White Paper

Examining SAP's Cloud Strategy
FUNCTIONAL SUPPORT SERVICES

Rimini Street
Engineered for Support

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Introduction

There are several important areas of inquiry to cover with respect to SAP and the cloud. These include SAP's cloud acquisitions and hosting of non-SAP cloud acquisitions, as well as SAP's actual sales and experience in the cloud versus on-premises. In this paper, we will explore these themes and others in order to provide a 360-degree perspective on the current state of SAP's cloud.

A great deal of information has been released by SAP on the topic of cloud solutions. SAP, a longtime on-premises application and database provider, has made a number of cloud acquisitions, including well-known vendors SuccessFactors, Ariba, and Concur. In this paper, we examine SAP's actual cloud strategy versus SAP's cloud reality.

There are several important areas of inquiry to cover with respect to SAP and the cloud. These include SAP's cloud acquisitions, and hosting of non-SAP cloud acquisitions, as well as SAP's actual sales and experience in the cloud versus on-premisess. In this paper, we will explore these themes and others in order to provide a 360-degree perspective on the current state of SAP's cloud.

This perspective is largely absent from the available advice in the SAP market. This is because SAP partners (where, along with SAP, SAP customers obtain most their information on SAP) are not allowed to diverge from the storyline that is developed by SAP marketing. Yet, by understanding the reality of SAP's cloud strategy and offerings, we believe our clients can make much better decisions.

Accordingly, at Rimini Street, the Strategic Roadmap Services team assists clients in understanding SAP's cloud strategy and in examining how this fits with their own enterprise resource planning (ERP) roadmaps. Rimini Street encourages clients and prospects alike to research all hybrid cloud applications to make sure they are filling specific ERP product gaps, either those not available from SAP or available less expensively from a secondary vendor.

Why the Focus on Cloud?

Cloud-washing is a term that is used when the vendor presents its applications and sales as more cloud-based than they actually are. This presentation of a cloud face is directed to multiple audiences and includes customers, IT analysts, and the Wall Street investment community.

SAP has historically been a software vendor (more so than it actually is today). Many of SAP's software solutions don't actually meet the full definition of SaaS because they are not multitenant. (This topic is covered in detail in the Rimini Street paper, "SaaS Pricing and Contract Terms.") SAP, like most ERP software and database vendors, currently sells a small percentage of cloud-based products, although that is changing over time. Oftentimes, these SaaS products are relatively new and not fully developed for the marketplace, as the early versions of their on-premises software products were. For example, both IBM and Oracle have non-cloud and cloud-based products, but unlike on-premises product offerings, a smaller percentage of their revenues are the result of their respective cloud-based product offerings.

Both IBM and Oracle have been repeatedly called out in the media for cloud-washing. (Sources: *Cloud-washed its earnings results, it's likely not alone, August 23, 2013; David Linthicum, SEC investigates IBM for possible cloud washing, last published August 2013; David Linthicum, Cloud washing goes beyond the Oracle lawsuit, June 7, 2016*) Cloud-washing is a term that is used when the vendor presents its applications and sales as more cloud-based than they actually are. This presentation of a cloud face is directed to multiple audiences and includes customers, IT analysts, and the Wall Street investment community. Oracle, for instance, has internally promoted the sale of its cloud offerings by incentivizing account executives with higher sales commissions on its cloud offerings versus on-premises software. That has resulted in gaming the numbers where cloud and non-cloud offerings are bundled as part of the sale. The sale of the cloud offering is recorded and reported to Wall Street and others, but customers will, in many cases, only go live with the on-premises edition of what they purchased. Meaning the cloud portion of the sale lies dormant and becomes shelfware, or in this case, shelved-cloudware, for the foreseeable future.

There has been a gradual, but noticeable trend in the revenue and pricing strategies of the software industry — especially for ERP software vendors. Their ideal goal is to convert as many of their on-premises software customers into subscription cloud-based software customers as possible. This conversion is strongly driven by expectations created by Wall Street. To their consternation, it's been somewhat slow going, because there is a general reluctance for many ERP customers to make the leap and immediately move to the cloud. At this point in time, the great successes in the public cloud (SaaS) have been limited to non-customizable applications such as Salesforce (Customer Experience or CX), SuccessFactors (HR), Arena Solutions (bill of materials management), and Concur (travel and expense management).

The predominant, underlying motivation for promoting cloud-based products is higher overall expected profits from the continual stream of subscription revenue. This can be viewed as pressure from the investor community and Wall Street analysts, because these groups place a higher value on cloud-based revenues due

to the perceived predictability and regularity of this type of income. While that may indeed be the current trend, the current reality is software vendors who have traditionally and predominantly sold on-premises software applications and database solutions are still more profitable than those who sell only cloud-based software.

