Unlocking the Secrets of Physical Product-As-A-Service

AUTHORS:
MICHAEL MANSARD,
EMEA CHAIR OF THE SUBSCRIBED INSTITUTE AND PRINCIPLE DIRECTOR OF SUBSCRIPTION STRATEGY, ZUORA
YANN TOUTANT, CEO AND FOUNDER, BLACK WINCH

Unlocking the Secrets of Physical Product-As-A-Service:

THE 8 UNTAPPED FOCUS AREAS FINALLY REVEALED AND DEMYSTIFIED BY SEASONED EXPERTS. EMBARK ON A JOURNEY INTO THEIR "REAL-LIFE" METHODOLOGY.

Michael Mansard, EMEA Chair of the Subscribed Institute and Principle Director of Subscription Strategy, Zuora

Michael is a seasoned Subscription Economy business strategist. Since he joined Zuora in 2015, he has been accompanying more than 350 companies globally and across industries in their business model transformation.

Those companies range from fast-growing start-ups to large enterprises (Philips, Siemens, Assa Abloy, Schneider Electric, St Gobain, Ubisoft, Doctolib, Renault-Nissan, and more).

Leveraging his 15-year experience at Deloitte Consulting, SAP, or as a start-up mentor, he has developed an original multidisciplinary profile in Sales & Marketing, Finance, and IT.

He currently serves as Principal Director, Business Transformation & Subscription Strategy within Zuora's Chief Revenue Officer's group, and is also the Subscribed Institute's EMEA Chair.

He recently authored several thought leadership pieces - such as Industry 4.0: an executive playbook for business model transformation, Subscription Economy Maturity Model, or A new formula for growth: The Financial Services Industry and the Subscription Economy.

Alongside Professor Wolfgang Ulaga, he is the co-creator of the Subscription Economy Bootcamp program at INSEAD.

As an investor and advisor, Michael is working very closely with 6 hyper-growth start-ups, in the fields of FinTech, FoodTech, MarTech, MedTech or PropTech—which are all subscription-based businesses.

Yann Toutant, CEO and founder, Black Winch

Yann Toutant has been implementing subscription-based models for hardware in the IT industry for 25 years, 12 years of which as CEO of Econocom's Dutch operations. Today with his own company, Black Winch, he helps CEOs and their teams to focus on the user experience by incorporating all components of an As-A-Service offer into a single in-house comprehensive, scalable subscription model.

Yann's first Book, 'As-A-Service'—How to turn your product based business into a subscription model was published in early 2022 with the aim of spreading his commitment to connect As-A-Service and circularity.

Yann is a passionate advocate for the circular economy and believes manufacturers have the power to make steps towards preserving our earth's precious resources. One way to do this is to shift their business from being product-based to an "As-A-Service" subscription model. As-A-Service allows manufacturers to remain owners of their products, transferring "usership" instead of ownership to their customers. This means being responsible for creating a good customer experience and service, as well as reusing and recycling materials—something customers are increasingly requesting.

But how do you turn a product-based business into As-A-Service? How to navigate from using this buzzword to actually implementing a successful and scalable in-house AS-A-Service business model? There is a large selection of books available about software As-A-Service, but none of them addressed product-based businesses. This, along with Yann's years of experience both personally and within his career lead him to the decision to write his first book.

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One-of-its-Kind Product-As-A-Service Guide

TAILORED FOR EXECUTIVES FROM THE "PHYSICAL PRODUCT WORLD"

In the present economic climate characterized by declining growth rates, inflation and postponed investments from customers and consumers, agile business models have become imperative for capturing untapped demand. The phrase "As-A-Service" has emerged as a popular buzzword, garnering widespread interest and fascination among industry experts and business leaders alike. This concept has captivated the attention and imagination of professionals across diverse sectors.

As-A-Service entails delivering assets (Product, Software, Platform, Infrastructure, Storage, etc.) through a subscription model, with customer-centricity at its heart. The As-A-Service model has taken the software and cloud industry by storm, becoming the dominant paradigm in those sectors. However, when it comes to physical products, true As-A-Service offerings are still in their early stages and face unique challenges. One key challenge is the fact that unlike digital goods, physical products involve tangible assets that incur incremental costs with each additional unit provided to a subscriber, thereby exerting a significant impact on a provider's balance sheet and cashflow. As a result, the creation of As-A-Service offerings for physical products requires a thorough assessment of funding strategies, residual values, and the identification of secondary markets.

Despite the fact that the As-A-Service literature is quite vast, executives from the "physical product world" are often left behind due to the lack of concrete guides on deploying Product-As-A-Service (PaaS) models. Obviously, many learnings from the digital do apply. But the vast majority of literature falls short when it comes to explaining what to do from a funding, finance, and accounting standpoint. As a result, we see too many As-A-Service projects in the physical product world being stalled or delayed, if not simply canceled. That's why we've made it our mission to focus on these crucial aspects.

Despite the complexity and effort, the rewards can be massive. Let's take a concrete example: Philips Enterprise Monitoring as a Service (EMaaS). EMaaS is a pay-per-use model that standardizes patient monitoring capabilities in hospitals with a holistic view of performance data to drive improvement. Philips owns the system and customers pay for what is used (tied to patient volume). This transforms Philips from a product seller to a service provider, increasing service-level expectations, adding continuous engagement touchpoints, and requiring quality adherence. For the end-users, such flexible pay-per-use models mean predictable expenses, use of OPEX (Operating Expense) budget (as opposed to CAPEX Capital Expenditure Budget), no finance charges, payment model tied to real usage, and end-to-end services included to support full adoption (See Figure 1 on page 6).

EMAAS IS TIED TO YOUR PATIENT VOLUME

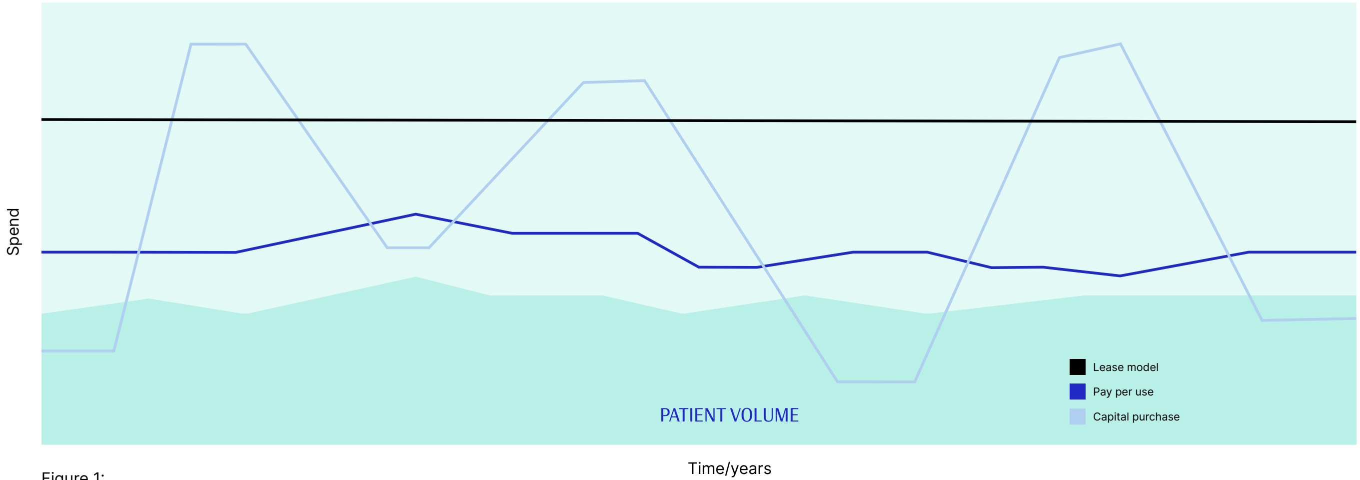


Figure 1:
Source: Philips

	Pay-per-use service	Capital purchase	Lease model
Predictable and stable YoY spend	+	–	+
Part of OpEx budget	+	–	+
No finance charges	+	+	–
Tied to patient volume	+	–	–
Includes services to support full adoption	+	–	–

The example of Jackson Memorial Hospital's partnership with Philips under EMaaS illustrates the value of this model. Jackson had concerns about their aging monitoring technology and desired access to state-of-the-art equipment and services. The Philips EMaaS solution addressed their challenges by providing access to critical monitoring capabilities, eliminating upfront costs, and offering ongoing optimization, education, and asset management services. The impacts included significant time savings (8 hours a day saved for the central monitoring unit telemetry technicians through automated measurement and export), increased nurse satisfaction (90% satisfaction rate), and an integrated approach involving Philips experts to address organizational needs beyond technology and financing, including baseline assessment with monitoring methodologies and systems best practices to improve patient management and care capabilities.

