



## After Acquiring Macromedia, What's Next for Adobe? Ask Bruce Chizen

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*In 1985, Adobe Systems had one major product -- a printer controller built around Adobe's PostScript imaging language marketed to printer manufacturers. Now, having completed its acquisition of Macromedia on December 3, 2005, Adobe is the fifth largest software company in the world.*

*Adobe currently controls two of the dominant formats for electronic content -- the Adobe Acrobat PDF format for electronic documents and the Flash SWF format for interactive web content. Adobe plans to leverage these and other core assets to provide an "engagement platform" that it hopes will provide the foundation for the next generation of software and application development -- both on the web and on users' desktops.*

*Adobe's vision is grand. CEO Bruce Chizen hopes that Adobe will provide the interface for any device with a screen -- "from a refrigerator to an automobile to a video game to a computer to a mobile phone." Such ambitions put Adobe squarely in the sights of Microsoft, which currently dominates desktop software development.*

*And Microsoft is moving quickly to counter Adobe's moves. It has announced a number of products poised to compete directly with Adobe's core products. Microsoft's strategy includes, among other initiatives, positioning elements of the forthcoming Windows Presentation Foundation to compete with Adobe's Acrobat and Flash applications, and potentially undercutting Adobe's profitable Acrobat product line by including PDF creation in the next version of Microsoft Office.*

*Knowledge@Wharton recently met with Bruce Chizen in his San Jose, Calif., office, where he spoke about the details of the Macromedia acquisition, Adobe's plans for integrating Macromedia's technology to develop the next-generation application platform, and his views on the challenges presented by Microsoft. An edited version of that conversation follows.*

**Knowledge@Wharton:** How does it feel to have closed the acquisition of Macromedia?

**Chizen:** It's great. It is going even better than I had anticipated. And we went into it being realistic. Any kind of merger and acquisition activity is hard. But there have been no surprises -- which is shocking.

That doesn't mean there won't be!

**Knowledge@Wharton:** Let's start with the basic question: What was the primary motivation behind the acquisition of Macromedia?

**Chizen:** Flash.

**Knowledge@Wharton:** That simple?



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**Chizen:** The combination of [Acrobat's] PDF [file format] and the Adobe Reader with Flash's SWF [file format] and the Flash Player enables us to create an "engagement platform." Think of it as a layer or a vehicle in which anybody can present information that could be engaged with in an interactive, compelling, reliable, relatively secure way -- across all kinds of devices, all kinds of operating systems. If you look at the success that Adobe has had with Adobe Reader and the ubiquitous nature of that client combined with what Macromedia has done with the Flash Player -- especially on non-PC devices -- that puts us in a position that is probably better than anybody else's.

**Knowledge@Wharton:** You have published a few things about combining HTML, PDF and Flash's SWF format -- and you have mentioned this Adobe engagement platform. But there's still a fair amount of confusion about exactly what that is. Can you give any details about what it will or will not do?

**Chizen:** We won't do a browser. But we do think that there are applications that need to run on the [user's desktop] client [software] that need to work in both a connected and a non-connected fashion, that require the richness of Flash, the reliability, the relative security, the layout capabilities of PDF -- but also need to consume HTML. Imagine a ubiquitous client that allows you to do all three of those -- and then a series of programming tools, like [Adobe's] Flex, making it easy for anyone to develop applications for this ubiquitous client.

**Knowledge@Wharton:** So this would be a desktop runtime environment?

**Chizen:** That's a good way of thinking about it, yes.

**Knowledge@Wharton:** This obviously brings up certain competitive issues. Microsoft's Windows Presentation Foundation has similar ambitions, and Microsoft is talking of "Presentation Foundation Everywhere." They may offer this platform not only in the Windows environment, but on the Macintosh and possibly others as well. Are we going to see head-on competition [between Adobe and Microsoft] to establish the platform for the next generation of web and application development?

**Chizen:** Perhaps.

I think the fact that we have been at this for more than 10 years with the Reader, and Macromedia has been at this for almost as long with the Flash Player, and the fact that we are ubiquitous today makes us believe that we will end up being the appropriate platform in which to have these rich Internet applications.

Microsoft's attempt with Windows Vista is a "1.0" attempt. What they end up delivering, when they end up delivering, and how portable it really is across operating systems, are still unknown. They are supposed to ship Windows Vista the end of this year. Avalon and Metro, or what's now the XML Paper specification -- which has become the Windows Presentation Foundation -- is an intriguing concept. It's great that they have recognized what we have done and have tried to imitate it.