For example:

– Salesforce and Workday are two of the largest SaaS vendors. Yet, while they are growing rapidly, neither is currently profitable (on a yearly basis). (Sources: *Steven Brooks, Did Workday hit a profit at last?, June 1, 2016*; *Trefis Team, Salesforce 2016Q4 Earnings: Revenue Growth Sustainable; But Profitability Nowhere in Sight, February 16, 2016*)

– Among the largest software vendors in the world are Microsoft, Oracle, and SAP. They are all profitable to varying degrees. IBM would likely rank higher if its software sales were reported as a separate company. Despite what Wall Street would have people believe, the largest segment of revenues from these top software vendors over the last few years continues to be made up of on-premises software sales and not cloud-based software sales. (Source: *Synergy Energy Group: Reno NV, August, 2016*)

The profit motive for being recognized as a cloud-based versus on-premises software vendor can be extrapolated to include other SaaS and on-premises software vendors from the following quote (with commentary provided in brackets):

> *"…[O]f the 26 index members to go public most recently, 21 are losing money on a GAAP (generally accepted accounting principles) basis…. Those unprofitable companies were a combined $388.7 million in the red in the last quarter…. [Such loss is largely ignored though, because] right now some 28 publicly traded cloud computing companies are worth at least $1 billion…. Beyond the financials, investors are betting on a massive paradigm shift in technology. Old packaged and desktop software is being tossed aside as businesses shift to simpler services that run in browsers and on mobile phones…."*
>
> Ari Levy, "Wall Street's ongoing struggle to make sense of the cloud," February 12, 2015

It is therefore, a combination of pressure from Wall Street and the perception of the future of the software industry that drives each company's business strategies. Companies, regardless of industry, must adapt over time in order to stay relevant — remember Kodak? Software vendors, by the nature of technology advancements, are forced to constantly re-evaluate and update their revenue strategies. Unfortunately for customers, some software vendors have blurred the lines, making it difficult to distinguish what is real and what has yet to materialize. The spinning of cloud messaging by CEOs can't change the facts. Many are no closer to being major cloud ERP vendors than they ever were. (Source: Steven J. Vaughan-Nichols, Oracle is not a cloud power, October 3, 2016)

Cloud-Washing

Cloud-washing is the purposeful and sometimes deceptive attempt by a vendor to rebrand an old product or service by associating the buzzword "cloud" with it. (Source: Margaret Rouse, WhatIs.com) As mentioned above, the industry term for representing one's revenues as more cloud-based than they actually are is called cloud-washing. SAP presents itself as a cloud-based software vendor to Wall Street, but then eagerly still sells on-premises software. (Source: *Vinnie Mirchandani, SAP Nation 2.0: an empire in disarray, page 110 of 146 Pages, last visited February 9, 2017. See SAP Nation 2.0 Page 110: Clearly, SAP is eager to report larger cloud revenues to Wall Street, so taking advantage of that eagerness may work for some customers. Customers report, however, that even in competitive deals, SAP cloud pricing is aspirational. It reflects a premium that has long since disappeared in the enterprise software market. Or SAP talks from both sides of the mouth, alternately defending their on-premises software and then claiming to be a cloud company.)* While SAP continues to position itself as being very cloud-focused, in reality it wants to maximize revenues by being both a cloud-based and an on-premises software vendor.

This is, in fact, a larger trend. Publicly traded software vendors continue to generate revenue and also strive to meet Wall Street's expectations, although they will typically sell their software in any form demanded by customers. In doing so, they sometimes blur the distinction and overstate cloud-based growth.

The transition to cloud-based product offerings for these software vendors will continue for the foreseeable future. ERP customers inevitably risk being forced to move to cloud-based products. Such migration is constrained by the shortcomings of the cloud-based product functionality when compared to mature and more robust on-premises ERP products.

However, customers now need to confront a shifting landscape: What was once a forced march by ERP vendors to maintain and upgrade legacy systems is now a focused march to reimplement product offerings in the cloud, often with less functionality and at a much higher total cost of ownership.

Many customers have realized that this is a very unpleasant double sting of "transitioning to less functionality at a higher overall license and support cost over the long term," and they are clearly not very receptive to this idea. (Source: Dean Petracca, PricewaterhouseCoopers, January 2007) Hence, there continues to be a slow cloud adoption rate, as with the SAP S4/HANA application and the HANA database, in general.

SAP HANA and the Cloud

The design of SAP HANA incorporates two database characteristics in one:

– **Analytics database design:** HANA is an analytics-optimized database. The column-oriented database design that SAP leverages with HANA was very sparingly used until several years ago. SAP picked up the design, and has since been promoting the advantages of column-oriented database design.

– **In-memory computing:** The second part of HANA is to load the entire database into memory. This memory is a combination of both memory types — read-access memory (RAM) and solid-state disk (SSD) or hard-disk drive (HDD) memory.

SSD memory is replacing HDD memory storage at an increasing rate. (Source: *Lucas Mearian, Flash memory's density surpasses hard drives for first time, February 6, 2016*) This is the case for SAP and non-SAP installations, and has been gaining momentum for several years. As for the column-oriented database design, it continues to be exclusively used for analytical applications. However, neither feature of HANA has anything to do with the cloud. Column-oriented databases, SSD and RAM can all be implemented in the cloud or on premises. If you would like more detail on HANA and in-memory computing, please read the Rimini Street article on HANA versus Oracle 12c, "Considering SAP HANA Versus Oracle 12c." SAP has proposed a single database design with HANA that is equally applicable to all applications and uses. SAP wants customers to adopt the same database for both cloud-based and on-premises applications.

