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UCaaS - The Business Case for Service Providers: Build, Hire or Partner?

A PCCW Global and Cavell white paper

PCCW Global®

Unified Communications-as-a-Service
The Business Case for Service Providers

Build, partner or acquire?

White Paper commissioned by:

Author: Marc de Marcillac, "The Cavell Group"

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Introduction

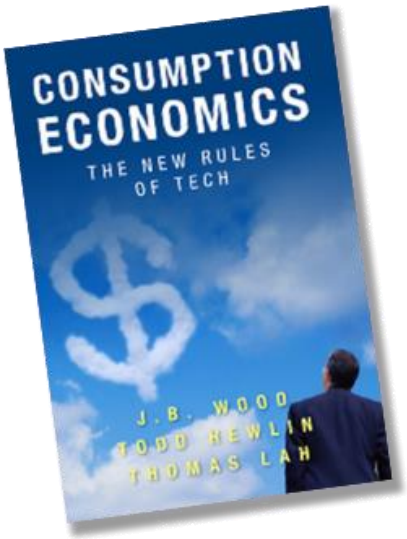
The ICT industry is undergoing the greatest turmoil in its history as the market turns away from purchasing equipment to paying for a service.

Driven by cloud computing, managed services and consumer technology, the consumption model for technology has been turned on its head. The Technology Services Industry Association (TSIA) book "Consumption Economics: The New Rules of Tech" describes the shift in purchasing power and risk from vendors to customers[1].

> *"If you're a tech company, the **most dramatic effect of megatrends like cloud computing**, managed services, and the rise of consumer technology won't be felt in your company's product line. The true **disruption will be to your business model**. Future customers **won't want to pay you high prices out of big "CapEx" budgets** any more. They will **expect lower "cloud" prices paid from "OpEx" budgets** only when and if they successfully consume the business value of your products"*[2]

The TSIA has identified several behavioural shifts in the relationship between tech vendors and consumers of their technology, including:

1. The risk in the purchase decision will shift from the customer toward the supplier
2. Complexity's long and illustrious reign will end. Simplicity will be king
3. Cloud customer aggregators will shrink the direct market for tech infrastructure providers
4. Big changes will come to the channel ecosystem.
5. IT departments will "get out of the way" of end users.



The process of selling tech will also change. The budget-owning buyer will shift from IT to business. Addressable budgets will be Opex, not Capex. And successful selling strategies will require business expertise, not technical expertise.

But what's not so good for technology vendors has created a new opportunity for Service Providers to become part of the technology solution value chain: they are in a unique position to build and deliver ICT "as-a-Service" – and one of the key addressable solutions is Unified Communications: "UCaaS".

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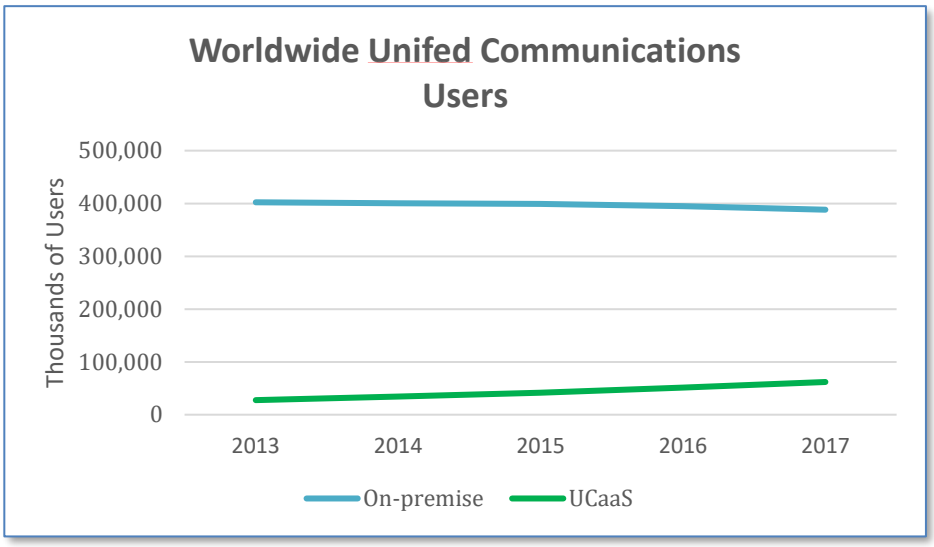
[1] http://info.tsia.com/consumption-economics-abridged; https://www.youtube.com/watch?v=q7s0-rB4LQE

[2] Point B Inc (Nov. 2011) J.B. Wood, Todd Hewlin, Thomas Lah, ISBN-10: 0984213031

