Market Adoption Due Diligence

When is Market Adoption Too Much of a Good Thing?

The primary challenge for all start up technology companies is adoption. How do you get people to buy something new from a company they have never heard of? To be sure adoption is a good thing. However, it does not necessarily follow that maximizing adoption is always best. Remember that the ultimate goal for companies is to maximize revenue and there are many cases where the two are not necessarily linked.

In the past, when the predominant business model was selling high ticket solutions to enterprise IT, adoption directly drove revenue. However, today, when many business models are predicated on providing low cost or even no cost entry level versions, the relationship between adoption and revenue is no longer a sure thing.

We break markets into three categories – high, medium, and low – based on the correlation between adoption and revenue and recommend companies set strategy accordingly.

High Market Adoption: These markets are governed by the network effect. Under the network effect, the intrinsic value of a product or service increases exponentially as the number of users increase. More adoption drives more value which in turn drives more adoption, etc. For these companies, the strategy is simple – acquire users. YouTube, where more users means more videos, and eBay, where more users mean more product auctions and more buyers, are both examples of network effect businesses.

Medium Market Adoption: These are businesses, technology platforms such as databases or application servers, where the value of the company's products is enhanced by a community of companies offering value added products and services. While adoption is important for generating a community, it is not necessarily true that the company that has the most adoption wins the market. Instead, it is the company that generates the most robust community. Such company strategy must focus on community development.

Low Market Adoption: These are markets where the fact that one user has adopted a new technology has little bearing on the value that the next user receives. Application software companies, online content providers, and search engines are all examples of businesses where the intrinsic value of adoption is low. For these companies the strategy needs to focus on acquiring profitable users, not just any user. The most common mistake companies make in this

segment is to under price the offering based on the assumption that all adoption is good adoption.

One example where this dynamic has played out is the Vulnerability Management (VM) market. VM solutions are corporate security solutions that scan devices attached to corporate networks to identify vulnerabilities to hacker attacks. Two of the main competitors in this market are the SaaS company Qualys and the Open Source company Tenable. Tenable gives away the base version of its solution and has a total user base that is over thirty times larger than Qualys. However, Tenable has been able to convert only 250 of its 75,000 free users into paying customers. In contrast, Qualys has over 2,000 paying customers, nearly ten times as many as Tenable. Ultimately, Qualys gained adoption where it mattered most, among paying customers. It didn't matter that Tenable had the most total adoption.

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