One interesting observation is that HANA is frequently sold in the cloud. SAP appears to convey the idea that HANA and the cloud are somehow interconnected. SAP has, in our view, pushed to commingle the concepts of HANA with the cloud over the last few years.[1] Part of this has come from the way in which HANA and S4 have been introduced as having such strong cloud options. Another example of this psychological commingling is SAP's introduction of the HANA Cloud Platform (HCP). The HCP is a front end, which allows companies to connect to databases and applications. In reality, we have observed the HCP, and though it includes hosting, it also provides hosted components within HANA on-premises environments. SAP's HCP allows SAP to declare implementations of HANA on premises are also connected to components hosted in the cloud. (Source: SAP Store)

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[1] This connection between HANA and the cloud is demonstrated through conversations with non-technical people who work in SAP's IT department. From our and our client's experience, when discussing HANA, they will sometimes bring up the concept that SAP is moving rapidly toward the cloud because HANA, a database, is somehow related to the cloud. Interestingly no one else makes the same claim about HANA's main competitive product, Oracle 12c. The Oracle 12c database can be delivered in the cloud or on premises. In fact, due to recent improvements in Oracle 12c that increased its ability to host multiple tenants, one might say it is more cloud-ready than HANA. Yet it is not psychologically connected to the cloud the way that HANA is. We surmise this connection of HANA to the cloud is only due to SAP's marketing literature.

In our experience, SAP's partners have repeated the same messaging: that HANA is a cloud-based product. In fact, it is common to present HANA in this framework. (Source: Mariadb.com, Webinar: MariaDB MaxScale – Scalability at its Best – 15. January 2015). SAP has placed enormous marketing resources behind the rollout of HANA, and it wants to communicate and demonstrate how much it is focused on the cloud. The reality, however, is that this messaging masks the whole truth. The following quotation provides a sampling of this messaging by transitioning from promoting HANA to directly discussing the cloud. (Source: SAP Store)

> *"In a keynote speech, SAP chief executive Bill McDermott said he wants businesses to be 'data driven and seamless' by using SAP's HANA platform and the software that sits on top of it by enabling manual processes to become digital. 'We believe it's a HANA world now and all data has to be put on one data platform and companies should be seamless,' said McDermott.*
>
> *In practice this involves SAP adopting a 'cloud first' approach, whereby new products are developed to be used in cloud environments then adopted for use on internal IT systems, rather than the other way round. One example of this is SAP's Business Suite 4 for HANA (S/4HANA), built for deployment on private clouds, and now expanded to public clouds through the launch of S/4HANA Cloud Edition."*
>
> – V3
>
> Source: Roland Moore-Colyer, SAP boss wants firms to be 'data driven and seamless' with HANA, May 6, 2015

According to SAP's messaging, HANA is cloud-based because the S4 application is designed to also reside in the cloud. SAP simply associates its S4 application and HANA database with the cloud in order to give the impression that HANA is exclusively a cloud database. Even though the HANA database can be used either in the cloud or on premises, it has not stopped SAP from marketing S4 and HANA as cloud-based products.

SAP and Amazon Web Services

Since the introduction of Amazon Web Services (AWS), the focus of cloud design places a strong emphasis on scalability and flexibility. Traditionally, most databases were designed to be sized and installed on a single piece of hardware. Amazon, who thinks big, made scalability of the MariaDB a primary design attribute because it wanted a database with specific cloud characteristics. (Source: *Mariadb.com, Webinar: MariaDB MaxScale – Scalability at its Best – 15. January 2015*) It's surmised this is how Amazon became the leading enterprise-hosting IaaS company in the world. SAP is not an IaaS provider, so it has become apparent that SAP will be predominantly using other infrastructure as a service (IaaS) providers such as AWS to host its applications, rather than offering to provide the hosting itself.

Currently, SAP sells its enterprise applications primarily for on-premises use. It also hosts applications such as SuccessFactors (i.e., acquired applications) in a proprietary SAP cloud. SuccessFactors was not designed to run on HANA originally (rather, it was designed for an Oracle Database). (Source: *Dick Hirsch, Oracle's attack on SAP's Cloud and what it tells about SAP's Cloud strategy, October 3, 2014*) This is an important distinction, and it relates to how SAP has designed HANA. Rather than designing an application specifically for the cloud, SAP appears to have mandated that all its new applications will be built using the HANA database concept. Accordingly, SAP designed such applications first as "HANA-based applications," not as cloud-based applications.