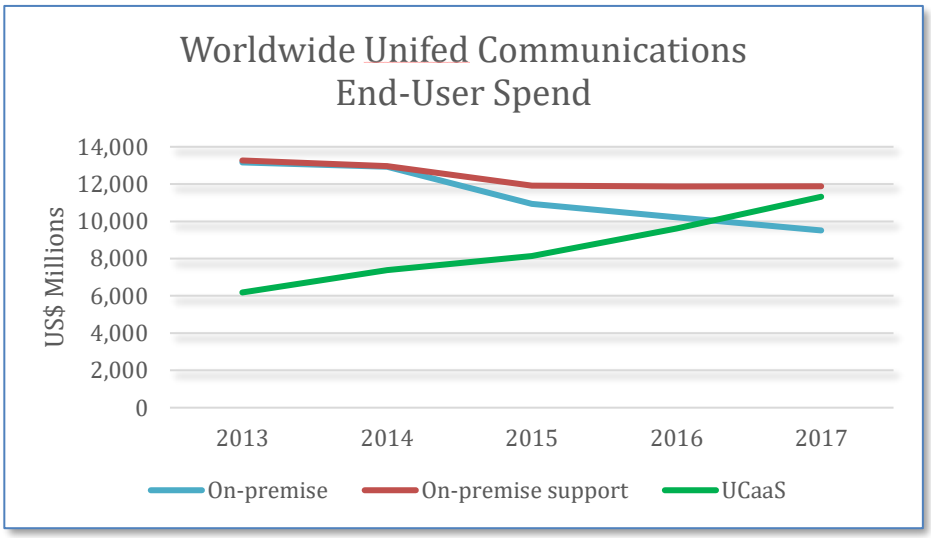
The Market Demand for UCaaS

Figure 1[3]



UCaaS, also known as Cloud Communications refers to a service model where Service Providers deliver telephony and collaboration applications or services, generally over the global IP network. This type of service is still in its infancy with a mere 41.8 Million users worldwide in 2016, compared with 399.2 Million legacy on-premise telephone seats (PBX, etc.), but the trend is clear: Compound Annual Growth Rates (CAGR) for UCaaS seats 2015-2020 is 21%, whereas on-premise seats are forecast to decline by -2.7% CAGR[4] (see Figure 1).

Figure 2[5]



[3] Source: Gartner
[4] Source: Gartner Forecast: Unified Communications, Worldwide, 4Q16 Update.
[5] Source: Gartner

However, when looking at the spend in these markets, the picture could not be more different: whereas the global market for on-premise-based telephony was worth US$10.2 Billion in 2016, UCaaS was worth US$9.6 Billion – the value of the on-premise telephony market is forecast to decline by 8.2% CAGR 2015-2020, the value of the UCaaS market is forecast to grow at 16.9% CAGR in the same period[6] (see Figure 2).

In addition, these market dynamics are global, with equivalent market opportunity and penetration in all geographic theatres world-wide.

The conclusion is clear: market spend is shifting rapidly from on-legacy premise telephony to UCaaS. Yet the majority (86%) of UC seats are still on-premise, creating a very large opportunity to convert legacy telephony to UCaaS over the coming years.

There is therefore a very large market opportunity to sell UCaaS – but how can Service Providers enter this market and drive scale and profitability with minimal risk? The rest of this white paper will examine the pros and cons of these options and identify criteria to help choose the right one for your organization.

Entering the UCaaS Market: the fundamental Operating Models

There are three fundamental models for Service Providers to enter the UCaaS Market:

1. Build and operate a UCaaS technology solution that meets their precise requirements
2. Partner (two sub-options) with:
    a. A technology vendor who offers an as a Service solution
    or
    b. Another Service Provider who operates an as-a-Service solution
3. Acquire another Service Provider who already has UCaaS

Each of these options have different pros and cons which will be examined below. There are however key criteria which need to be considered.

Time to market

Delay in addressing latent market opportunities loses revenue and leaves the market open to alternative solutions. This is not just about technology deployment, it's also marketing and sales readiness.

Customer segmentation

Not all Cloud Communications platforms can address all customer size segments, driving the need for a multi-platform strategy.

[6] Source: Gartner Forecast: Unified Communications, Worldwide, 4Q16 Update.

Differentiation
A wide range of on premise and Cloud Communications solutions are available – how to create a unique value proposition in the market?

Cost & margin
Different choices will have impact on Capex/Opex models and margin sharing.