What shortcuts can we learn from this success story? What are the best practices? What pitfalls should be avoided? We will see in this whitepaper that the Philips story is not a mere exception, but the beginning of a business model tidal wave! This whitepaper will offer you the essential advice for effectively building your own PaaS solution. And, unlike any other, we'll delve into the '3-10-50 funding strategy' employed by industry leaders. Get ready to unlock the secrets of PaaS and revolutionize your business.

PHILIPS*

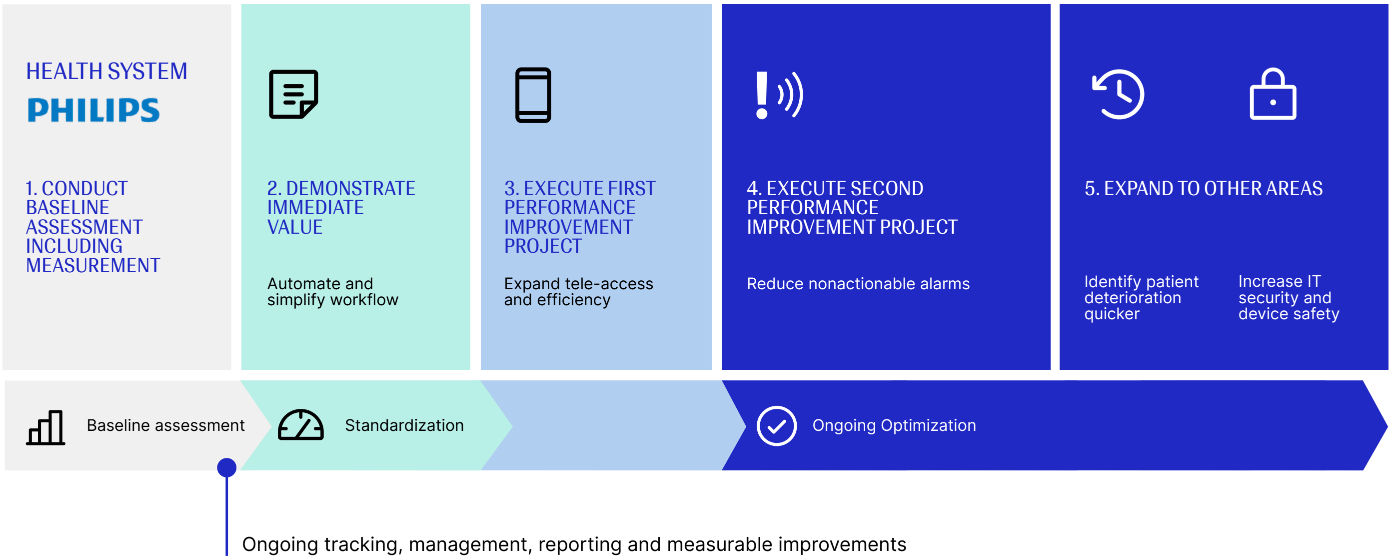


Figure 2
*Source: Philips

The Incredible Power of the Product-As-A-Service Industry

Curious to know who the big players are in the world of Product-As-A-Service? Wondering which industries they dominate? Feast your eyes on the visual below, which will shed light on this entire model. Many sectors, including IT, machinery, healthcare, energy, and transport, are adopting the Product-As-A-Service trend.

When it comes to IT, Apple, ACER, Lenovo and Panasonic are leading the charge with their innovative As-A-Service programmes. But there are other exciting solutions out there too! Ever heard of Drilling-As-A-Service from Atlas Copco? How about Light-As-A-Service with Signify? And let’s not forget about Michelin, who’s revolutionizing the game with their Tyres-As-A-Service concept.

Get ready to dive into the world of Product-As-A-Service. It’s a thrilling ride filled with groundbreaking ideas and industry leaders who are reshaping the way we consume and experience products.

Product-As-A-Service Top Players

IT

- Lenovo
- FUJITSU
- Panasonic
- SAMSUNG
- hp
- xerox
- CTOUCH
- Dustin

MACHINERY

- HILTI
- LOXAM
- FESTOOL
- JBT
- CATERPILLAR
- DASSAULT SYSTEMES
- Atlas Copco
- EPOS
- KÄRCHER
- MITSUBISHI
- xerox
- HEIDELBERG

HEALTHCARE

- SAFECHEM be responsible
- BASF We create chemistry
- PENTAX MEDICAL
- stryker
- GE HealthCare
- Honeywell

ENERGY

- signify
- Schneider Electric
- Carrier

TRANSPORT

- Swapfiets
- MAN
- MICHELIN
- woom
- riversimple

FURNITURE

- NOR NORM
- move & rent
- CHAINABLE
- Lyght Living
- ahrend
- Martela

BUILDING

- blitta THE BEAUTY OF INNOVATION
- VOLVO Volvo Construction Equipment
- SRV
- MHWILLIAMS CONSTRUCTION GROUP
- ArcelorMittal
- ZEPPELIN WE CREATE SOLUTIONS
- klarx
- LOXAM

AGRICULTURE

- EKOBOT
- JOHN DEERE
- hello tractor
- CULTIVATD
- H&A
- BEEQUIP

ROBOTS

- KUKA
- LOCUS ROBOTICS
- INVIA ROBOTICS
- Relay ROBOTICS
- KNIGHTSCOPE
- fetch robotics
- ambi ROBOTICS

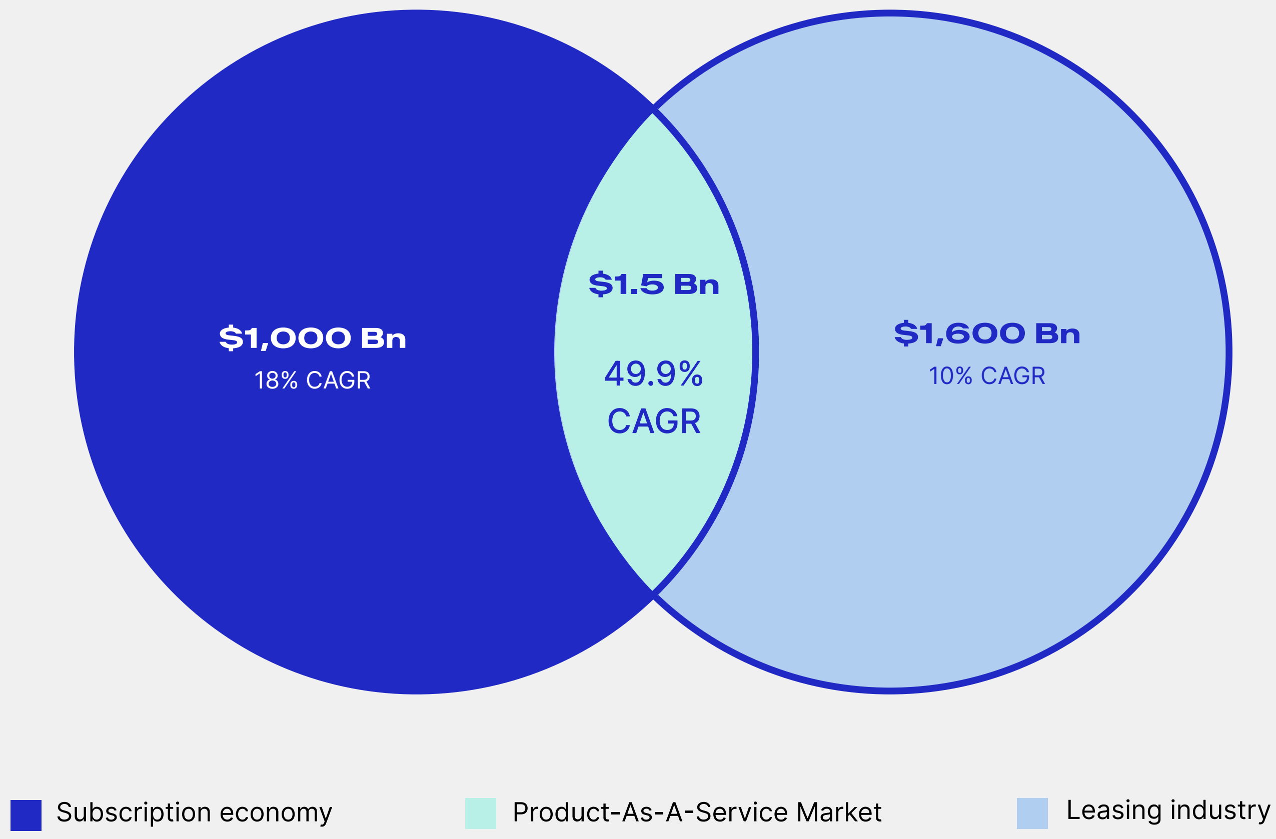
FITNESS

- Life Fitness
- TECHNOGYM

When implemented effectively, Product-As-A-Service models provide comparable advantages in terms of flexibility and scalability as Software-As-A-Service solutions. By embracing these models, enterprises can effortlessly adjust their usage in accordance with demand, allowing them to promptly adapt to evolving market dynamics. Alternatively, they have the option to easily opt in or opt out from a solution as required.