The ecosystem that exists around both Flash and PDF -- and the fact that we are cross-platform and [have an] open specification -- give us reason to believe that we will be the one that is successful.

All the publicity over the state of Massachusetts' proposal around open formats -- and the fact that PDF was a part of that initial proposal -- are other examples of where we are versus where Microsoft is. We're there. Right now they are just talking about what they plan on shipping.

**Knowledge@Wharton:** PDF's status as a published standard has always been key to your positioning. But, as you know, Microsoft is submitting Office Open XML to [the standards organization] ECMA to get it published as a standard. And Sun and others are supporting [an alternate] Open Document format.

Since one of PDF's big competitors has always been native application file formats, do you see this move toward standardization on the part of these formats as a serious competitor to PDF going forward?

**Chizen:** I would if PDF hadn't become the standard it's become. Because you have so many mission-critical workflows built around PDF -- everything from IRS tax forms to FDA drug regulatory submission documents to U.S. court electronic briefings -- and because Adobe has a 20-year history of not messing with the open specification process, I believe the community at large trusts the approach we have taken. This is demonstrated by their willingness to adopt us as their standard.

**Knowledge@Wharton:** One of the other things Microsoft has announced is the ability to save as PDF in Office 12. This means that, once that happens, non-Adobe technologies are creating PDF in MacOS X, in StarOffice, and on Windows in Office [applications]. Isn't this a challenge to one of your major revenue streams?

**Chizen:** Maybe. But we don't think so. First of all, it's somewhat flattering that Microsoft has validated a document format that is not theirs, but one that is Adobe's -- which suggests that their customers were demanding that it do so.

We had anticipated for many years that the revenue we achieve around PDF creation would, at some point in time, go away. It's an open standard! There are many clones out in the marketplace today that create PDF and compete with Acrobat.

What we have done over the last five years is added functionality beyond PDF creation in our product line-up. If you look at Acrobat today it is much more than just simple PDF creation. In fact, we have a product, called Acrobat Elements, that just does PDF creation, and it represents a relatively tiny piece of our overall revenue -- less than one percent. Most customers choose to buy the more feature-rich products, Acrobat Standard and Acrobat Pro, which do annotations, digital signatures, web capture [and so on]. And many customers are buying LiveCycle, the server products for mission-critical workflows. That suggests to me that even though PDF creation will become free with products like Microsoft Office, our revenue streams will continue on.

In fact, with more PDFs being created from Microsoft Office, it gives us an opportunity to take those PDFs and do more with them, like building mission-critical workflows around them.

**Knowledge@Wharton:** The enterprise sales cycle that's required for the LiveCycle products is very different from the two-tier shrink-wrapped product sales you have traditionally done. Is that a challenge -- changing the way you sell?

**Chizen:** I think people forget that Adobe started out as the PostScript company. PostScript was a mission-critical application to every printer manufacturer that we sold to, and, even today, we sell to most of the major printer manufacturers around the world. Selling to a Canon, HP, Xerox or Ricoh requires an enterprise sales capability; it requires a high degree of support and service; it requires sophisticated negotiations and contracts.

Over time, a big piece of our business has shifted to shrink wrap, and we have been spending the last three years enhancing our enterprise sales capability. It's been hard. It's been a lot of work doing the transformation. Fortunately, the rest of our business has been so strong that we have been able to take some of the profits from [there] and [use them to] help us learn and invest in the enterprise software business. But now that we have three years worth of success under our belt, it's becoming a lot easier.

Plus, over the last couple of years, Macromedia had invested heavily in an enterprise sales organization. By acquiring Macromedia, we pretty much double the enterprise sales organization that we had

previously.

Last quarter, we had 63 customers that bought at least \$50,000 worth of LiveCycle product licenses. Not professional services, just \$50,000 or more in product licenses. Think about that: If someone spent \$50,000 buying a product license from us for a server, they probably spent \$200,000 or more in deploying it, either through their own resources, through a third party or through Adobe.

That says to me, we're making a ton of success.

**Knowledge@Wharton:** If the deployment costs [for these enterprise products] are roughly four times the software costs, is that a business you plan to get into? Will the services piece be something you will be doing in partnership with other companies or something you will build up internally?

**Chizen:** Our intent is not to be in the services business as a business objective unto its own. We *are* in the services business. I think we have more than 100 people out in the field today who do services. However, the intent is to do it for those customers that require it, those customers that we believe we can learn from, so we can take what we learn and bring it back in the product development teams. Plus, we want those services people to be able to train third-parties, like Accenture, like IBM Global Services, like the Indian professional services companies Tata and Infosys, and so on.