Go-to-Market skills & resources
Selling Cloud Communications can be a more complex sale, or require new digital marketing assets and capabilities, and a more sophisticated and longer process than selling simple connectivity.

Whilst these key criteria need to be considered, the ultimate choice should be driven in a strategic context, and by pragmatism.

The Strategic Context

Firstly, a mixed strategy should be considered: one in which a variety of models is used to address different customer segments, or to create a roadmap in which the model changes over time. Some examples of Service Providers who have done this successfully are listed below in "Approaches adopted by other Service Providers" on page 7.

Choosing a wholesale or white label capability means that the provider doesn't have to "go it alone" – and can learn from the experience of their supplier, especially if entering the UCaaS market is too risky or too onerous. Again, examples are listed below.

Experience shows that platform choice is of itself only one part of a complex puzzle. Other areas requiring investment include billing and operational capabilities, regulatory compliance, local language support and localisation, etc.

From a strategic perspective, entering the UCaaS market is a big step for many Service Providers: they are now selling and delivering "value added" services to end-users, and not network connectivity to an ICT Department. Therefore, before making decisions about a UCaaS operating model, there needs to be a clear strategy around the value the Service Provider wants to offer, and how to offer it to the market.

Strategic topics should include:

- The internal skill pool of the organisation
- The fiscal imperatives of the company
- Appetite for risk, and ability to manage it
- Appetite to support SMEs and multinational Enterprises.

A long-term view also needs to be maintained, as selling UCaaS is not a transaction. A roadmap approach, in which smaller and less risky steps to deployment can be taken when

entering the market, should be considered. As an example, partnering can be an initial step for rapid go-to-market, and then followed sometime later by an internal build.

Approaches adopted by other Service Providers

A variety of hybrid approaches has been taken by significant Service Providers when entering the UCaaS market. Notable examples include Verizon in the US who invested in a vendor-based offering, but when they entered the non-US market chose to build their own platform. In the UK, Daisy's off-the-shelf vendor platform was discarded and they moved to white labelling a BT Wholesale UCaaS service – even though they compete with BT.

A large US Service Provider has implemented an off-the-shelf vendor platform in the US, but internationally has chosen to white label UCaaS from PCCW Global. And BT Wholesale made an initial choice of a Hipcom (later acquired by Broadsoft) UCaaS system to accelerate its go-to-market, but has now invested in developing their own platform in-house.

Finally, it is worth mentioning Microsoft and its market disruption: initially selling Skype for Business through Service Providers, it is now also selling its Cloud PBX platform (now relabelled "Teams") direct to Enterprises, in competition with their own channel.

The pros and cons of each model are examined below.

Model 1: Build and operate your own UCaaS technology solution

Positives

- A Bespoke solution that fits market and SP requirements perfectly
- A unique proprietary USP and feature set
- Total Control: The SP can manage and develop features to match its needs
- The uniqueness of the solution makes for a strong marketing message

Negatives

- Complexity and risk: software development is not a core SP discipline, and carries technical and commercial risk
- Time to market is stretched by long development cycles, and risks of overrun
- Maintenance means an ongoing drain on resources
- Significant resources will be consumed on support and development
- Go-to-market: without the support of a vendor, the SP will need to create its own GTM collateral, processes and resources

Model 2A: Partner with a cloud provider / technology vendor who offers an as-a-Service solution

Positives

- Time-to-market will be shorter as the vendor will offer a virtually off the shelf solution
- Pressure on resources will be reduced as key resources are effectively "outsourced" to the vendor
- The vendor takes responsibility for support – normally with SLAs
- The vendor is responsible for keeping the solution on latest release, with latest features
- Go-to-market support: The vendor will normally provide free or fee GTM collateral, processes and resources

Negatives

- The solution comes from a technology vendor, and the focus will be on their technology, not operating a "service"
- The SP will be tied to a vendor and unable to change platform with ease to pick "best of breed" solutions
- The financial model will be less flexible as the vendor will impose terms, and there is risk of margin squeeze, or stacking
- Vendors' approach is technology/transaction-based, SPs are relationship-based. Vendors often do not provide the full solution (e.g. back-office OSS/BSS, regulatory, numbering, etc.)

Option 2B: Partner with another Service Provider who operates an as-a-Service solution

Positives

- Accelerated time to market as the SP will be aligned to enable not just technology scale, but also sales & marketing
- Pressure on resources will be reduced as key resources are effectively "outsourced"
- The SP takes responsibility for support – normally with SLAs
- Service Providers understand each other and will use business and support models that are compatible
- Global SPs will often offer other important complementary services (Integrated OSS/BSS tools, MPLS, Security, Fraud detection, handsets, regulatory cover, on the ground support, etc.)