Similarly, Product-As-A-Service undoubtedly represents a significant step towards the implementation of circular economy principles. In fact, it can even be viewed as a strategic approach that acts as a catalyst for achieving circularity. Product-as-a-service models inherently possess a high degree of flexibility, allowing customers to choose to opt in or out, or pay based on usage. Consequently, it becomes imperative to ensure that the same product can be offered to other users when it is no longer required by the previous customer. This is an inherent consequence of the flexibility offered by these models and plays a crucial role in effectively managing associated risks. Therefore, Product-As-A-Service models can be considered as circular in nature. Furthermore, these Product-As-A-Service models concentrate the risk of ownership solely on the manufacturers, rather than dispersing it among multiple users. As a result, manufacturers bear the responsibility of caring for their products, extending their lifecycle, and implementing appropriate circular models. This approach serves as a gateway to achieving circularity, as it encourages manufacturers to adopt sustainable practices and embrace the principles of the circular economy.

MARKET OVERLAP



According to UBS, the Subscription Economy market, which encompasses both Product-As-A-Service (PaaS) and Software-as-a-Service (SaaS), is poised for significant growth, with projections indicating an increase from USD 650 billion in 2020 to USD 1,500 billion in 2025. Currently, PaaS represents a small portion of the overall Subscription Economy market, with SaaS comprising the extreme majority. This presents a significant growth opportunity for manufacturers.

If we focus solely on the global Equipment-as-a-Service (EaaS) market, also referred to as Product-as-a-Service (PaaS), it is currently valued at USD 1.5 billion in 2023 and is expected to expand at a compound annual growth rate (CAGR) of 49.9% from 2023 to 2030, reaching USD 27.8 billion, as reported by Grand View Research.

Let's look at the bigger picture: the traditional leasing market is valued at USD 1,674 billion in 2023 and is projected to grow to USD 2,424 billion in 2027 at a CAGR of 9.7%, according to Research and Markets. The natural overlap between the two markets could result in PaaS becoming a substantial segment within the Subscription Economy.

Furthermore, the Subscription Economy Index (SEI) reveals that subscription-based companies within the SEI have demonstrated a growth rate 3.7 times faster than companies listed in the S&P 500 over the past 11 years, according to Zuora's Subscribed Institute. What's more: subscription businesses have demonstrated impressive resilience in times of crises, with 4 out of 5 businesses continuing to grow in 2020 during the COVID-19 pandemic as a striking proof point. This data suggests a promising opportunity for growth within the PaaS market.

Switching to Product-As-A-Service models can be a complex endeavor, but the benefits it brings make it well worth the effort. We see many companies freezing or fleeing in front of this intimidating task. While there are certain pitfalls to avoid, the advantages of adopting an As-A-Service approach far outweigh any initial challenges.

So, what are the concrete steps to make Product-As-A-Service happen within your organization? What plan to follow? What challenges can occur along the way and how can they be overcome?

A Journey Through Time

PRODUCT-AS-A-SERVICE IS THE NATURAL EVOLUTION OF THE RENTAL INDUSTRY

- In the 80's, the first rental solutions were provided by financial institutions (Equipment Finance organizations).

- In the early 90's, independent players (e.g. Econocom, CHG, Leaseplan for cars, Xerox for copy machines etc.) entered the market with their capacity to invest in residual values (e.g. estimated value of a fixed asset at the end of its lease term or useful life).

- Then, captive entities - which are essentially a wholly-owned financing subsidiary of an organization that provides financial services to its customers, such as. Cisco Finance, Dell Finance or Apple Financial services, entered or reentered the market. Why?
    1. They wanted to address their customers' needs for financing in a simpler way and act as a one-stop-shop.
    2. They wanted to retain some level of relationship with their customer, instead of handing it over to an independent financing
    3. They wanted to create a strong margin lever, i.e. up to 15% margin expected by the captive instead as compared to 5% on average in traditional product sales.

- In the year 2000, in order to answer market demand for complete rental and faster time to value solutions, managed services were added to the existing rental models creating a full service offering (e.g. IBM IT Managed Services including Helpdesk support, authentication, system management, data backup, cloud transformation etc.).

Let's pause for a moment and reflect: was all the hard work put into this evolution truly worth it? By shifting away from the rental options provided by financial institutions and bundling their top-notch products with exceptional services, manufacturers have not only offered more value to their customers but also witnessed a staggering 15-25% increase in revenue and 5%-8% boost in their profit margins on average and depending on the industry.

- Nowadays, the next natural evolution taking place consists in adding full flexibility to the existing rental solutions via Pay-Per-Use and/or Opt-In/Opt-Out offerings, instead of flat inflexible contracts where customers are locked-in and where value capture and delivery are disconnected. (Ex. Signify (formerly Philips lighting) offers a pay-per-use offering (called "Pay-Per-Lux") providing the exact amount of light for workspaces based on the customer's specific needs. The offering includes a full lighting service - design, equipment, installation, maintenance and upgrades, and clients only pay for the light they consume.

PRODUCT-AS-A-SERVICE: NATURAL EVOLUTION OF THE RENTAL INDUSTRY

5. PRODUCT AS A SERVICE

Customer-centric and data-driven sales model that prioritizes full flexibility through pay-per-use and opt-in.opt-out solutions
Ex. Share Now Car-as-a-Service, Michelin Tires-as-a-service, Philips Monitoring-as-a-service, BASF price per gallon, Steelcase Furniture-as-a-service

4. MANAGED SERVICES

Rental models with full service offerings.
Ex. IBM IT Managed Services, ATOS managed services etc.

3. CAPTIVE ENTITIES

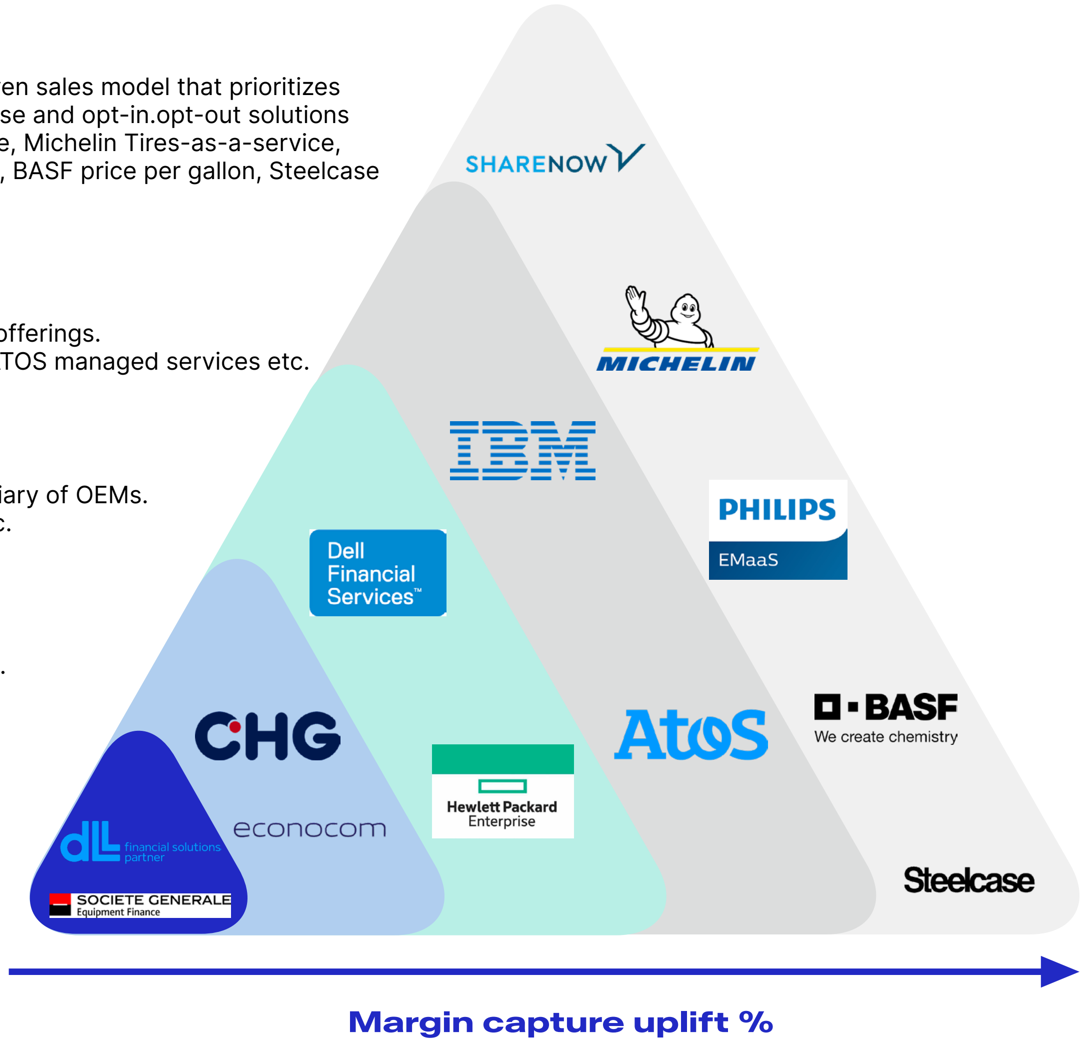
Wholly-owned financing subsidiary of OEMs.
Ex. HP Finance, Dell Finance etc.

