REPORT REPRINT

Kaminario stakes future on service providers and software-only business

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The all-flash storage specialist has handed the hardware side of its business to a giant distributor, and says its expanding strategy of focusing on sales to service providers is paying off. Has Kaminario found a path to long-term survival?

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Kaminario was part of the wave of startups that pioneered all-flash storage about five years ago. Now, it is one of the last of those companies to exist as an independent entity. That is a difficult position to hold – the market for all-flash arrays (AFAs) has since become dominated by giant suppliers. However, Kaminario expects to become cash-flow positive this year. Given the struggles of other would-be entrants to the storage system sector over the last several years, that is a noteworthy positive sign.

Since 2015, Kaminario has been switching the sales and product development efforts for its scale-out AFA away from its previous midrange enterprise focus, and toward SaaS providers or web-based businesses. Roughly 85% of the company's revenue now comes from the latter type of customers, and Kaminario is beginning to reach out to various flavors of IaaS provider.

Kaminario has long described its systems as being based on commodity hardware. The company has announced that, although its customers will continue to buy appliances, it is handing the hardware side of its business to giant distributor Tech Data. Separately, Kaminario says it will soon ship an all-NVMe version of its existing AFA, alongside management software that it says will make its new device highly composable (i.e., dynamically reconfigurable). We will cover those products in a separate report.

THE 451 TAKE

It's hard to fault Kaminario's strategy. Focusing on SaaS providers reduces its sales overhead because those customers buy in larger quantities and make more repeat purchases than enterprises. Extending the focus to cover MSPs and other types of IaaS providers takes Kaminario into a sector in which infrastructure spending is growing faster than in the enterprise market. The move to a software-only model makes Kaminario more attractive to investors by improving its margins, but more importantly, it promises to reduce costs for customers by exploiting Tech Data's scale in hardware supply and support. The risk is that potential buyers may balk at separate sources for technical support of hardware and software. However, we think the risk is limited. Tech-savvy service providers are the most likely of all customers to appreciate the benefits of the software-only model.

COMPANY BACKGROUND

Founded in 2008, Kaminario launched its first K2 storage system in 2010. But the company did not settle on the current form of the K2 (powered by SAS flash drives, like most other AFAs) until 2012, and the device did not become truly competitive until 2014, when it gained dedupe and compression functions. We believe the company was also slow to develop a channel partner network. The company says that almost 100% of its sales are now made through its network of more than 200 partners.

Kaminario has never said how many customers it has won, but since 2016 it has been saying they number in the hundreds. Currently, there are just over two dozen named customer case studies on Kaminario's website, including both SaaS providers and conventional enterprises. Privately, the company has revealed the names of several dozen customers to 451 Research.

Headcount at the firm is about 280. VC to date totals $218m. The most recent fifth round of funding was announced in January 2017; raised a healthy $75m; and was led by new investor Waterwood, a private equity firm, and CIRTech, a venture capital firm, with participation from previous investors.

SAAS, AND NOW IAAS PROVIDERS

Kaminario has been selling to SaaS providers that deliver web-based services across a number of industries – for example, healthcare management, retail and financial services. In 2015, Kaminario said that about 50% of its sales came from that source, with the rest coming from non-SaaS enterprises. For 2017, the percentage rose to about 85%, the company says. Four of the world's largest payment processors have bought Kaminario AFAs, according to the company.

Kaminario is still making sales elsewhere, including (for example) a recent large healthcare VDI implementation. However, although such non-SaaS deals can be large, they are not the priority because they incur larger sales and marketing overhead. Across the board, the company says deals averaged roughly $250,000 in 2017, and that it scored multiple eight-figure deals.

Although OEM vendors are reporting dramatic growth in sales of AFAs, that simply reflects the current market transition from disk-based to all-flash storage for many primary workloads. Overall, enterprise spending on storage is flat. Among enterprises that are SaaS providers or web-based businesses, none but the very largest want to run their own datacenters. This has been driving their infrastructure spending toward service providers. According to Kaminario, only about one-quarter of SaaS or 'cloud software' is now running on on-premises infrastructure. We find that estimate believable.