So, it's not our intent to be in the services business *per se*, but we know, as an enterprise software company, it's necessary for us to be in the services business. And we are.

### Structuring the New Adobe

**Knowledge@Wharton:** Let's turn to the details of the acquisition. As you are finalizing the acquisition and looking at joining the two companies, what is the process by which you determine the structure of the new company and, in particular, the management leadership of the now combined company?

**Chizen:** First of all, what I enjoyed about this process was that it was not one of those where we said, "Gee, we should buy Macromedia." It came after we took a look at the strategy and our ability to execute against the strategy.

We wanted to do a rich client [software application]. We didn't have the animation pieces. We wanted to be more aggressive in the video realm, but we didn't have a video playback mechanism. We wanted to be much more involved in publishing to non-PC devices, but the Adobe Reader can only deal with a certain type of device and a certain type of content for those mobile devices.

And then we looked at Macromedia and said, "Wow. They could actually fit many of the holes in our ability to execute against the great strategy we had put in place." Strategy is one thing, but you need to be able to execute.

Fortunately, at the time Macromedia was also realizing it had too much on its plate, and that being part of a bigger company would allow it to fulfill its vision.

So, strategically we realized it was the right thing; they realized it was the right thing. Then it came down to: How are we going to organize for success? Where should the focus be? Where are the synergies?

And we said, the first thing we have to do is have a real platform group and begin to treat our engagement platform the same way an operating system company would treat its operating system. You want

developer tools, you want to be able to work with third parties, you want to treat your internal customers -- the other business units -- appropriately, and you want to prioritize your needs.

We looked around and saw that there was a person at Macromedia who was the perfect fit to run that -- Kevin Lynch. Kevin, as you know, was responsible for a lot of the success that Macromedia has had over the years on the technology side.

Then we looked at the creative [professional] business and said, "The combination of [Macromedia's] Studio and everything we have done around the Creative Suite should all be in one business unit." And we looked at both Adobe and Macromedia and we realized there wasn't anyone in the combined organization who had experience at running a business of that size, and we had better go outside to hire that expertise. That's what we're doing.

And so on. We looked at each of the businesses and found the most qualified person to do it. Fortunately, there were a lot of qualified people on the Macromedia side. And we did work hard to see if we could find people in Macromedia to fill key positions, because we wanted to make sure that we didn't destroy the assets that we were buying.

We're an IP [intellectual property] company. At the end of the day, what we do is in people's heads. If we spent \$3.4 billion on Macromedia and all the great people left, we would be left with nothing. So being able to provide management opportunities that were appropriate for the Macromedia executives ended up being a great thing.

**Knowledge@Wharton:** You have six business units in the new organization and, as you have already noted, one of them has an interim head.

**Chizen:** Correct.

**Knowledge@Wharton:** Of the other five, four -- 80% -- are run by former Macromedia employees. Is there something we should conclude from this? Did Adobe need to be "shaken up" in some sense?

**Chizen:** Let me just clarify one thing. All those business units report to Shantanu [Narayan, Adobe's president and COO], and Shantanu is Adobe. Shantanu works for me, and I'm Adobe. Some of the other executives are Adobe -- the head of marketing, head of HR, and, up until recently, the finance head. I look at that overall management team, and there's some balance there. We can't lose sight of that.

To answer to your question specifically, Shantanu and I used the Macromedia integration process as an opportunity to figure out what we needed to do for the future of this company. This is a company that's gone through significant growth over the last few years. If you look at our compound annual growth rate over the last three years, it's 23%. For a company our size, that's enormous growth. With that kind of growth, you end up creating organizational challenges that you want to be able to fix.

We used Macromedia as an opportunity to reorganize the company. At that point we wanted to put the right people in the right job.

Also, there are a number of Adobe executives who have been here a while, who made a lot of money, and saw it as an opportunity to do something else with their life on the personal side.

It's the combination of those factors that led us to the decisions that we made.

**Knowledge@Wharton:** How will you evaluate the success of this acquisition?

**Chizen:** We were fortunate, I guess, that the regulatory bodies took their time. That gave us a lot of time to do planning. It gave us a lot of time to deal with cultural issues, integration issues, management issues.

When I think about a year from now, there are three things I'm measuring.

First of all, revenue and profits. Did we meet our business objectives for the year? Because if we do the right thing, our customers will continue to buy our products. That's the first thing.

The second will be our product milestones, where we begin to integrate some of the products through the year. Some will ship this year; some won't ship until 2007, but I'll be able to look at the milestones and see if we've gotten there.