Commingling Cloud and Non-Cloud Products

Cloud-washing may also be performed by cleverly including the word "cloud" in an application name. The reader can judge if this is the case with the HANA Cloud Platform (HCP) naming convention. (Source: *Brightwork Research & Analysis, Is the SAP HANA Cloud Platform Designed for Cloud Washing?*) SAP has in the past two years, increasingly placed a great deal of marketing emphasis on the term HCP, because that allows it to further commingle this naming approach with the HANA database. The following quotation is an example of this:

> "One of SAP's key moves championed at Sapphire Now is the closer integration of its [S/4] and HANA Cloud Platform, aimed at enabling firms to shift from systems running old SAP software on legacy hardware, to cloud services supported by HANA."
> – V3

Source: Roland Moore-Colyer, SAP's 'Run Simple' cloud strategy is on a path of evolution not revolution, May 8, 2015

The HCP may be considered a suite of products with many under development. Some people incorrectly state that HANA is a both a database development environment and an application. HANA is exclusively a database. HCP is an infrastructure-as-a-service (Iaas)/platform as-a-service (PaaS) front-end. S4, on the other hand, is an application as is identified in the HCP Cockpit "screen capture" below. (Source: *Saphanatutorial.com*)
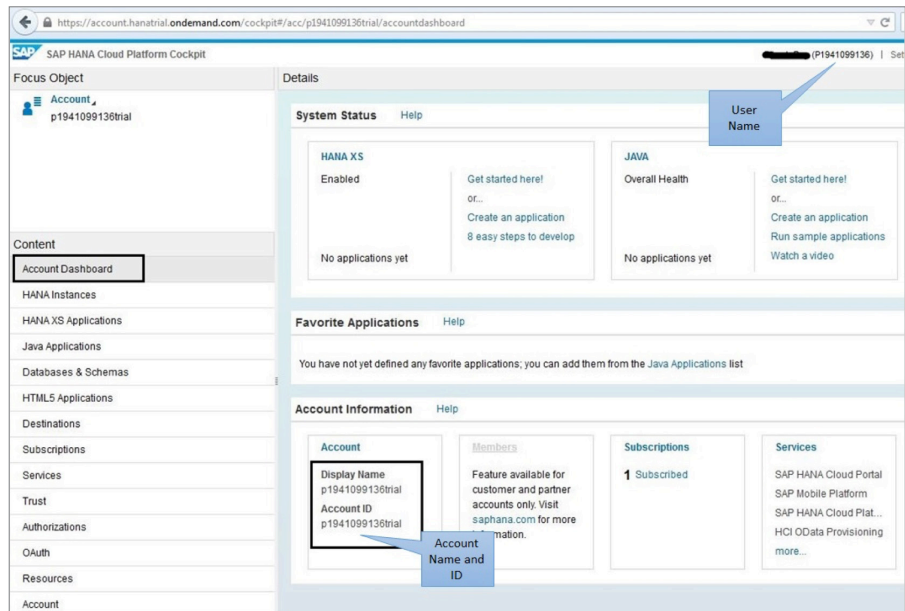

Figure 1. A View of the HCP Cockpit

Like other IaaS/PaaS environments, the HCP allows a user to connect to databases that may either be remote or on premises. The HCP can also connect to applications. Other IaaS/PaaS environments are also available that allow one to connect to both databases and applications. AWS provides one such example. So, SAP is not unique with its design.

In our view, after three-plus years of development, the HCP is still "new and improving." HCP does not provide a one-for-one replacement of existing SAP ERP ECC application products or functionality. However, this has not deterred SAP from making HCP a central theme in its marketing initiatives. The HCP is able to connect to HANA or any other database, for that matter. However, this platform is not the same thing as a database.

Will SAP Provide Hosting?

Earlier, we explained that while SAP proposes hosting its applications for customers, our research has shown that this is not a core strength for the company, and it has placed little emphasis on it in the past. SAP has certainly made a lot of noise about how companies could host with SAP and presents itself as if it is building out hosting capacity and is ready to host all the solutions for its customers. However, it is becoming increasingly apparent that SAP is not in a position to fully take on this endeavor. This is in part explained in the following quotation from Vinnie Mirchandani's book titled *SAP Nation 2.0: an Empire in Disarray*:

> *"There is another concern about SAP's S/4 public cloud. The data center, in Sankt Leon-Rot, Germany, while close to SAP's impressive Waldorf headquarters, does not itself inspire much confidence. It has been called 'puny and primitive' compared to the data centers of infrastructure as service providers like Amazon, Microsoft Azure, and Rackspace. Indeed, competitors like Info and Unit4 are using infrastructure as a service (using data centers from Amazon and Microsoft respectively) rather than try to compete with their scale. Oracle has invested in their own formidable string of global data centers to be competitive with Amazon and other cloud infrastructure providers. Additionally, given SAP's tendency to prefer partnering over building, it is likely that even the 'public cloud' could end up getting spread across many of its hosting and other outsourcing partners."*

Source: Vinnie Mirchandani, SAP Nation 2.0: an Empire in disarray, page 43

Mirchandani's book was written in August 2015 and, to date, SAP continues its marketing campaign with respect to hosting, while in practice, it has been outsourcing the hosting to other parties that are true IaaS providers.