2. LEASING

Leasing by independent players.
Ex. CHG, Econocom etc.

1. EQUIPMENT FINANCE

Equipment finance by financial institutions.
Ex. BNP, DLL,
Societe Generale etc.



Source: Black Winch - All rights reserved.

As organizations strive to innovate and outperform their peers, embracing the As-A-Service model becomes a bold but necessary move. This transformative approach requires a complete shift in mindset, as it places an enormous emphasis on being client-centric throughout the entire journey.

If you are reading this whitepaper, it means you possess the right mindset and have a clear vision in mind. However, embarking on such a transformative journey cannot be done alone. It requires convincing key stakeholders within your organization and presenting them with a detailed action plan.

Identifying and Convincing C-Suite Executives for Your As-A-Service Programme

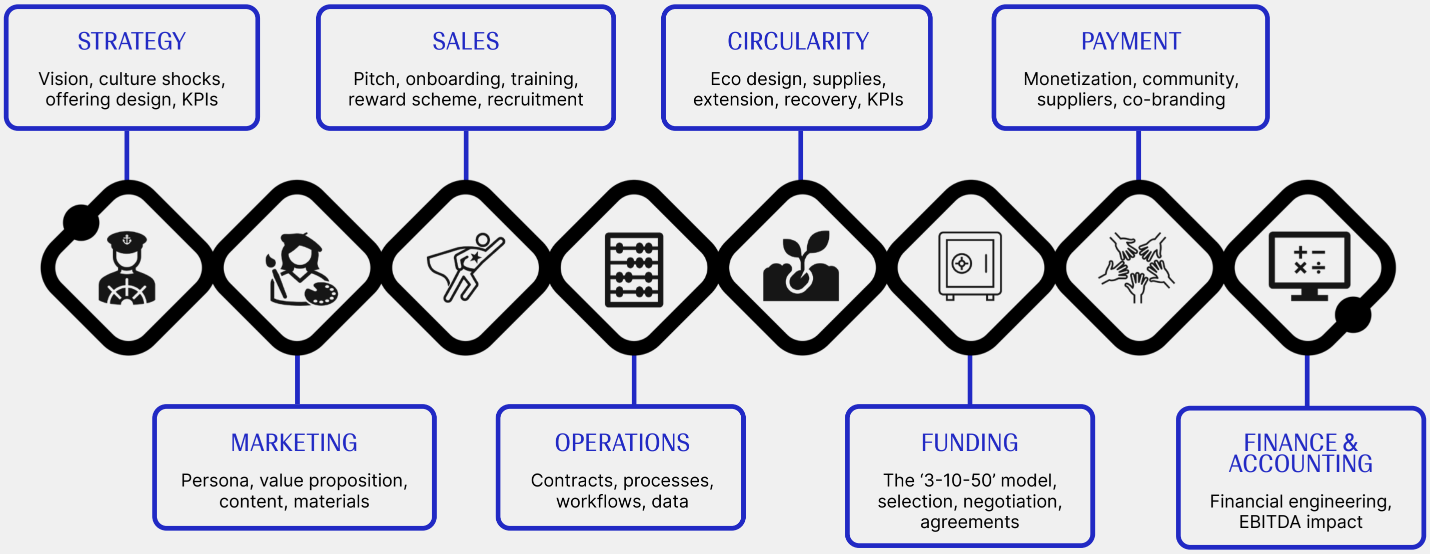
Implementing a transformative As-A-Service model is a challenging task. Of course, you can't convince everyone. But you need to and most likely shouldn't - at least to get started in the journey, or else you might get stuck trying to!

Often, CCO/CMO/CTOs are the most enthusiastic about such models, especially when looking for new growth platforms in atonic markets or for their latest innovation. Alongside these leaders, the key allies you need when building an As-A-Service programme are typically the Regional / Country leaders, the Chief Financial Officer (CFO), the Chief Operations Officer (COO) and your investors. At first, CFOs and COOs may be the biggest opponents to such models. Yet, they can turn into the strongest promoters once convinced. For good reason: they are the "guardians of the temple" when it comes to margin discipline and compliance.

- Convincing the Regional / Country Leaders of the benefits of the As-A-Service model is crucial. They can help align resources and priorities accordingly and their support can help rally other employees behind your As-A-Service programme.
- Demonstrating to your CFO how the As-A-Service model can lead to recurring revenue, increased margin, or improved shareholder value, is table stakes to get things in motion. However, you will also need to anticipate discussions and be prepared to collaborate around cash flow and balance sheet impact, financing strategies, accounting principles or risk and fraud management to fully win their endorsement (cf. points 6,7 and 8 of the whitepaper).
- When launching your As-A-Service programme internally, it is crucial to gain the support and confidence of your investors. This holds true for both private and public equity scenarios, and becomes even more challenging when covenants are involved. However, it is important to recognize that adopting the Product-As-A-Service model is a strategic approach to drive business growth and expansion. This understanding should aid in effectively persuading investors and demonstrating a promising return on investment.

When it comes to translating your vision into reality, having a clear roadmap is essential. This roadmap should encompass various focus areas that need to be reviewed in order to successfully make Product-As-A-Service part of your DNA. The top 8 focus areas are: strategy, marketing, sales, operations, circularity, funding, payment and finance & accounting.

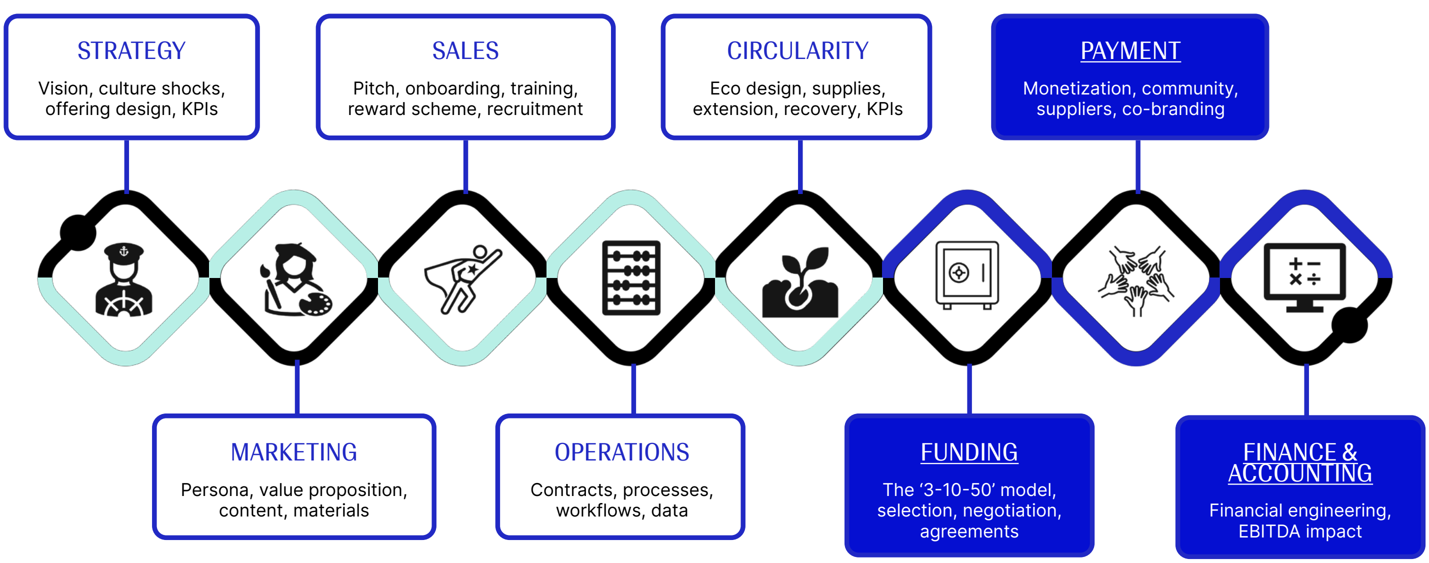
THE 8 PRODUCT-AS-A-SERVICE FOCUS AREAS



This whitepaper will delve into each focus area, with a deliberate emphasis placed on the '3-10-50 funding strategy', as well as accounting and payment facets. This emphasis is justified due to the evident lack of comprehensive literature on these subjects.

