

KEVIN DOBBS: So thank you for joining us for our X as a Service Files Podcast. My name is Kevin Dobbs and I'm with Accenture. And today, we're really happy to have Doug Merritt, the President and CEO at Splunk joining us to talk a little bit about his business model transformation.

Doug, in the last segment, we were talking about what was happening in the market. Now, I think it'd be really interesting to kind of understand your kind of transformation over the last few years. I think you called it the Term Cloud transformation. Can you give us a little bit of background about kind of what you were trying to do and kind of what your North Star was when you kind of set of the program?

DOUG MERRITT: Kevin, thank you for having me on the show, very excited to be here. So what I highlighted briefly in the last segment was the North Star for us. And I think a really effective North Star during transformation is the customer - the overall customer base or your view of how customers drive value from what you're intending to offer. And Splunk was founded to be a data technology, a data tool and the challenge with data is it can solve just

about any problem depending on the data tool. There's limitations to what different data tools can do based on what they're architected to actually solve and manage.

And our experience with customers was for them to be successful, especially because we're a big data tool and that is now a hot buzz term, buzz word, just like AI and ML are, but still is something people, certainly 10 years ago, were not familiar with at all and are still having difficulty really wrapping their arms and minds around to drive value. That the value of the data is the solution, the answer, the insight, the action that you take a lot of time and energy to get to. So you've got to find the data and you've got to begin to play with and understand it and then stripe it in the right way.

And, therefore, if our customers want to get significant value out of Splunk, we had to have a whole series of solutions on top of our data tool at that point in time to show them the way. To show them what was capable and to make sure they had the right return on investment and the right time to value.

And what we experienced is if we really want to do at scale, one, we had to turn our underlying technology into much more of a platform and more elegant way to serve thousands, tens of thousands, millions of potential use cases. We had to move the technology to be cloud based, both to adhere to the trends that we're seeing in the marketplace around cloud, but really more importantly, to give customers and partners that really rapid time to value we were talking about.

And then for Splunk, as we're doing those two things, we really had the opportunity to rethink the business model and create a more resilient company and move us from a company that like our last segment talked about sold you something that you took possession of up upfront, we collected our big check. If you do our job, we get some maintenance dollars and maybe a little bit of consulting, but that was generally done by our partners, like Accenture, and then hope we could sell you a bigger item in the future. So the pretty meaningful transformation on the business process approach and the business model approach on the cultural artifacts for the company, on the

technological landscape, the day in and day out way that people would have to start to think about doing business at Splunk.

KEVIN DOBBS: And what I think is really interesting about your story, Doug, is that unlike other companies who do the big bang and did it all at once and kind of massive transformation, you kind of did it in what we kind of call a two-step transformation. There was sort of like initially, we're going to move everything to a new economic model, monetization model, get the customers used to buying in a new way, driving value in a new way and then kind of set yourself up for longer term. We'll deliver the technology and everything else in a new way that you can consume.

So it's a really interesting model and I'm seeing more and more companies kind of take this kind of two-step approach. Tell me a little bit about how that worked for you?

DOUG MERRITT: Yeah, and a piece of it is certainly some strategy and a piece of it was the mother of necessity. It takes a while to build a highly capable

customer centric world-class cloud offering, but our view was from a human change management perspective, which almost always is the harder part of any type of change to move our buyers from a perpetual license that was generally capitalized and because that came from a different budget pool, to a rental license, a term contract that generally is treated as an expense and comes again from that different budget pool, was going to be a pretty dramatic shift from our own salesforce, from our own accounting department, our systems and then obviously our customers and the different finance teams on the other side of the fence with the customers.

So if we could really do our job effectively, then we could get that buying motion and that now more partnered approach with customers that, hey, we're in this with you. We're going to write a one or two or three year term contract and hope that we do a good enough job that you're going to want to renew with us in the future. And we're willing to collect less money over that one, two or three years than if you paid it everything upfront because we have confidence in our software and overall solution.

And that was that first step, but the ultimate goal and where we are now, which is let's continue to enhance our offerings, so that they would be really compelling in a cloud framework, which is very different than a customer managing the software, the hardware and the environment on their own.

KEVIN DOBBS: Yeah, and I think you guys have done a fantastic job kind of moving down that journey. One of the areas that times companies struggle with is you move into these new models, kind of the way you lead, the way you organize, kind of we had talked in the last segment a little bit about kind of the culture. I'll pick on sales for a second 'cause I know you and I know a lot about sales. But it's hard sometimes to get the seller who's used to selling the big deal, getting paid upfront to think about, no, I'm going to sell a smaller deal and maybe my comp plan's going to change and the way we approach it is we're equally concerned about renewals as we are new sales. How is it that you kind of changed the leadership and kind of maybe the way the organization functioned over time?

