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Change in the Procurement of Enterprise Network Services: Are We Moving Down the Track or Jumping It?

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Whatever else you can say about the Great Recession of 2007-2009, it has had a major effect on network services procurement. Last month Tom Nolle posted a typically insightful piece on *No Jitter* entitled "How Light is the End of the Tunnel for Enterprise Spending?" After reporting the results of an enterprise survey showing that 80% of users now think there has been a significant, recession-driven paradigm shift in IT procurement, he closed with this:

> Vendors usually try to instill a sense of change and thus a need for modernization. Enterprises in 2009 say that their vendors are trying to stay the course in technology while they, the buyers, are trying to look at new options … Enterprises are seeing a whole new technology world out there, and they think their suppliers are missing that shift. If that's true, then 2010 might bring some very profound changes in the market landscape.

A "paradigm shift" is a discontinuity in behavior accompanied by a change in world view. Labels aside, there is always a legitimate question about whether a major change is something new and different or just the acceleration of an existing trend. Economists call this the difference between moving along the demand curve and shifting that curve, and the line between them can be fuzzy at times. There is not much that's ***really*** new under the sun, so if you look closely enough even the most novel technology or behavior has antecedents.

But whatever you want to call it, there is unquestionably a big shift in enterprise telecom procurement. Evolution driven by changes in technology and user needs has accelerated or morphed in the face of pressure to cut costs without reducing the volume or quality of service.

Here are some ways this evolution is changing how enterprise telecom managers do their jobs.

Wireless Services

Wireless is something like 40% of the enterprise telecom budget, and growing fast. Many companies don't know this because they pay for employee cell phones through T&M and don't manage the expense well, if at all. But since that's where the money is, in an era of tight budgets attention is being paid.

First, we are seeing exponentially more aggressive pursuit of low hanging fruit. You can knock 80% off of the cost of international calls that originate in the US by funneling the traffic through services like Google Voice. And if you integrate mobile devices and the office wireline network, wireless calls placed in the office go out over the wireline system, where they are basically free.

Second, companies are taking heightened aim at waste, fraud and abuse; saving money; and plugging major security holes through exponentially tighter management of wireless devices paid for by the company. If the enterprise is paying for it, only approved apps should be loaded on it, traffic will be monitored and if the device is lost or stolen it can be remotely activated to wipe it clean.

Third, some companies are simply getting *really* tough. At least one household-name company we work with has just eliminated company reimbursement for employee cell phones – it's a business tool like a tie or a briefcase, and the company doesn't pay for those so it believes it shouldn't pay for this one. We don't think this will spread too far, but it will absolutely happen at organizations *in extremis* or with "focused" leadership. And it has interesting implications. In one recent survey, a clear majority of BlackBerry users said they "chose" their devices because they were the ones their employers gave them. If the boss isn't paying, different devices will become popular.

Wireline Services

Despite their frequent protestations to the contrary, the ILECs control more than 90% of the market – and therefore have a virtual monopoly – for the T-1 and T-3 access pipes that have been essential to enterprise private line, frame relay and ATM networks for the last 25 years (and now MPLS networks). You may see the names of other companies in that marketplace, but at least with respect to dedicated access for the most party they're only re-selling the ILECs' pipes. As a result those services have been and remain overpriced. They are now facing their first serious challenge from Ethernet and wireless broadband (4G mobile, either WiMax or LTE) access. The economics are compelling – we bought a 10-Mb Ethernet access line *and* a backup T-1 a few months ago for the same price we had been paying for a T-1 alone. Due to bandwidth demands, the Great Recession and ILEC refusals to "cannibalize" pricing on their installed base, this is going to spread very fast. (Although recent FCC action de-regulating the ILEC pipes that Ethernet providers need to provide service will not help.)

Second, wireline services/revenue have not been a bright spot for the big carriers, mostly because of residential access line shrinkage as those customers migrate to wireless or drop second lines that were being used for Internet access. They've been trying to make up the lost revenue by packaging transport and router management and selling the bundle at a premium as managed services. But providing remote router management is not actually very expensive and, aided and abetted by unrelenting customer pressure, we anticipate the rapid commoditization of managed services followed by a most welcome price collapse.

The Purchase and Sale of Network Services

Change is afoot in the purchase and sale of network services as well. First, the economy is interacting with Moore's law to push – indeed accelerate -- product substitutions. Stuff we have been talking about for a decade is rapidly moving from the fringes to the mainstream.

One example is the replacement of non-essential travel with video conferencing. Another is the growth of teleworking. A third is the replacement of powerful and relatively expensive desktops with virtual desktops working off of a cloud. A fourth is the move to offshore rather than onshore services in areas like customer support and writing code.

Many of these trends (*e.g.,* offshoring) have been under way for years; others (*e.g.,* widely used video conferencing) have been "coming next year" for decades, but the former are accelerating and the latter are actually arriving due to a perfect storm of cost pressure, technology advances and the growing availability of cheap "middle miles" bandwidth.

Second, the recession has also accelerated a long-term trend (driven by technology and the economic dominance of data networks since about 1995) to replace telecom staffs with IT

network services staffs. If you are cutting headcount, the voice people (those who are left) and their managers go first – voice is just an application now anyway.

A similar trend, also accelerated by the downturn, is the replacement of IT/technical folks with procurement staffs at the center of the network services purchasing. That has several effects, but perhaps the most important are the ascendance of product standardization (engineers want the latest and coolest; accountants want off-the-shelf apples that they can compare easily to other off-the-shelf apples) and the acceleration of the cost focus described above.

Third, the same forces are encouraging increased use of vendors other than the usual, gigantic telecom suspects. This waxes and wanes; it's waxing right now.

After almost a decade of consolidation, several second-tier carriers – XO, Level 3, tw telecom, Global Crossing, PAETEC – have annual revenues approaching or exceeding $1 billion. They have been quicker than the RBOCs to offer services like wide-area Ethernet and "all the minutes you can put through a pipe" pricing. That, combined with the commoditization of transport services (other than MPLS and managed services) positions them to grow their enterprise business quickly in an era when cost is king.

Conferencing vendors (BT Conferencing, Premiere, WebEx) are widening their niches, and cable companies (like Comcast) are increasingly active in the telework market.

Finally, the carriers – the record companies of connectivity – will respond to all of this with redoubled efforts to eliminate competition and still more surcharges and other (uncontrollable) fees.

Offering less expensive alternatives to core products with huge, entrenched sales staffs that are highly profitable because that is the path to long run success makes eminent sense, but it is hardly ever a way to win intracorporate battles. Hunkering down can succeed in the short term (witness the 100% returns that the RBOCs earn on T-1 and T-3 access) but in the long run their tactics will just accelerate migration to alternative technologies and providers. I've written elsewhere about the tactics carriers are using to get more revenue from their customers (http://whitepapers.thevoicereport.com/ViewSurvey.aspx?survey=56&whitepaper_id=60); introducing new services at price points that incent folks to buy doesn't make the top 10.

Conclusion

So do we have a "paradigm shift" or are we just seeing trends that have been several years in the making speed up since the bottom fell out of the economy (and IT budgets)? In other words, are we jumping the rails or just traveling a bit faster down the track?

For what it's worth, I don't think any single development listed above, in and of itself, represents a fundamental change. But when they are viewed together, it is pretty clear that we are not just getting where we were already headed faster; we are moving in a different direction and will end up in a different place.

Whatever you call that, it is a big change in the way network services are viewed and purchased, with implications for everyone in the industry.