If you're already at ease with typical As-A-Service transformation, we recommend you to proceed directly to points 6, 7 and 8. There, you will find very specific and pragmatic recommendations.

EXCLUSIVE FOCUS ON FUNDING, PAYMENT & FINANCE ACCOUNTING



The Journey to Product-As-A-Service

MAPPING OUT YOUR ROADMAP FOR SUCCESS

1. STRATEGY

In order to successfully incorporate As-A-Service into the overarching vision of your organization and to guarantee its contribution to shareholder value, it is imperative to undertake a thorough evaluation and adjustment of your business strategy. This involves evaluating your current offerings and identifying areas where an As-A-Service model can be implemented. Consider the scalability of your products, customer demand for subscription-based models, and potential revenue streams that can be generated through this approach.

Defining your ambitions is essential when integrating As-A-Service into your company vision. Clearly articulate what you aim to achieve through this new business model – whether it's securing recurring revenue streams, boosting margin, improving customer stickiness etc. Following the evaluation of your Product-As-A-Service solution and analysis of historical data, you should be able to determine your As-A-Service penetration rate objective, which outlines the proportion of your annual revenue generated through the As-A-Service model, such as 10%, 20%, 50% etc.)?

It is also imperative to engage in strategic discussions with your Chief Financial Officer (CFO) in order to meticulously plan various scenarios that evaluate the consequences of transforming key performance indicators (KPIs) such as Cash Flow, Revenue Recognition and Net Financial Debt. This comprehensive assessment will play a pivotal role in determining the direction and speed at which the As-A-Service transformation should proceed.

"OUR OBJECTIVE WAS TO SWITCH FROM A 10% AS-A-SERVICE PENETRATION RATE TO 40% IN 2 YEARS. IT'S ONLY AFTER CAREFULLY ADAPTING OUR ENTIRE BUSINESS STRATEGY AND DEFINING RELEVANT KPIS THAT WE MANAGED TO CONFIDENTLY WORK TOWARDS THIS GOAL."

Managing Director - European Solar Panel Manufacturer.

2. MARKETING

Marketing faces numerous considerations when launching a new As-A-Service value proposition. One of the primary responsibilities entails a complete reevaluation of segmentation and the identification of a fresh persona with an entirely new promise. Subsequently, the following considerations must be taken into account:

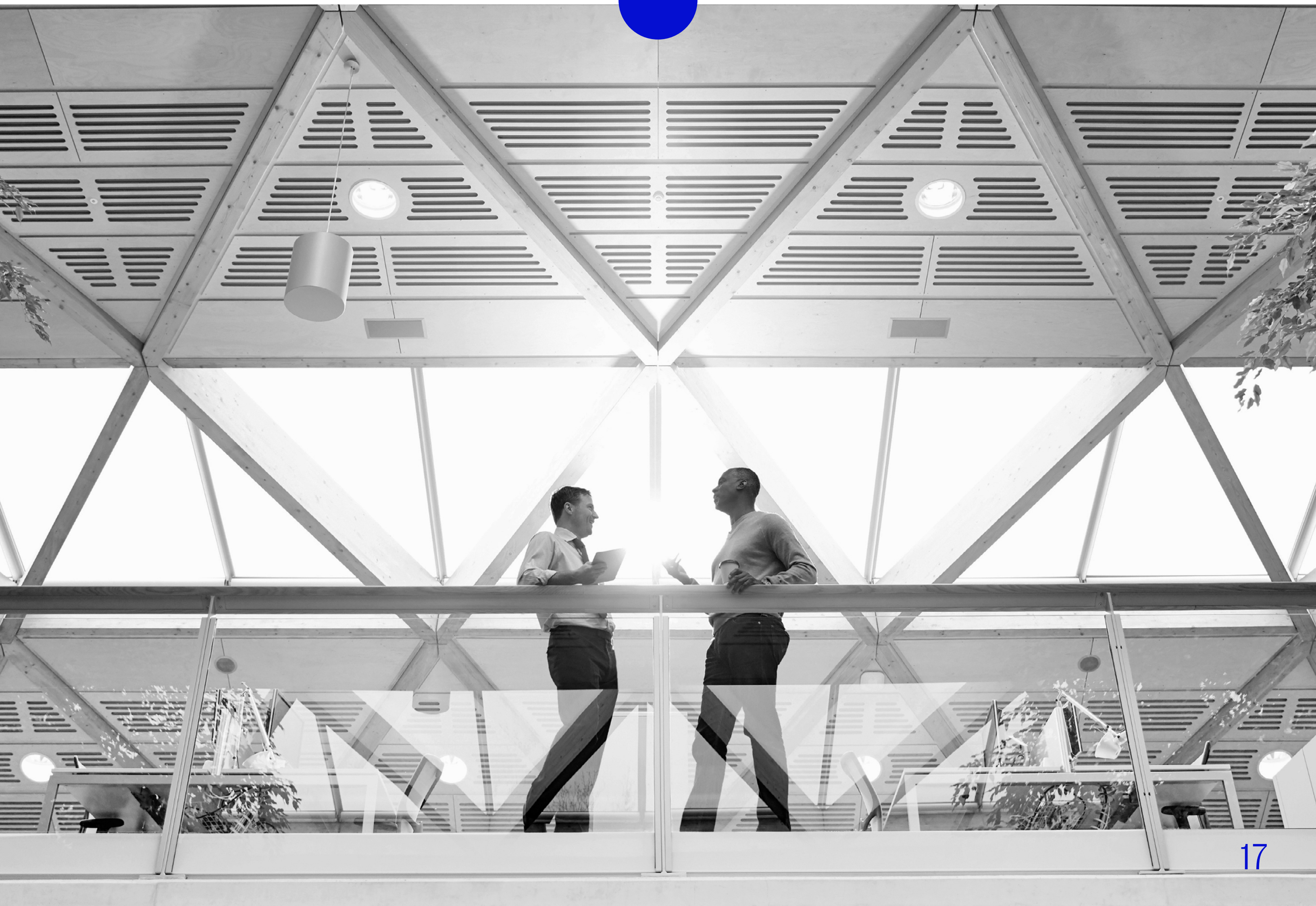
- How will the new value proposition be effectively communicated to the intended target audience? When you make the switch to a PaaS model, it's not just a simple change in how you offer your product. It's a whole new way of designing, pricing and packaging your offering. The new PaaS solution can't simply be seen as a principal and an interest rate. You are not just offering a product, but a whole new way of doing things. So, when it comes to marketing your new offering, your messaging should ca pture the essence of this paradigm shift and showcasing the value you bring.

- Will the creation of a new business name accompanied by a new logo be necessary, or will it be integrated into the existing branding?
- Is a separate website / dedicated sales channel required?
- What marketing materials will be compelling for your new persona? How will they be designed and disseminated?
- Which lead generation strategies will be adopted? Etc.

Product-As-A-Service offers a whole new level of experience for your customers, and consequently, for your own company as well. It's time to step out of the box and market this game-changing concept in a way that captivates and entices your target audience.

"OUR MARKETING DEPARTMENT WAS INSTRUMENTAL IN TAKING OUR CIRCULAR VALUE PROPOSITION TO THE MARKET. THEY WENT WAY BEYOND SIMPLY ADDING RENTAL PRICES TO OUR EXISTING SALES MATERIALS. THEY DEFINED A NEW SET OF PERSONA INCLUDING THE CFO, CTO AND CSO AND CARRIED OUT THOROUGH RESEARCH TO UNDERSTAND THEIR DRIVERS AND PAIN POINTS. THEN, THEY REDESIGNED AN ENTIRE NEW NARRATIVE WITH SUPPORTING MESSAGING FOR EACH OF OUR TARGET GROUP."