But for various reasons, many SaaS providers are not moving to IaaS provided by hyperscalers such as AWS or Microsoft Azure, and are more interested in a range of alternatives. As a result, Kaminario is expanding its sales efforts to cover a spectrum of other IaaS providers, in the form of telcos, outsourcing providers, MSPs, hosting service providers and regional VARs.

Currently, about three-quarters of Kaminario's revenue comes from North America, in part because that region includes the greatest concentration of SaaS businesses. During 2017, the company began expanding its APAC presence.

HANDING OFF HARDWARE

Until January, Kaminario had been selling appliances, but from now on it will be a software-only vendor. However, this change will not allow customers to make software-only purchases. They will continue to buy K2 appliances, but the appliances will no longer be built by Kaminario. Instead they will be built by Tech Data.

The change is possible because – like many other storage systems – the core value of Kaminario's K2 device is in its software, which runs on commodity hardware. Tech Data is the world's largest distributor, and because of its scale and supply chain specialization, Kaminario says Tech Data can buy hardware and create appliances at lower costs than Kaminario itself, using specifications supplied by Kaminario. Tech Data will sell the appliances through Kaminario's channel partners, with what Kaminario says will be a transparent, single-digit markup on the hardware.

Tech Data will provide 'supply chain support services,' while Kaminario will continue to provide 'centralized support management.' We understand this as meaning broadly that Tech Data will not only supply the appliances, but will also handle field hardware replacements, and Kaminario will continue to provide higher levels of technical support. Kaminario will provide Tech Data with a range of hardware specifications, and in the past has said that its systems were based on Supermicro servers.

The software will be licensed separately, on flexible usage-based schemes in the style of enterprise license agreements. ViON, a service provider to US federal agencies and an existing Kaminario customer, has been named as the first buyer of K2 appliances under the new model.

COMPETITION

The overall market for AFAs is dominated by five companies: Dell EMC, HPE, IBM, NetApp and Pure Storage. Although the majority of those companies' AFA sales are made to conventional enterprises, they all also sell to nonhyperscale service providers. These are the companies that Kaminario will encounter in the majority of deals.

Alongside the all-flash version of its flagship FAS system, NetApp sells AFAs originally developed by SolidFire, an AFA pioneer that it bought in 2016. SolidFire is worth mentioning because there is both a mirror-image contrast and a direct parallel between SolidFire and Kaminario's strategies. SolidFire came to market in 2011 with a scale-out AFA that it initially aimed at service providers, but in 2014 it widened its sales efforts to include enterprises, which soon became a major part of its business. That is the reverse of Kaminario's history. We think this is explained by the relatively high price of flash in 2014, compared with now. Back then, that high price forced SolidFire to widen its net and expand its market reach, we believe. Since 2014, the per-GB price of flash has more than halved, making conditions different for Kaminario.

However, in a direct parallel to Kaminario, in 2016 SolidFire launched a program in which customers can buy appliances based on SolidFire software, but built by resellers. Like Kaminario, SolidFire stressed that the value of its systems is in software, not hardware. One difference, however, is that SolidFire did not quite go the whole hog, and continues to offer customers appliances built by itself, alongside the option to buy appliances built by the channel.

SWOT ANALYSIS

STRENGTHS

Kaminario has established what it says is a sizeable and growing customer base. Its focus on SaaS providers, and its plan to extend into multiple forms of IaaS providers, reduces the cost of acquiring new customers, and leads to greater repeat business.

WEAKNESSES

Kaminario's biggest weakness continues to be its small size compared with the incumbent suppliers that dominate AFA sales.

OPPORTUNITIES

Enterprises and especially SaaS providers or web-facing business are moving out of their own datacenters and into a range of different types of IaaS provider, making the latter a growth market compared with the sluggish enterprise market.

THREATS

Service providers may not warm to Kaminario's software-only model, although we believe this is unlikely.