Day one, the fact that we announced three brand new bundles was very compelling. Or the fact that Lightroom, which is the new beta [software for professional photographers], supports Flash in its first incarnation is pretty telling. You'll begin to see integration throughout our product lines where the customer gets a big win. I'm going to look at those things we have on our three-year product roadmap to make sure the milestones in the first year are being accomplished.

The third thing we will look at is attrition. Have I been able to keep both the Adobe employees and the Macromedia employees excited and motivated? It's a cultural challenge anytime you bring two companies together. My goal is to make sure the employees are motivated, inspired. A true test of that will be the attrition rate. Is it below the industry average?

So those are the three things I will be paying attention to.

## Looking Forward

**Knowledge@Wharton:** You are now in a fairly broad selection of markets. You have creative pro, developer, consumer, enterprise, the mobile space. Which of these is going to be your principal focus for the next six months?

**Chizen:** All!

First of all, we will never lose our focus on creative professionals. That makes up the bulk of our business. We continue to believe that as long as we add value for our customers, we'll continue to grow that business.

And the world of publishing -- I'm using the word "publishing" in a broad sense -- is changing so quickly that there's a lot for us to do. Video is exploding, which means that we want to enhance our video solutions. We want to publish to non-PC devices, and that requires a set of tools.

And we want to be able to begin to integrate the Studio products, especially Dreamweaver and Flash authoring, with products like Photoshop, Illustrator and InDesign. The Creative Suite with Studio -- we want to see more integration there, making our customers' lives easier, more productive, more efficient.

So that's one big area of focus.

The second focus will continue to be on the enterprise. We have come a long way with LiveCycle.

We had an initiative at Adobe around rich Internet applications for enterprise applications. Macromedia has something called Flex, and we think the combination of those two, especially for quick development cycles with things like [Macromedia's] ColdFusion [web application development product], makes for some really great applications. If you think about a mortgage application that's electronic, where you have real-time charting based on what kind of mortgage you choose -- that would be an example of the marriage of Flex and LiveCycle.

So you will see a continued push on the enterprise side.

As for knowledge workers, Acrobat is a \$600 million to \$700 million a year business for Adobe; we're not going to walk away from that business. We think Breeze, as a real-time collaboration solution, will allow us to enhance what we have already done with Acrobat, which is a serial communication product. So you will see us begin to marry Breeze and Acrobat together. That will be a major focus.

Then, of course, there's the whole area of mobile and our goal of continuing to become the ubiquitous client on mobile phones and non-PC devices, and coming up with solutions like FlashCast to take advantage of that.

That's how I see the world. In terms of which one will be prioritized over what period of time, that will change as we understand more about those opportunities.

But right now, it's great to be sitting here. It's a unique position.

**Knowledge@Wharton:** You mentioned the mobile space. This has been a big focus for the former Macromedia. Adobe had moved into that space with some PDF penetration. How do you see that space playing out, in particular as contrasted with the engagement platform where we are talking about a richer, fuller, larger desktop client?

**Chizen:** Just think of it as a "mini engagement platform." You already have agreements with most of the mobile manufacturers with Flash Lite. In some markets where you have fast, high speed bandwidth from the carrier, like Japan -- where you have third generation phones and even fourth generation phones -- they are actually including the Adobe Reader because both the networks and the devices are capable of that type of content.

What you will see us do is focus on taking what we are doing with the engagement platform and shrinking it down. In reality, we will start small and build it up. And you will see a mini engagement platform on all of these clients.

Now, the speed of the network and the capability of the device will determine how big that footprint can be. Clearly, today, on most of the mobile phones it needs to be relatively small. But these devices will become more and more powerful and you will see many, especially in emerging markets, bypass the PC and go right to these devices.

So our goal is to get our engagement platform, or the "light" version of it, on these devices. You will see us add mobile capabilities in our existing authoring products the way that Macromedia has done with Flash authoring and its emulators. But you will also see us come out with servers like FlashCast, where you can actually push data right to these phones or consumer electronic devices.

**Knowledge@Wharton:** Is the business model a challenge as you move into these different spaces? The Flash Player, free on the desktop platform, is a licensed product for Macromedia on handsets. The Adobe Viewer is generally free.

**Chizen:** Except in the case of some of the mobile devices and consumer electronic devices.

**Knowledge@Wharton:** And when Macromedia was looking at a product called Central -- which in some ways seems to have several of the characteristics of the engagement platform -- it had a license-free runtime, but would charge publishers [to deliver content]. Any sense of how you are going to monetize all this?