In May 2016 at its SAPPHIRE event, SAP announced a partnership with Microsoft that will have HANA and S4 hosted by Microsoft's Azure. (Source: *Microsoft Azure, SAP HANA on Azure*) Among a number of announcements made as part of this new partnership, hosting was not necessarily the primary emphasis point, but Microsoft joins AWS as providing the hosting capability for SAP. The realization is apparent that SAP is not all that interested in investing in its own hosting infrastructure of HANA for its ERP customers, and that most hosted HANA environments in the future may not be handled by SAP, but rather by either AWS (which we currently suggest as the best pathway to hosted SAP) or Microsoft Azure. This brings up the topic of hosting for acquired companies that were previously cloud-based before being acquired by SAP. Mirchandani's book *SAP Nation 2.0: An Empire in Disarray* (page 43), comments on this as well:

> *"Even where SAP offers public cloud options — for example with its SuccessFactors and Concur customers — the individual data centers are undersized and often supported by co-location vendors around the globe. SAP's 'about 82 million cloud users' are fragmented across products and across geographies. Little attempt appears to have been made, to date, and to consolidate data centers that support them. While compliance requirements dictate regional diversity in such facilities, they are further reminders of Balkanization of the SAP economy."*

Source: Vinnie Mirchandani, SAP Nation 2.0: an Empire in disarray, page 43

Indirectly, Mirchandani brings up an important question. That is, will SAP continue to have the cloud-based vendors that it purchased host their own applications, or will they follow the SAP model, which is to outsource the hosting?

It is important to consider that IaaS providers are currently growing at a rapid pace and growing the IaaS environment significantly in terms of the revenues that are generated. For example, Amazon's AWS is now larger than Salesforce, Microsoft, IBM, and Google's cloud infrastructure service *combined* (Sources: *Alice MacGregor, AWS bigger than cloud rivals Google, Microsoft, IBM and Salesforce combined, April 28, 2015*)[2] In the 2016 "Gartner Magic Quadrant for Cloud Infrastructure as a Service," Amazon was placed in the number one position, Microsoft in number two, and neither SAP nor Oracle were among the 14 companies profiled. (Source: *Lydia Leong, Gregor Petri, Bob Gill, Mike Dorosh, Gartner Magic Quadrant for Cloud Infrastructure as a Service, August 3, 2016*) And if more emphasis is needed to illustrate what is happening in the IaaS market, recently Salesforce made the decision to partner with AWS to host its customers. (Source: *Parker Harris, Salesforce Selects Amazon Web Services as Preferred Public Cloud Infrastructure Provider, May 25, 2016*)

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[2] See Mihăiță Bamburic, AWS more popular than Microsoft, Google and IBM's clouds combined (last visited March 6, 2017). Something that is beyond the scope of this paper is why AWS is profitable. AWS appears to be the major driver of profits within Amazon, which overall as a company has been known for being quite unprofitable. Interestingly, the other major player, Azure, appears to be unprofitable, and Salesforce and Workday, two of the largest SaaS vendors, also appear to be unprofitable.

Exaggerating the Transition to the Cloud

It is important to truly understand who the primary intended audience is when new software announcements are made. For example, here is a typical cloud announcement, and it caters to the investor community and analysts on Wall Street, instead of SAP's customers:

> *"The German vendor, Europe's biggest software company, said third-quarter cloud subscriptions and support revenue grew 116 percent year on year to €600m, while new cloud bookings, the key measure for SAP's sales success in the cloud, doubled in the third quarter to €216m. All numbers are non-IFRS. Cloud and software revenue increased 19 percent to €4.12bn, and operating profit increased 19 percent to €1.62bn.*
>
> *SAP CEO Bill McDermott said the results were 'the latest validation of our strategy.' The company said it now has 800 customers for its SuccessFactors Employee Central HR system, which is an increase of 79 percent in 12 months, and said new cloud bookings for its Customer Engagement and Commerce packages 'saw strong double-digit growth.'"*
>
> *– ZDNet*
>
> Source: Steve Ranger, Cloud, HANA surge are a validation of our strategy, says SAP chief, October 20, 2015

> *"To investors, the primary appeal of recurring revenue models is the value of predictable recurring revenue, particularly in comparison to one-time transactions. For example, a $20 million dollar company with eighty percent recurring revenue can count on sixteen million dollars at the beginning of every year. That figure is stable and predictable. Management can plan and invest accordingly."*
>
> Dave Key, Zuora, 3 REASONS WHY WALL STREET LOVES SUBSCRIPTION MODELS, last visited February 9, 2017

Here, ZDNet quotes McDermott as emphasizing SuccessFactors' growth. However, keep in mind SuccessFactors was 100 percent cloud-based before SAP purchased it, and SAP has expanded its scope by making it the system of record for Core HR, which, in turn, is forcing additional adoption.

Furthermore, SAP repeatedly classifies non-cloud revenue as cloud revenue. Therefore, we speculate it is difficult for analysts to really figure out what portion of SAP's revenues actually come from the cloud. The reason why SAP and its competitors do this is simple. Cloud revenues are considered by Wall Street as a barometer of a software or hardware vendor's ability to make the transition to what is generally agreed to be the new model of software delivery. A major reason why Wall Street prefers this software delivery model is due to the resulting predictability of revenue, as supported by the following statement:

> *"To investors, the primary appeal of recurring revenue models is the value of predictable recurring revenue, particularly in comparison to one-time transactions. For example, a $20 million dollar company with eighty percent recurring revenue can count on sixteen million dollars at the beginning of every year. That figure is stable and predictable. Management can plan and invest accordingly.*
>
> *The same cannot be said of a $20 million dollar business with no recurring revenue. That company has to start the year at zero. Of course it can make some predictions based on past performance, but it doesn't have a contractually obligated revenue stream to base ambitious expansion plans around."*
>
> *– Zuora*
>
> Source: Dave Key, 3 Reasons Why Wall Street Loves Subscription Models