Chief Transformation Director - Leading specialist in workplace and office fit-out



3 - SALES

The As-A-Service sales journey is very different from a traditional one-off transactional one.

Converting a customer who is used to buying to a renting model requires specific skills and a different pitch. The focus should be on the customer experience instead of price and specifications. Similarly, refreshing contracts of existing As-A-Service customers requires another skill-set. The expertise, the pitch and the team members required are different for each.

It is essential to select As-A-Service sales champions within your organization and offer them personalized As-A-Service training programmes to help them navigate the As-A-Service sales methodology with confidence.

Setting up appropriate reward schemes will incentivize your sales team to prioritize As-A-Service offerings over traditional transactional sales. Therefore, we strongly advise you to assess your commission plans and incorporate both positive and negative incentives. Despite being frequently disregarded, this is, in fact, one of the most crucial impediments to achieving optimal As-A-Service performance.

When it comes to selling As-A-Service offerings, salespeople must always keep their eye on the end goal. One crucial tip for achieving success in this field is to collect maximum data points throughout the customer's journey. By doing so, salespeople can be proactive when it comes time for renewal.

Using the monthly price paid by customers as a starting point for building renewal offers is crucial. This approach ensures that the renewal offer is aligned with the customer's budget and expectations and secures you a profitable sale.

"GIVING SALESPEOPLE A GOAL TO STRIVE TOWARDS IS NOT SUFFICIENT (I.E. 30% OF YOUR ANNUAL SALES SHOULD BE DONE VIA AS-A-SERVICE) ; THEY ALSO NEED HIGH-QUALITY RAINING AND THE RIGHT BONUS SCHEME TO ACHIEVE THAT GOAL.FOR EXAMPLE, BY ADDING AN ACCELERATED BONUS PLAN FOR OUR SALES, WE INCREASED OUR AS-A-SERVICE TRANSACTION NUMBERS BY 50% AND OUR DEAL SIZE BY 30%."

XaaS Director - Global IT manufacturer.

4. OPERATIONS

The As-A-Service Operations department takes care of a wide range of tasks, including handling customer requests, coordinating legal documents, managing assets, handling funding, billing and collections, as well as dealing with asset disposals. These back-office operations play a crucial role in delivering a seamless and efficient As-A-Service experience to customers.

Some of these tasks are specific to As-A-Service programmes and not done in traditional transactional models. Defining these new processes and workflows will set the grounds for an organized Back Office structure, key to creating a scalable As-A-Service solution.

The focus is of course on the customer experience, but don't forget the impact of the As-A-Service model on the experience of your sales force. Selling services means additional requirements from the Operations department, so it's crucial that processes are adapted and designed to improve the experience of the sales force.

'OUR AS-A-SERVICE OPERATIONS TEAM HAS BECOME FULLY INTEGRATED IN OUR SUSTAINABILITY & CIRCULARITY DEPARTMENT. WHEN ASSETS REACH THEIR END-OF-LIFE OR ARE NO LONGER NEEDED, OUR OPERATIONS DEPARTMENT ENSURES THEIR PROPER DISPOSAL OR RECYCLING. THIS INCLUDES ADHERING TO ENVIRONMENTAL REGULATIONS AND MINIMIZING WASTE."

Head of Europe - Japanese multinational electronics company.

5. CIRCULAR ECONOMY AND SUSTAINABLE DEVELOPMENT

The concept of the circular economy is all about doing more, creating more value while using less resources. When moving to As-A-Service, you remain the owner of the assets and can offer access to them in combination with customized value adding services. As the perpetual owner you can make money from the products as long as they can fulfill your customers' needs, then the parts can be used as spare parts and ultimately the materials can be sold for recycling. By controlling the entire lifecycle of the equipment, you can secure that they are managed responsibly, and this is of increasing importance to many customers relating to their efforts to support a more sustainable development and their ESG reporting.   All this goes way beyond the only 'end-of-life' services since a As-A-Service model allows for a system wide sustainability approach. This includes the opportunities to

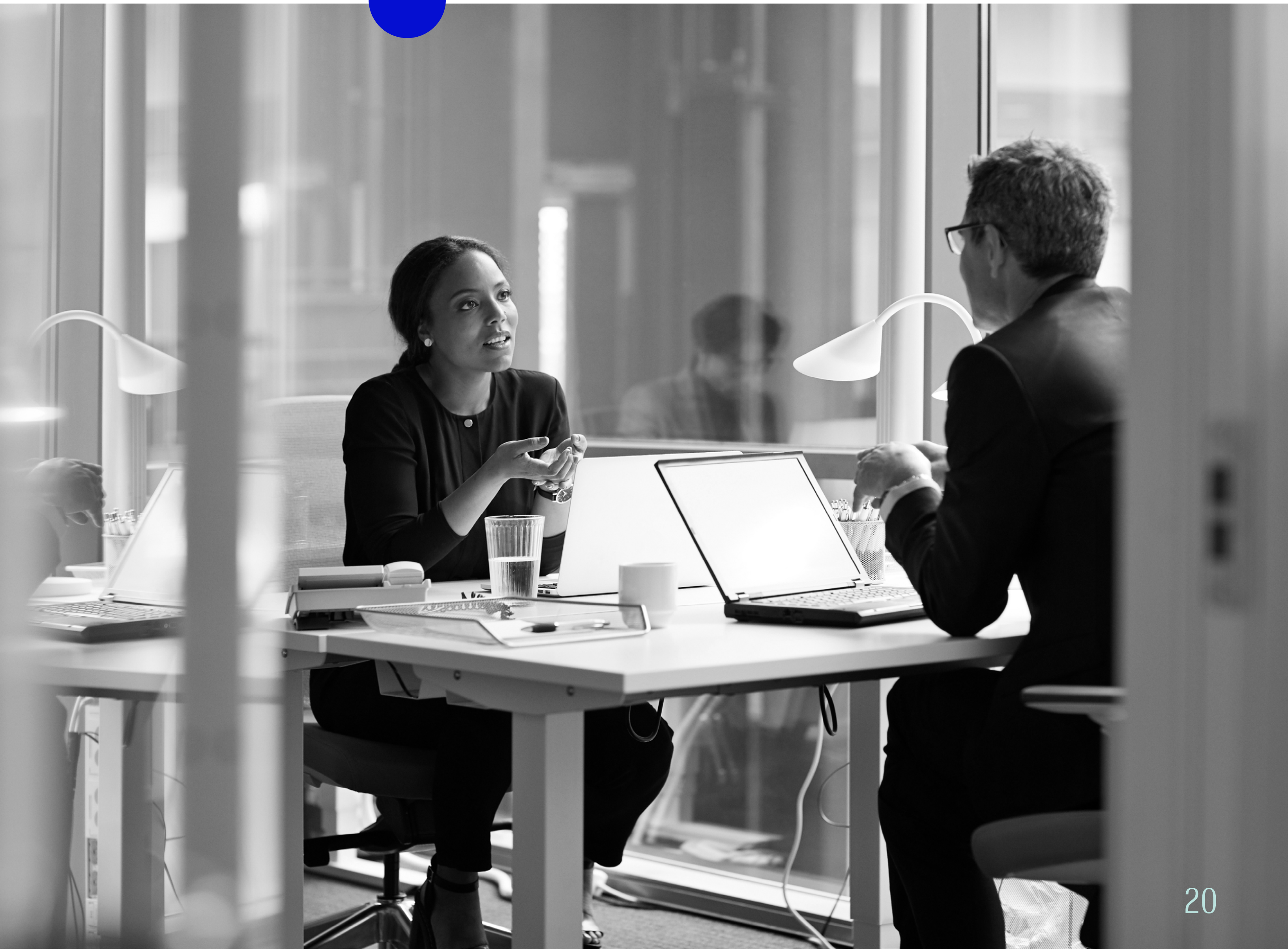
- Rethink all stages of the product life cycle in a resource efficient more sustainable way.
- Use of more sustainable supplies: using renewable energy, bio-based or potentially completely recyclable materials.
- Product life extension: extending the life cycle through repair, maintenance, upgrading, re-manufacturing and if necessary resale.
- Recovery and recycling: recovering usable resources or energy from waste or by-products.

By illustrating the circular essence of your Product-As-A-Service solution and establishing well-defined key performance indicators (KPIs) in alignment with it, you possess the potential to solicit green bonds. Undoubtedly, green bonds hold significant allure for investors as they provide a means to attain transparency regarding their investment portfolio, enabling them to discern the environmental, social, and governance (ESG) impact of their funds. Furthermore, green bonds present an effective avenue for diminishing the carbon footprint associated with a portfolio.

By considering all these factors from the start, businesses can design service offerings that are more sustainable and easier to manage over time.