Negatives

- The route to technical support will be less direct
- With no direct vendor relationship, SPs may have less influence over feature development
- The Service Provider will impose terms, and there is risk of margin squeeze, or stacking
- In some markets, this option could mean partnering with a competitor

Option 3: Acquire another Service Provider

Positives

- Market presence: the target SP will already be present in the market, with its own GTM collateral, processes and resources
- Existing revenues: The target SP will already have a revenue stream that makes the acquisition costs easier to swallow
- The target SP will already have subscriber base that is ready for cross/up-selling

Negatives

- The world of Mergers and Acquisitions is not a core competency of most SPs
- M&A transactions are complex, lengthy and often fail, sometimes for causes out of the acquirers control
- Integration of systems, processes or platforms can be very onerous
- Financial model: swallowing an acquisition can be a difficult financial activity, beset by financial and regulatory burdens

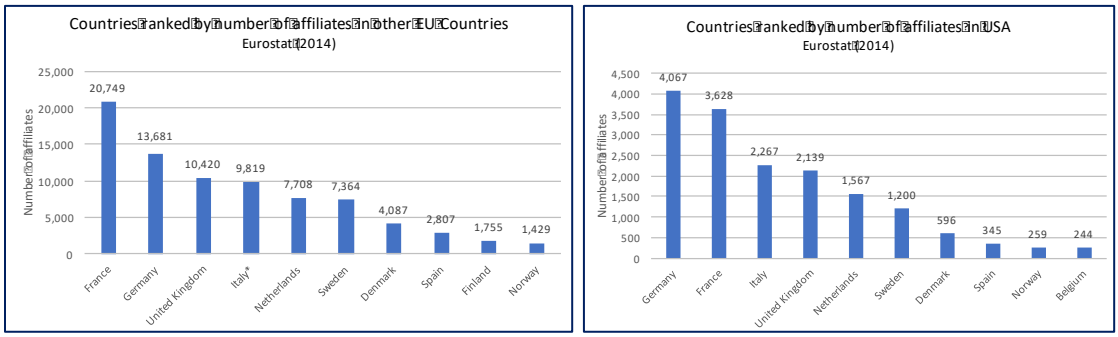
Differentiation to compete

Other market dynamics can help differentiate and drive more valuable UCaaS value propositions:

1. Serving multinational customers with a global solution
2. Verticalising the offer
3. Offering a richer roadmap of features.

Serving multinational customers with a global solution

Figure 3[7]



Mid-market and large companies are increasingly likely to have foreign subsidiaries and seek to source UC from a single provider: international reach is key to address these

[7] Source: Cavell

markets. Figure 3 shows European countries ranked by the number of affiliates in other EU countries, as well as European countries with the number of affiliates they have in the USA.[8]

Cavell research shows that 60% of UK Service Providers believe that the importance for offering an international service to their customers will increase in the next 12 months, yet there are relatively few providers who can offer SME international services effectively.

Offering international services is therefore potentially a good way to differentiate and make a UCaaS offer more attractive.

Verticalisation

Figure 4[9]

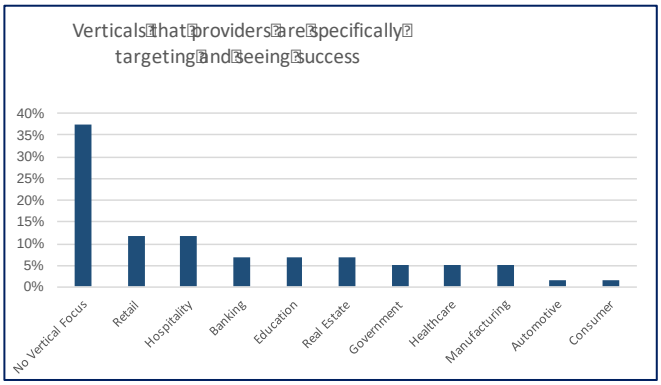


Figure 4 shows that over a third of UC offers are "vanilla" with no verticalisation. However, this is one way to enter the market with a ready-made UCaaS differentiator, as different verticals have distinct needs, currently served by integrators but not cloud providers.