The storyline is described by this quotation:

> *"Let's take a look at what happened to Adobe when it made a broad, systemic shift to a subscription-based model. Adobe transitioned its Creative Cloud Suite to a subscription model in May of 2013….*
>
> *At least initially, the market did not receive the news well. There was some debate as to whether the company should halt trading. But despite an 8% decline of overall revenue (but with a near doubling of subscription revenue) Adobe stock soared 55% in 2013.*
>
> *Today the company says 20% of its customers that are purchasing the updated online tools weren't Adobe customers before the switch. Piracy is down, and now it can more accurately track how customers are using its products and constantly push updates to individual users. Microsoft is seeing similarly successful results with its transition of Office 365 to a monthly subscription."*
>
> *– Zuora*

Source: [Dave Key, 3 Reasons Why Wall Street Loves Subscription Models](#)

One of the companies that is currently favored by Wall Street is Amazon. Amazon's AWS, which offers an enormous number of IaaS options, is currently growing very rapidly. AWS, unlike SAP or Oracle, has no on-premises business to protect. Actually, AWS was never on premises, so it is more appropriate to say that Amazon is growing its AWS cloud business rather than protecting an AWS on-premises business or transitioning it. Because Amazon is having real success in the cloud, it is the most transparent in its reporting and clearly differentiates its AWS business from the rest of its business operations. Unfortunately, most companies in this industry fall short of this standard. Organizations such as IBM, which have not been able to achieve a high level of success transitioning to the cloud, appear to be obscuring this with creative accounting.

> *"IBM has some of the most confusing 'cloud' reporting. Despite boisterous claims that it earned $9.4 billion in cloud revenue last year, a closer look at the figures raises questions showing that $4.5 billion of that revenue is related to 'as a service' offerings. Gartner wonders: 'What cloud revenue is not 'as a service?'' leading it to believe IBM is lumping non-cloud revenue, such as consulting and professional services in with cloud line items."*

Source: [Brandon Butler Network World, Feb. 9, 2016 Gartner: Vendors hype cloud revenue to impress Wall Street](#)

SAP is very similar to IBM in this regard. SAP has a lengthy history as a mainline on-premises software vendor, but due to the emergence of the cloud model, on-premises revenues are not valued the same way that they were previously. Independent research indicates that SAP's cloud prevalence is not nearly what it would like Wall Street to believe. The following quotation explains this:

> *"'Over the last 18 months, we have seen more of our members looking to move elements of their SAP estate to the cloud. However, as the survey results show, users still face challenges when it comes adopting SAP's cloud offerings,' said Paul Cooper, vice-chairman of the UK & Ireland SAP User Group. 'For organizations that have heavily invested in on-premises applications in the past, there still needs to be an attractive business case for them to move to the cloud.'"*
>
> *– The Register*
>
> Source: Jamie Davies, SAP cloud offering lacks clarity — user group survey, May 6, 2016

It is not only SAP that engages in this practice. The following quotation explains the lengths that Oracle goes to obtain sales with cloud revenue:

> *"What the account teams are doing is seeding cloud deals within larger deals. So if a customer does a $10 million deal, we are throwing in $500,000 in PaaS (Platform as a Service). The rep then gets his accelerator of 5X or 3X on that $500,000. I have seen this on 90 percent of our large deals. It is still booked as a sale and goes through the appropriate approvals with account reps getting credit. But in reality it is being given away. Somewhat amusingly, the customer's IT staff are not even aware of the inclusion."*
>
> Source: Eric Knorr, Oracle insider: We're not walking the cloud talk, November 9, 2015

Therefore, we can see that due to the enormous pressure from Wall Street to demonstrate growth in the cloud, organizations like SAP and Oracle expend a great deal of effort to give the appearance of being dedicated to the cloud.

The Battle for SAP Marketing Message Supremacy

We can observe SAP's twin strategies of promoting HANA as a new database innovation and, at the same time, promoting SAP's new cloud-based products. On one hand, SAP is emphasizing to its ERP ECC customers that the new database approach is a critical migration strategy, while on the other hand also promoting the idea of moving to cloud-based applications. SAP has de-emphasized the back end, because it will be managed by another software vendor or an infrastructure partner such as Amazon's AWS.

SAP wants customers to move to its cloud-based products, but there are two different areas that must be considered when analyzing such a move:

1. **Native SAP applications —** How realistic is it for you to be able to continue to utilize your existing SAP apps, in concert with S4? S4/HANA is not a one-for-one replacement of SAP ECC6. In addition to S4, should you plan to keep your many ECC modules live for the next 4 years?

2. **Acquired cloud-based applications** — Can SAP's acquired cloud-based apps really help you? Are they affordable? Did SAP purchase cloud-based apps with a primary motive to appear to be providing at least some cloud-based apps?

Today, as best as we can surmise, SAP has not yet successfully motivated its HANA database customers to purchase its other cloud-based products in significant numbers.