**Chizen:** Time will tell what approach we take. Macromedia has been able to charge for Flash Lite for mobile devices, as well as Flash running on consumer electronic devices. Adobe's strategy, with some exceptions, has been to not charge for the client.

Even though I like the revenue, I suspect over time you will probably see us back away a bit from charging for the client and look to make our money through servers, desktop software, advertising revenue models, and so on. But not charging for the actual client.

Clearly today there is so much value in what we are offering that the customer is willing to pay. So, I'm not willing to walk away from that. But if I have to make a trade-off between ubiquity and revenue -- as it relates to the mobile client business -- I'll go for ubiquity. Because if I have my client everywhere, then I can make money doing other things, as we have proven with the Adobe Reader.

**Knowledge@Wharton:** Are you dedicated to cross-platform?

**Chizen:** Apple is still critical.

**Knowledge@Wharton:** How important is Linux? How many platforms are we talking about?

**Chizen:** On the desktop it really means Linux, Mac and Windows. On the non-desktop it means just about everything, but most folks on the non-PC side are moving over to Linux. So that makes it easier on us.

**Knowledge@Wharton:** To some extent, Apple's continued strength plays to your advantage. If it's a single platform world, much of the advantage that you bring isn't there.

**Chizen:** I agree. Microsoft could control the whole workflow. Fortunately, it's not just Apple. It's Apple on the desktop side, but it's also folks like SAP, Sun and EMC and others on the infrastructure side. Because if it was just a Microsoft world, there is no room for Adobe. But people don't want to be locked into a certain workflow -- whether it's a desktop workflow or an IT workflow. They don't want to be locked into any one workflow.

Microsoft works well if you own their servers and their desktop and their handhelds. Then they have a great story. It begins to fall apart when you add in a Java-based server, a Linux desktop or a Mac desktop and so on. That's where Adobe comes into play.

**Knowledge@Wharton:** When you talk about your engagement platform, how important will digital rights management be to the platform? Will that be something you will be providing as an essential core service?

**Chizen:** We will, at least today, as it relates to documents. Where it gets messy is in other media types, especially media types that impact the consumer. It's a pretty messy environment, and I'm not sure Adobe

will be able to add anything to clean up that mess, so we might be better off just staying out and being [neutral].

**Knowledge@Wharton:** We have been talking about next-generation *client* environments, both on the desktop and the mobile platforms. There's a lot of talk about software as service in a web-top clientless environment. You have experimented with this with your Create PDF Online service, but haven't gone into it in the way that companies like Salesforce.com have. What do you see as the future and, in particular, does Adobe have plans to do more in the software as services space?

**Chizen:** We will do more software as services. With Breeze's real-time collaboration we already do hosting. We will continue with CreatePDF Online. And you will see us begin to experiment with other services, either directly or through aggregators like Salesforce.com. There are probably things we could add to their AppExchange that could be of interest to others.

You can expect us to do more in areas where Adobe has strength. It will also depend on broadband [deployment] and the needs of the users. If I look at products like a Photoshop or an Illustrator or an InDesign -- given today's broadband speeds -- I don't think that software as a service makes sense. But there are some applications where it would make sense that fall into Adobe's mission.

### The Future: Adobe Everywhere?

**Knowledge@Wharton:** We started off talking about what your priorities were for the next six months or so, and we have gone a little further out now. Let's jump further ahead. Acrobat itself is about twelve and a half years old. Netscape's IPO was just a little more than 10 years ago. Where do you think we will be 10 years from now? What will the computing platform look like and how is Adobe positioned?

**Chizen:** If we execute appropriately we will be the engagement platform, or the layer, on top of anything that has an LCD display, any computing device -- everything from a refrigerator to an automobile to a video game to a computer to a mobile phone.

Our software [will be] delivered as a service, either charging the consumer directly, the network provider directly or using an advertising model.

I believe Adobe's focus will continue to be on those applications that help people and organizations in areas where the presentation of the information makes a difference. We have always been about helping people with their ideas, and sharing their ideas and information in a visual, graphical, reliable way. That will be true 10 years from now.

If I think about Adobe, we have revolutionized the world -- and when I say "Adobe" today, that's inclusive of Macromedia. Just about everything you look at -- a label, a movie you go to, a video on the web, a billboard, a sign when you get off the airplane -- was probably touched by a piece of Adobe software.

By having that engagement platform we could do more of this into the future. [We can] make our customers' lives easier and make the user's experience that much more interesting. All of us are being bombarded with information. I want a great experience, even if I am filling out a boring mortgage application or a tax form. I want a great experience. Ten years from now we will be providing that.