DOUG MERRITT: I think a lot like the shift from perpetual to term which accelerated like crazy. I was so surprised. We thought as we had 5 to 7 year journey and we had told the investor community, as we started this journey, which was my first year at being CEO, that we'd feel great when we get to 60% to 70% of our installed based being on term contracts in that time period. And we wound up at the final quarter of that three-year journey actually taking perpetual off the price list because we're at 99% term contracts. So, actually, it went much more quickly than we thought, but we chartered it a slower course.

On the sales change side, it's been a very patient journey and the perpetual license would be equivalent to a total contract value of three plus years of a term contract. And so, we had many, many years of working the dials on total contract value, so that they would begin to accept term contracts and then begin to accept cloud contracts from a payment basis, without the perpetual business falling off a cliff too quickly and us surprising our investment community. And we have tweaked that every single year to, one, try and neutralize the effects of term

and cloud versus perpetual and then begin to make perpetual licenses less attractive based on what we're seeing from our customer base and whether they're enthusiastic or not, given customer success is at a peak of our hill. And now, we're at the point where we finally rolled out annual contract value as a quota, which obviously, and we've taken perpetual off the price list entirely, which is obviously what we wanted to get to from a very simple commission plan and quota plan that has them focused on the right thing, which is let me serve my customers one year at a time. There are some incentives for additional years if a customer signs up, but all quote activity and focus is on that annual contract.

KEVIN DOBBS: And I know a lot of companies, one of the things they look at as they're making the shift is a lot of them don't even have customer success organizations because I think you and I being old time software people, that was usually tech support or just the support organization and that was much more orientated towards break/fix. You know, if something breaks, call the 800 number and we'll help you.

Whereas, customer success is for most companies, it's a new function that kind of emerges obviously critically important. How did that kind of manifest itself at Splunk?

DOUG MERRITT: As part of the now five-year journey, where as you started, we didn't have a customer success team five years ago. And we had a tech support team and professional services team in it and we inaugurated a customer success team, hired a leader, actually promoted a leader internally. And very patiently, like with the conversion to term and the now conversion to cloud and then helping the salesforce wrap their minds and arms around the transition and in building up that customer success team.

It's amazing what that team has done. It's gotten award after award from some of the most out in front and innovative organizations that evaluate customer success teams. But it's not an overnight journey. It's now a sizable organization. Every major contract comes with a free customer success representative. We had to instrument both the on-prem product and then make sure we had the right implementation of the cloud products. We've built a whole series of on ramps for customers to ensure for to the

sales teams, customer success teams and the customers to feel like they know exactly how they're beginning their relationship with Splunk. They know what the different value drops are along the way. There's continuous check-in periods. There's online ROI tools and payback tools. There's usage dashboards that they get access to. So it's been an evolving capability that every organization that goes down this path has got to get to. Just going back to a few - if you take the risk, to not get your payments upfront, you better be successful and that requires a true side-by-side walk between the organization providing the service and the customer themselves.

KEVIN DOBBS: And it's really kind of enlightened self-interest because if you don't get this right, it's not going to work.

DOUG MERRITT: It is. And for something like Splunk, it's interesting because the uniqueness that we have as a data product is the initial ingestion of data or touching of data doesn't force structure in the data. It's a very different way of looking at data universe. We're still one of the only companies in existence that has that mentality.

There's many benefits, but one of those benefits is you can begin to bring different people to that raw data set and they will each get some incredible insights and value from that data, which makes that customer success journey even more important and partner oriented because our success within a company comes as more and more departments, more and more users, more and more business value is driven from that same core set of data that's powering the initial set of use cases and value drivers that we work with with the customer.

KEVIN DOBBS: And I want to kind of talk a little bit about 'cause, again, you're a data company. We were just talking about kind of metering and kind of measuring what people are doing. So one of the things that I've always seen that these type of companies, these as a service companies are very metrics driven, key performance indicators. So I mean it's Splunk running the company. How is it that you're thinking about success and how do you measure it?

DOUG MERRITT: As you guessed, there are too many measures and the challenge is always on focusing which ones

are the most important and going back to the beginning of this conversation. The top of the page metrics that we stare at and we care about the most are the overall customer health and customer success metrics. How many customers are we onboarding? How many customers are active and how many customers - how rapidly do customers achieve the initial value definition? How far over that value definition are they? How many users are interacting with the system on a daily, monthly basis? But those really are the leading indicators that we care most about.

