaluation of SaaS. Data security, service disruption and apprehension to host critical data off-site remain the most cited reasons for incredulity.

Nancy Phillippi: Clients still want control of where their server is located and the apparent ease of access, even though this is not a real issue, just a perception. I have had some interest in this solution, however no matter how savvy the customer is, the issue of secure formulas and bill of materials is still at the forefront. The mind set will need to change to trust the SaaS model just as if the server was in their building.

Ned Lilly: It's one option, one of many that we believe customers should have. Several of our partners offer xTuple ERP as a hosted service, and we're experimenting ourselves with a service in the Amazon EC2 cloud. But there are still a large number of people, particularly financial people, who prefer to have the

system onsite.

All things considered, we expect SaaS solutions to grow in popularity. Most SaaS shortcomings have been addressed (read "The SaaS Dilemma"), and manufacturers are increasingly embracing this deployment option.

Software Vendors Adjust Prices to Compensate for the Recession

As we noted in part one of this series, the recession created pent-up demand as many companies delayed their ERP projects. This has placed pressure on software vendors' revenues, which has prompted many to drop their prices.

Nancy Phillippi – Vendors have reduced pricing to spur sales at the cost of profits. Product specials is the primary way vendors facilitate price reductions. Specials allow vendors to state end dates to the pricing, therefore customers do not have the mindset that this is a permanent price change.

Meanwhile, manufacturers have tighter IT budgets and are demanding more from their investments. Consequently, vendors are competing on a cost basis and are reducing both license and maintenance fees. Jonathan Gross summarizes three key ERP pricing trends:

License fees: With increased vendor competition, the vendor fight is now about market share. Over the last year and a half, vendors have slashed the prices of ERP licenses. Many are also prepared to negotiate with individual customers. In a recent case, SAP discounted its license fees by 64% to secure a particular client. Further, in a bid to reduce the up-front capital costs, some vendors are offering payment plans. Finally, many vendors now offer purchase financing.

Increased incentives: Many vendors are using various incentives to entice buyers. Common incentives include: additional training, reduced maintenance fees, and lower implementation costs.

Maintenance fees: Buyers are fed up with paying high maintenance fees, particularly since they do not believe that they are receiving corresponding value. Many vendors are prepared to negotiate lower prices given buyer dissatisfaction and the emergence of third-party competition. In our view, companies like Oracle and SAP will not be generating 90% profit margins on maintenance fee revenues for much longer.

More Manufacturers Seek Integration Across Offshore Facilities

As a growing number of manufacturers move offshore, facility and supply chain integration is becoming a greater – and often requisite – driver of ERP software acquisition. Why? Many manufacturers find it difficult to communicate with and manage offshore plants and partners.

Nancy Phillippi – Overseas plant communication can be an issue for parent companies located in the USA. Often times the ERP package the USA company is running is not offered in a localized language for the overseas company, so they will run separate systems.

Alternatively, manufacturers are acquiring modern ERP systems to electronically integrate their plants and supply chain. As Ned Lilly points out, most modern ERP systems should provide support for multiple languages and currencies.

Ned Lilly – We see a great deal of interconnection between domestic and offshore operations. Additionally, the vast majority of our customers do some portion of their sales globally as well. Any ERP system worth its salt should be multicurrency, multilingual, and support multiple tax structures out of the box.

In an interesting twist, SMEs are acquiring ERP software just to make a business case for offshoring.

Jonathan Gross – The ability to electronically administer disparate facilities has helped SMEs make the business case for offshoring. Previously, high administrative costs oftentimes offset cost-saving opportunities in developing countries. With integration, those administrative costs can be significantly reduced, making offshoring a more attractive alternative.

New ERP Buyers Seeking Integrated Suites Over Best-of-Breed Applications

The choice between implementing an integrated ERP suite or best-of-breed applications is now easier than ever. Why? The functional gaps between the two offerings have started to narrow. ERP software vendors are enhancing the functionality of their modules, adding vertical depth and acquiring best-of-breed applications into their ERP suites. As Jonathan Gross points out, "deciding between ERP and best-of-breed applications is no longer an issue that involves a balancing of clear tradeoffs."

For this reason, we find the majority of first-time ERP software buyers are implementing integrated ERP software suites. However, best-of-breed deals are still getting done. Larger manufacturers and those with legacy ERP systems are following a piecemeal approach, adding and extending functionality as needed.

Ned Lilly – The general trend is that smaller companies tend toward one integrated system, while larger IT organizations seem to prefer best-of-breed. For core ERP functionality, we believe it's best to stick with an integrated system. Having said that, our open source ERP has a rich API, and our customers and partners have done all kinds of integrations into separate, adjacent systems – such as ecommerce/shopping carts, EDI systems, CAD/CAM/PLM, and many more.

Jonathan Gross – From what we see, manufacturers that operate stable, legacy ERP systems are more likely to extend functionality with best-of-breed applications. However, companies seeking new ERP systems are less likely to acquire best-of-breed applications because many of today's ERP systems are functionality-rich, industry specific solutions.

We provide a framework for making the best-of-breed versus integrated suite decision at: Best-of-Breed or Integrated Suite? 10 Questions to Consider

This concludes our 2010 report on the state of the manufacturing software industry. Please feel free to comment on the trends we describe above, or share your observations on shifts taking place in the market. And be on the lookout for future installments of our Expert Roundtable Series.

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Great analysis! As a software vendor, we've certainly noticed some of the trends you've outlined above taking shape for us in 2010. Interest in SaaS has increased substantially and buyers are tending to express more interest in purchasing the full suite than they were in previous years.

I've written up some thoughts about what we're seeing over at Slingshot's blog: <http://blog.slingshotsoftware.com/bid/40553/Weighing-In-On-Manufacturing-ERP-Software-Industry-Trends>

Comment by Allen Williams
May 21, 2010 @ 7:33 am

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