"WHEN CREATING OUR OWN AS-A-SERVICE SOLUTION, WE PLANNED FOR THE END-OF-LIFE SCENARIOS BY BUILDING IN PROGRAMMES FOR DATA WIPING, REFURBISHING, AND RECYCLING.. BY DOING SO, WE ENSURED THAT THE VALUABLE MATERIALS AND COMPONENTS USED IN OUR PRODUCTS ARE NOT LOST, BUT RATHER, ARE KEPT IN CIRCULATION AND GENERATING CUSTOMER BENEFITS FOR AS LONG AS POSSIBLE."

CEO - European Commercial Refrigeration Division - Multinational heating, ventilation, and air conditioning corporation



6. FOCUS - THE '3-10-50' FUNDING MODEL

Funding is a critical enabler of Product-As-A-Service, allowing for a scalable business model.

As your As-a-Service business takes off, it's important to keep up with the changing times and adapt your funding strategy accordingly. That's where our '3-10-50 funding' model comes in - it's the ultimate guide to navigating the funding journey for As-a-Service. This model is designed to help you find the perfect solution as you move up the ladder and generate more As-A-Service revenue each year. So whether you're just starting out or you're a seasoned pro, our '3-10-50' model will help you stay ahead of the game and keep your business thriving.

Depending on the As-A-Service yearly business volume generated (here we take into account the yearly net production funded (i.e. the Annual Recurring Revenue of your contracts: value of recurring revenues from the subscription contracts signed for a calendar year), there are 4 main funding milestones:

0 - 3M€ = START WITH YOUR OWN FUNDS

This means that your organization uses its own funds to finance the assets used by your customers. This is a first step to test the market, allocating a maximum envelope and starting building a portfolio and co-build the product with your core customers. The objective is to establish a suitable envelope that accommodates both your acceptance of cash investments and the risk of customer insolvency. This is doable at first, however as your As-A-Service business grows it will limit you as you can't have your balance-sheet full of your customers assets on a mid to long term basis. If you want to address a wider end-customer base, diversify your funding sources and reduce the risks of exposure, you will need to find external sources of funding. This "ownbooked" portfolio may serve as a solid foundation for initiating discussions with potential external funding partners, and may be offered for sale to such partners initially.

3M€ - 10M€ = SINGLE FUNDER STRATEGY

Now that your model has reached some level of materiality and you start being comfortable with the associated unit economics, the next logical step is to scale your funding model. By selecting an asset financing pathway and securing an external funding resource, you can effectively unburden your balance sheet and enhance your working capital. This is a crucial step towards expanding your business model without compromising your company's metrics and financial ratios. This step involves selecting the right funding partner and establishing partnership with them.

Asset financing, a long-standing practice employed by Equipment & Vendor Financing entities (referred to as Funders), particularly in the realm of IT assets, can be replicated for various equipment types and tailored to suit the unique requirements of the As-A-Service business model.

The most commonly seen funding schemes proposed by the equipment funding industry are the Sales & Lease back, the Operating lease, the assignment of Receivables, the sub contracting.
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The primary focus of funding lies in evaluating the precise requirements of a vendor/customer, while concurrently comprehending the various forms of funding that are accessible. It is imperative to direct efforts towards identifying the most appropriate funder and establishing a durable relationship that is founded not only on the legal obligations of both parties but also on trust. A shared comprehension of expectations at every phase of the funding procedure is of utmost importance for the effective execution of a scaled As-A-Service proposition.

A funder mapping analysis should be conducted to select the most relevant funder. Some points to consider for your selection include approval process performance, geography, contract type available, pricing, legal support etc.

When you have identified the most appropriate funder, a funding communication pack should be carefully prepared. The objective of such a pack is to provide reassurance to the funder and to demonstrate that the potential performance risk of working with you is minimal and that large As-A-Service business volumes are likely to happen.

Then, you will need to sign a Vendor Programme / Cooperation Agreement with your selected funder. A thorough analysis and review of their clauses by experts is recommended at this stage as these agreements will govern the relationship in the long term.

10M€ - 50M€ = MULTI-FUNDER STRATEGY

When the total value of current deals becomes significant, it becomes necessary to diversify funding sources to avoid relying on a single entity. This diversification provides more flexibility in allocating deals and reduces interdependent relationships.

A multi-funder approach allows a company to implement an asset financing program that offers a wider range of coverage across different types of funding and financial institutions. This approach prevents companies from being solely dependent on the risk tolerance of a single financial institution or their large corporate customers.

However, it is not advisable to onboard numerous partners with insufficient business volume. If the available resources are limited, it becomes impossible to satisfy all partners or none of them when distributing the resources.

50M€+ = OWN CAPTIVE

Creating a captive is the ultimate step in your As-A-Service funding strategy. It consists in creating your own financing entity and acting as a complete one-stop shop for your customers. When opting for such a strategy, here are some points to define:

- The type of Captive Finance scheme according to your strategy.
- The strategy of the Captive in terms of Circularity compliance.
- The geographical coverage.
- The margin sharing between the organization and the Captive.
- The Business Plan for the Captive Investors with profitability scenarios.
- The strategy on portfolio refinancing, with the investors' funds at first and adding external portfolio funding.

7. FOCUS - PAYMENT

Compared to traditional business, with their one-off transactions, As-A-Service recurring subscriptions generate both : more volume per customer given the higher frequency of invoicing and more complex invoices per customer given associated rules such as consumption/usage rating or proration when a subscription changes.

This makes the whole process a lot trickier for two reasons: first, invoicing and payments are a source of overhead costs if not properly automated, and second, if you don't do it right, customers will be dissatisfied.

Because of lower price points, digital consumer subscription businesses had to tackle recurring invoicing and payment automation a long time ago (or at least the successful ones did!). Without doing so, there is no way to scale a business, as most, if not all, margins would be eaten by back-office processes. As a result, highest-converting consumer subscription offerings have seamless digital invoicing and payment processes that let their customers select their favorite recurring payment methods against which to collect automatically.

By comparison, it is not uncommon in the B2B space for the cost of invoicing to clock in at around $10 per invoice (and as a matter of fact, very often a multiple of that!). Such numbers can be tolerable for "classic" one-off invoices of amounts large enough to make $10/invoice a negligible cost, but as the volume of invoices and payments per customer grows in a recurring subscription business, this cost would be a real problem. Beyond undesired overhead costs, non-automated processes are also often linked to later payment, weaker collection, and, consequently, higher write-offs and as a matter of fact even lower customer conversion rate!

Even though there is a popular belief that digital invoicing and digital payments methods aren't really mainstream in B2B, the Subscribed Institute's data show the exact opposite. In fact, almost 90% of high-growth B2B companies are leveraging digital invoicing and very close to 50% are doing recurring digital payments, versus respectively less than 80% and less than 22% for low-growth companies. Here are a selection of key reasons proving the point:

- Glitches in invoicing and payment processes often represent 20% to 40% of all involuntary churn, which can silently, but surely, kill a subscription business.

- Invoicing and payment errors directly translate into revenue leakage, that can average around 3% of total revenue.

- Inspired by consumer-like practices, high-growth subscription B2B companies tend to leverage practices that make renewal a non-event as much as possible. For example, 56% of customer contracts are on automatic renewal, which certainly impacts churn positively with a significant 13-point positive difference versus lower-growth subscription businesses.

More important: beyond operations, catering to customer payment preference is crucial, making payments an integral part of the subscriber experience. This means your As-a-Service shift needs to treat this dimension as an important FACTOR, and not simply as a back-office "necessary evil task". Again, research from Zuora's Subscribed Institute shows that choice of payment methods and currencies have direct correlations with business growth:

- Businesses that accept more payment methods grow their revenue 4 points faster through both better acquisition and retention

- Businesses that accept more payment methods have 4 to 5 point more effective invoice payment rate (i.e. defined as the percentage of total invoices being paid 90 days after due date)

- Business that accept more currencies grow their revenue 8 points faster

- There are significant differences in terms of preferred recurring payment methods preferences depending on geographies, industries, services offered, invoice amount bands, etc. For instance, card payments are a lot more frequent in the US as compared to Germany.

Finally, we can’t talk about recurring payments without addressing the issue of fraud. Frauds of course can happen, as in any other payment models, but can easily be mitigated with the right strategy. In the As-A-Service industry it can take several forms, such as:

- Document falsification
- Fictitious asset
- Overestimation of equipment worth
- Double Financing of the same piece of equipment
- Fraudulent financial statements
- Kickbacks
- Theft of one’s identity

Fraudulent activities often occur due to inadequate verification procedures of the applicant company. Nevertheless, the implementation of detection technology can effectively reduce the incidence of fraud. Furthermore, equipment finance entities can serve as a reliable mitigation strategy against fraudulent activities, given their professional approach to customer screening.