If those are going the right direction and we wind up with really interesting and effective net dollar based expansion rates, effective overall renewal rates. But they go back to our we serving our core end user communities effectively or not?

KEVIN DOBBS: And this is another question I get asked a lot is like, how frequently do you check your metrics? You know, in the old world, it was like we would report metrics. We would have a QBR or we would have our quarterly releases. It seems like best in class companies are really

thinking about their metrics much more frequently than that.

DOUG MERRITT: I think the teams within Splunk are looking at those metrics hourly and daily. As an executive staff, we have a weekly tactical executive staff meeting which is really focused on the operating cadence within the company and is deeply centered around these metrics.

So we look at the whole slate of metrics and from a core weekly basis, we pair those down to a little bit under 40 metrics. Not all of them move on a week to week basis as you'd expect. But the check-in in our meetings is let's go around the table and like any other company, we are very functionally centered and look at the landscape for each one of our executives based on what's happening with the metrics and the hard part with active and the classic Type A personalities is this is not an exercise to thump your chest and pump your arms that, hey, everything is green. This is an exercise to be excited about finding a yellow or red 'cause it gives us an opportunity to improve as a company and as a team. And that's a hard one to continue to

reinforce for me, all the way down because we all want to be successful and look successful in each other's eyes.

And that's I think a constant cultural exercise to make sure that we're all about retrospectives and data inspection and finding ways to make ourselves better. And as a team, that's our job is not to attack each other, not to point fingers, not to cast blame, but find a way to work together to improve the business.

KEVIN DOBBS: Yeah, and that's another thing that we see is that a lot of times having team metrics, the multiple groups have to work together in order to deliver the metric is really helpful and kind of solidifying. I even think about a customer journey from the point of discovery through the time you sell them, to onboard them, to renew them.

I mean there's a lot of groups involved in that kind of experience. So it's hard if the metrics just measuring one piece of it and the customer in the end is feeling like they got five different experiences as opposed to one single experience.

DOUG MERRITT: Yeah, I mean the good news is there's really no way to have customer value achievement be one group's charter. There definitely is the customer success manager at the head of that team, but that value achievement is everybody. What were they promised and how effective was the ROI calculation going in? How our partners actually facilitating in that drive? Is the product working the way that it should as it continued to be modified in the appropriate way? Did we market the right messages? Is the legal contract easy to administer?

But that value - anyone of those metrics really is an umbrella metric that winds up including the vast majority, if not all of the functions within a company.

KEVIN DOBBS: That's great. So going through your transformation over the last few years, you mentioned one of the surprises was, wow, everybody adopted this a lot faster than I thought. Were there other surprises along the way that you kind of encountered?

DOUG MERRITT: Without a doubt, the speed that everything happened, I think, was a pleasant surprise with setbacks along the way also. There's been so many different

pivots that we've had to make. But I think because we really started with let's visualize and find the customer journey and how customers will find value in this. Most the targets are going to be in pretty - I'd guess you call them almost sandbags in the rearview mirror. Although, the 70, 80, 90-hour weeks to get there, that all of us have spent, it didn't feel like the sandbag in AOA.

I think the other piece that I think we knew going in, but was still interesting to see along the way is culture matters a ton. We simultaneously did a lot of work on evangelizing, growth mindset and having a whole chunk of explicit training, individual training, manager training, tooling, to really reinforce that the universe is more abundant than scarce. To use that to gain confidence to lean in to serve customers and don't worry about is the deal going to shrink or are you going to leave value on the table.

So the cultural drivers to try and make sure they're all on the same page. And then making sure that you continue to drive a diverse team. Diversity from the larger number of organizations that we recruited from, you know,

five, six years ago, I'd say the number of recruits that came into Splunk that had a really strong Software as a Service background was probably much lower, much higher today, but diversity overall.

We started publishing our diversity metrics three years ago. It was always one of those I think important moves, but maybe the teams could find that to be risky. And then very aggressive goals on all avenues that we still need to triple down or effort on 'cause you're never hitting the target, so you want to make sure that we're bringing diverse viewpoints and resilient and greater viewpoints to the table.

KEVIN DOBBS: So, again, fantastic insights, Doug. We really appreciate you spending time with us today.

DOUG MERRITT: Well, thank you, Kevin. I really enjoyed the time together and looking forward to more.