As reviewed on pages 12 and 13 of this document, SAP is not motivating a significant number of any of its customers to implement its HANA database, either in the cloud or on premises, even with over 5,800 licensees as of Q1 2017. This is touched on in this quote by Mirchandani in the preface of his book, *SAP Nation 2.0: an Empire in Disarray* (page 2).

> *"When you compare how nicely IT costs via SaaS applications, cloud infrastructures and mobile broadband have dropped in the last few years, you have to ask why those in the SAP economy have not followed that trend."*
>
> Source: Vinnie Mirchandani, SAP Nation: a runaway software economy, December, 2014, Preface Page 2

SAP appears to be somewhat protected from marketplace pressures for some of the applications that it sells. However, if SAP continues to acquire SaaS applications to comprise more of its portfolio, this will likely change. A true SaaS offering means a change in not only how the software is consumed, but to its sales process, how customers receive exposure to the application, and how salespeople are compensated, among a host of other changes.

Many of the early-adopter SAP customers were licensed to implement HANA apps, such as HANA Business Warehouse (BW/4HANA). It's not clear how many of these HANA licensees will eventually implement the S4 application. SAP may struggle selling its internally developed S4 application until the S4 app compares in functionality to the ERP ECC Business Suite products. See Figure 2 below, which shows removed or non-interwoven components of Business Suite missing in S4. SAP is evaluating which of those components will be critical enough to be reintroduced with later releases of S4. SAP is apparently careful not to market the S4 application as a completed business suite until S4 is comparable to ECC Business Suite 7i.
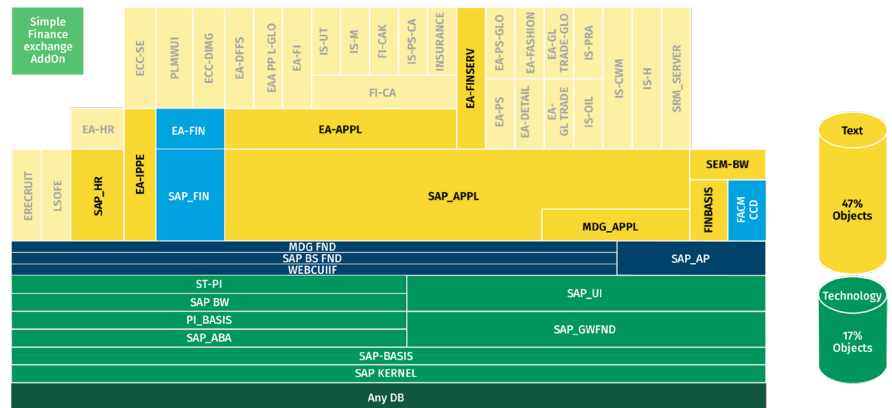
Figure 2. Removed or Non-interwoven Components of Business Suite Missing in S4.
Source: TEC206 – Architecture and Components of SAP S/4HANA

Not all of the representations of items that are labeled as "cloud" are actually cloud-based. If we look at an underlying component of the definition of cloud, it means that there is just one set of code base for the software that is used by all customers. This is referred to as a multitenant architecture.

Many of SAP's offerings are hosted cloud offerings and would not meet this definition. Even the most dyed-in-the-wool SaaS vendors have recently started to outsource their infrastructure. A second part of the definition of SaaS is that the underlying data model and system architecture are not customizable. This allows the software vendor to spend less time dealing with platform patching, compatibility, and upgrades. In fact, a true SaaS vendor is supposed to upgrade a single instance, which then updates all customers. This should then imply less support expense, and it brings up the question of SAP's support model with its 20 percent annual support costs. (Source: Gruman, Galen. "The Truth About Software As a Service," CIO Magazine, May 21, 2007) SAP has been mum about how it will provide and justify the value of its support in the new cloud environment. Further, SAP's customers are confronted with choosing among a growing group of software vendors that have significantly varying degrees of success implementing such SAP cloud products.

Conclusion

SAP is highly focused on selling cloud applications and has, during the past two years, been aggressively marketing its cloud-based products, after years resisting the growing SaaS trend. SaaS had never been a significant part of SAP's business model. In fact, there are still many questions about how SaaS will affect SAP's long-term profitability. SAP attempts to be very persuasive with its customers in order to motivate them to purchase its cloud-based products.

Within the past few years, this SaaS/cloud focus has motivated SAP to "open the vault," and embark on an acquisition pursuit to attempt to fill in some of the gaps in its product offerings. Yet, significant differences remain between SAP's stated cloud strategy and its cloud reality.

Few of SAP's deployments meet the definition of SaaS because they are not multitenant (among other factors). They are hosted, "private cloud" data center deployments. Wall Street provides higher valuations, i.e., "favors", cloud-based software vendors because Wall Street is sold on the concept of recurring revenues and the cost reductions associated with a SaaS-public cloud approach.

To buffer those expectations, SAP has taken creative liberties with product naming and marketing spin in an attempt to demonstrate that only its products should be considered when moving to the cloud. For example, SAP presents HANA as essentially commingled with all of its cloud offerings. However the following is also important to note:

– HANA is a database and not inherently a cloud product.