All these reasons combined make it clear as to why best-in-class As-A-Service businesses digitize early on their invoicing and payment to be able to scale properly even, both in B2C and B2B. A strong capability in these fields is thus required to support your As-A-Service offering. Customers want end-to-end solutions for simplicity purposes. Therefore, teaming up with best-in-class partners will ensure your customers access to the best platforms, software and services for a superior user experience.

8. FOCUS - FINANCE & ACCOUNTING

As-A-Service models will have a strong impact on your financial statements, KPIs and accounting procedures driving tremendous changes in the Office of the CFO. When deploying As-A-Service programmes, here are some of the top financing and accounting considerations to discuss:

FINANCIAL COMMUNICATION

The revenue recognition rule associated with the new revenue streams can be quite different compared to business-as-usual. This is especially true for revenues coming from core services priced using brand new models and even more so for services beyond traditional financial services, including subscription bundles that, from an accounting perspective, are complex.

Depending on the specification of your offer and the way you fund it (which risks you keep or externalize), you may have to apply IFRS 9 (Financial instruments), or IFRS 16 (Lease accounting).

There is even a strong chance that the revenues may actually fall into accounting standards such as IFRS 15/ ASC 606 (similarly to commissions, advisory contracts, bundled products, credit cards and loyalty schemes, but with potentially different rules). This could mean substantial challenges from both a process and a workload perspective for a company's finance team.

KPIS DEFINITION AND IMPLEMENTATION:

As-A-Service has revolutionized the financial game, and the KPIs are no exception! Gone are the days of dwelling on past events and budgeting. Instead, the focus is on creating a brand new business model that prioritizes predictability.

COMMON KPIS USED IN THE AS-A-SERVICE BUSINESS MODEL (SOURCE ZUORA):

1. **Annual Recurring Revenue (ARR):**
   ARR is the amount of revenue a company expects to repeat in a year, which provides a holistic view of a company's health. With ARR as the foundational metric, companies can forecast revenue, set realistic goals, and make informed decisions to maximize growth.

2. **Churn Rate (Attrition Rate):**
   Churn rate is the rate at which a business loses subscribers, and something that becomes critical as you grow your subscriber base. It is 5x more expensive to acquire a new customer than to maintain an existing one. As one digital innovation exec at an IoT company notes: "customer retention, at a very eye-level, is paramount. If you spend money to acquire customers but you lose them as fast as you acquire them because you don't provide the right experience, then its an economic business model that will not scale at all."

3. **Customer Lifetime Value (CLV):**
   CLV may be a novel concept for many manufacturers. It's the expected net present value of profit across the entire customer lifecycle, taking into account the cost to acquire, serve and maintain. It is a critical indicator to model across different dimensions and cohorts in order to assess for example : go-to-market resources allocation, acquisition and retention strategies etc.

4. **Net Revenue Retention (NRR):**
   NRR calculates total revenue (including expansion revenue) minus revenue churn (contract expirations, cancellations, or downgrades). NRR measures your ability to retain and expand customers. It can be seen in short as your customer base organic growth.

FINANCIAL PROCEDURES DESIGN:

Setting up an As-A-Service is going to introduce a whole new set of financial and operational dynamics that require some adjustments in various financial procedures. The shift from a traditional one-time purchase model to an As-A-Service model is a game-changer that impacts revenue recognition, customer management, billing cycles, and more. So, let's dive into some of the key changes and important things to consider when it comes to the financial procedures when adopting an As-A-Service model:

- Revenue recognition
- Billing management
- Expense management
- Financial forecasting
- Pricing strategy
- Compliance and reporting

SHAREHOLDER'S VALUE INCREASE

The notion of shareholder value encompasses the financial benefits, such as capital gain and dividends, that shareholders derive from their investment in a company. In the context of As-A-Service business model, we are confronted with a recurring revenue stream that has the potential to impact shareholder value in multiple ways. It is important to acknowledge, however, that the actual effect will be contingent upon the successful implementation and management of the model. Presented below are several ways in which the As-A-Service model can potentially augment shareholder value:

- Predictable Revenue Stream
- Customer Lifetime Value enhancement
- Scalability
- Customer relationship improvement
- Market valuation is higher thanks to the recurring revenue model (predictability and stability boosting market valuation)
- Competitive edge

All the above considerations will have a tremendous impact on the type of As-A-Service solutions you will create, so they should be treated with high importance. Additionally, both the specific implementation and the manner in which these financial concepts are utilized will be influenced by the company's ownership structure, whether it's private-equity owned, publicly traded, or venture-backed.

9. THE POWER OF SMALL CHANGES

In any organization, it's crucial to have a forward-thinking approach when it comes to restructuring departments. While it's understandable that not all departments can undergo simultaneous transformation, it's imperative to keep the big long-term picture in sight when building As-A-Service models. The key lies in having a well-defined roadmap that ensures the scalability of the model.

However, being pragmatic is equally important. While it's essential to be ambitious and futuristic, blindly implementing sweeping changes all at once can lead to chaos and resistance within the organization. Instead, the implementation of changes should be approached in an incremental manner. By breaking down the As-A-Service transformation into manageable phases, departments can adapt steadily, ensuring smooth transitions and position themselves for sustainable As-A-Service success in the long run.

"DURING THE DEVELOPMENT OF OUR AS-A-SERVICE SOLUTION, WE RECOGNIZED THE SIGNIFICANCE OF TESTING AND LEARNING. BY IMPLEMENTING AS-A-SERVICE BEST PRACTICES AND REAL-LIFE METHODOLOGY OF EXPERTS LIKE BLACK WINCH, WE SUCCESSFULLY EXPEDITED THE MARKET LAUNCH OF OUR SOLUTION. REMARKABLY, WITHIN A MERE 6-MONTH PERIOD, OUR AS-A-SERVICE SOLUTION GENERATED AN IMPRESSIVE REVENUE OF 5 MILLION EUROS."

XaaS Director - Global IT manufacturer

Get Started Today

Ready to take on the challenge of implementing As-A-Service models? Use this roadmap to overcome bottlenecks and rally others to your cause.

Psychology teaches us that when faced with stressful situations, we can either 'Fight', 'Flight', or 'Freeze'. Implementing As-A-Service is a major shift that challenges the status quo, which can cause teams to resist, avoid, or become overwhelmed. That's why so many attempts fail to take off.

But with this guide, you'll be fully equipped to avoid these counterproductive reactions and help your team 'Flourish' by navigating change with confidence, eagerness, and ease.

Get started today!

Contact Black Winch blackwinch.eu or Zuora zuora.com for more information.

Subscribed Institute

Subscribed Institute

Zuora's Subscribed Institute is a dedicated think tank focused on the Subscription Economy. The Institute supports its 1500+ business executives across 600+ global companies with critical data, thought leadership, and connections. Research provided by the Institute helps business leaders and their organizations to maximize the opportunities of the Subscription Economy.

More at www.zuora.com/about/subscribed-institute/

BLACK WINCH

Black Winch

Black Winch is the world's exclusive authority in Product-As-A-Service solutions. They engage, inspire and empower intrapreneurs to achieve their Product-As-A-Service ambitions by building and scaling their in-house recurring revenue models.

More at www.blackwinch.eu

Looking To Explore Some Topics Further?

Did the content of this whitepaper leave you wanting more? Are you eager to explore the topics discussed in greater detail We've compiled a list of additional resources that will take you on a deep dive into these fascinating subjects. Check out the links below and expand your knowledge today.

- Philips Enterprise Monitoring as a Service (EMaaS): link and more info here on its use case at Jackson Memorial Hospital.
- The most commonly seen funding schemes in the equipment funding industry (e.g. Sales & Lease back, the Operating lease, the assignment of Receivables, the sub contracting): link
- Research from Zuora's Subscribed Institute showing that choice of payment methods and currencies have direct correlations with business growth: link
- Common KPIs used in the As-A-Service business model: link
- Article on Net Revenue Retention NRR: link

Next White Papers In The Making

Exciting news! We're thrilled to announce that our next whitepaper series is currently in the works. Our dedicated teams at Black Winch and Zuora are hard at work, preparing a collection of insightful resources just for you. Get ready to dive deep into the world of Product-As-A-Service and gain expert knowledge that will make you a pro in no time. Stay tuned and get ready to unlock a whole new level of understanding on:

- 'Overcoming Fraud Bottlenecks in the As-A-Service Economy'
- 'Product-As-A-Service: How To Create Your Own Captive'