– S4 Finance is part of the S4 application, offered either as an SAP on-premises or an SAP cloud application.

– Both S4 Finance as a hosted application and S4 Finance running on premises, require the HANA database. SAP will not certify other databases, even though our research shows that there is no technical reason for it to limit S4 to HANA. (*For details on this topic, see the Rimini Street white paper "Considering SAP HANA Versus Oracle 12c."*)

– S4 Finance will, in most cases, be hosted as part of the private cloud and as a single tenant. This means it will not meet the definition of SaaS. Any multitenant application would be required to be deployed without any customizations, which is how very few of S4 Finance's predecessor implementations (ECC FI/CO) have been configured.

A thorough analysis of SAP's statements versus SAP's actual usage shows a strong predisposition to cloud-washing. Therefore, future SAP statements should be viewed through the perspective of understanding that SAP has an incentive to present a much more cloud-centric impression than currently exists. Stating one's strategy is an easy way to do this, because the strategy unfolds over time and does not have to reflect the current reality. You can see this in SAP's response to a famous statement by Oracle's Larry Ellison:

> *"Ariba runs on Oracle. SuccessFactors runs on Oracle. They just bought Concur; it's moving to Oracle. I have no idea what runs on HANA, but it ain't their cloud. That runs on Oracle. It's rude, but it's the truth."*
>
> Source: [Cloud Computing at SAP](#)

And SAP's response:

> *"This boasting rings hollow. SAP has clearly stated its strategy. We are enabling all SAP applications, including our HCM portfolio and the Ariba Network, on SAP HANA as the superior innovation platform. With HANA our customers can handle more data, process more transactions, and derive more actionable insight. Ariba SpendVisibility, SAP Cloud for Sales, and SuccessFactors Workforce Analytics are already on HANA today with greater performance, simpler operations, and higher user adoption. Key cloud applications built on HANA and productive with many customers today include Simple Finance, Customer Engagement Intelligence, SAP Cloud for Sales, and Mobile Documents."*
>
> Source: [TEC206 – Architecture and Components of SAP S/4HANA](#)

Notice that SAP begins by talking about its strategy. However, a strategy can be anything; it does not necessarily reflect the present and does not necessarily reflect the future. Larry Ellison was speaking about the present situation (at the time of the quotation), while SAP responded not to the present state, but to a potential future as outlined in its strategy.

SAP promotes the purchase of licensing for S4 Finance and entices customers with speed innovations provided by the HANA database. However, few SAP customers with existing ERP ECC 6.0 licenses have found a business justification to initiate the transition to the S4 Finance on-premises or cloud-based product.

SAP has stated:

> *"You can rely on proven enterprise cloud security and hosting services — and choose from a public, private or hybrid cloud environment."*
>
> Source: [TEC206 – Architecture and Components of SAP S/4HANA](#)

However, most can only choose a public cloud or even a hybrid cloud under conditions of implementation that are so rare that the options do not exist for most SAP customers. Therefore, the statement regarding choice is misleading. Instead, almost all SAP S4 customers will either implement on premises or in a private cloud. When the discussion moves to a non-multitenant public cloud, i.e., a private cloud, the cost advantages of having another entity host the SAP solution greatly decline. When you understand SAP's underlying motivations, it becomes obvious why this is conveniently omitted from the dialogue between SAP sales and its customers. Rather, potential SAP customers have found that the overall intended message was that all of the hosting would be taken care of by SAP, and that the cost implications of having an SAP single-tenant host as the solution was de-emphasized.

SAP is also selling cloud solutions obtained from its acquired software vendors. Many SAP customers are currently in the process of determining the requirements for migration to these cloud-based SAP products and attempting proof of concept migrations, and such are being analyzed. From their analysis, what is clear is that customers considering an S4 upgrade from ECC 6.0 or a new S4 implementation should retain system integrators who have been fully trained on S4 and HANA and also have certified teams. Due to the relatively few deployments, customers may find it difficult to find suitable system upgrade and integration consultants with the requisite S4 application and HANA database implementation experience.

The overall objective of this white paper is to encourage readers to investigate SAP's cloud offerings more closely, i.e., with a microscopic focus. When you do this, you may find, as we did, that you want to more deeply understand what is being offered and at what advantage, compared to what is needed and what has already been paid for. SAP's simple message is that it is swiftly transitioning to become a cloud vendor.

Rimini Street Functional Support Services

Rimini Street's Functional Support Services team helps clients develop a strategic roadmap for the modern ERP era. This roadmap reflects the strategic decision many of our clients have made to intentionally stay several releases behind the latest available version in their software archive and extract the maximum value from their ERP applications investment.

Rimini Street is at the forefront in helping customers optimize current systems and enabling their strategic roadmaps to the future by offering the following services:

– Functionality mapping

– Optimization analysis

– Innovation maps

Rimini Street conducts ERP research on behalf of our clients to answer specific questions or to resolve issues they have encountered, including:

– Oracle's cloud strategy

– SAP HANA versus Oracle 12c

– SaaS pricing and contract terms

– Changes necessary for SAP S4/HANA

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