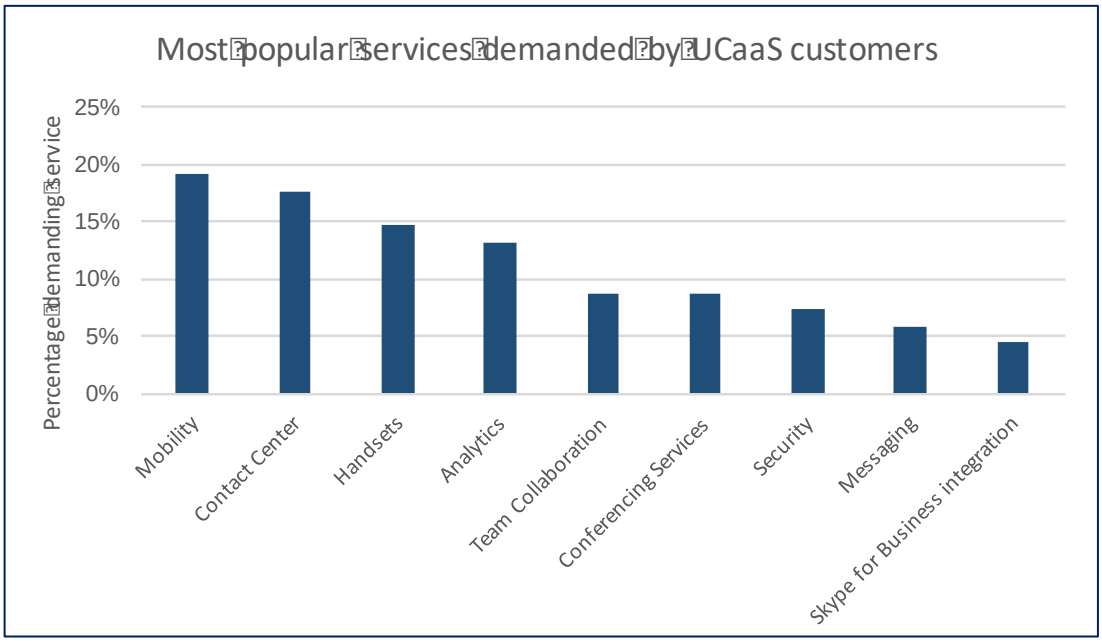
There is however no "stand out" vertical that all SPs are having success targeting. Retail & hospitality are usually easy to penetrate and differentiate, and financial services offer rich pickings, but have very specific dynamics around compliance and security.

[8] Foreign affiliate in the framework of outward FATS is an enterprise or branch not resident in the compiling country over which an institutional unit resident in the compiling country has direct or indirect control.

[9] Source: Cavell

Offering a richer roadmap of features

Figure 5[10]



Most UCaaS systems offer relatively simple features that are simple extensions to traditional “dial tone” telephony.

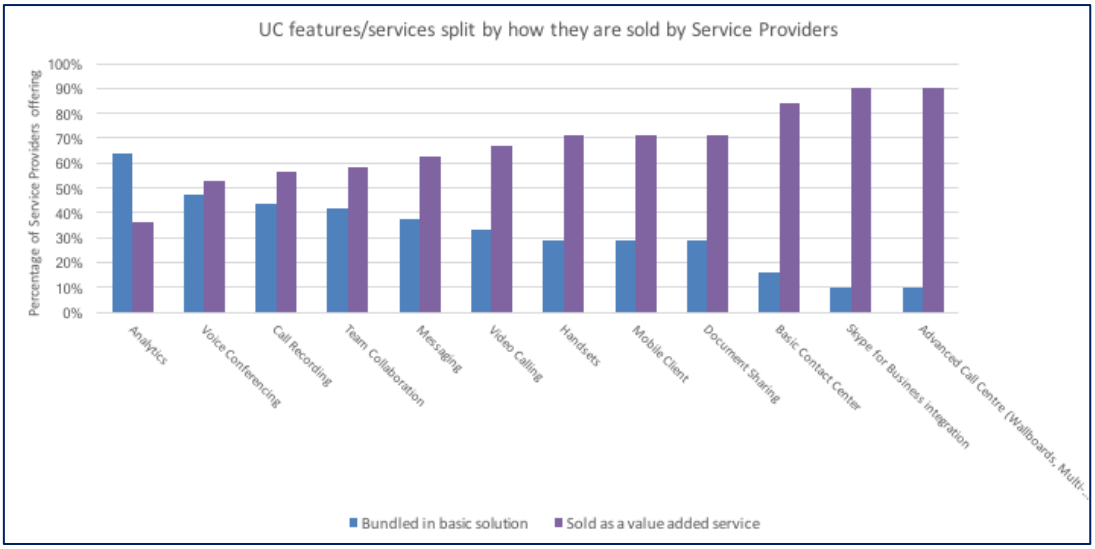
However, the market is becoming increasingly sophisticated: customers who might have been reluctant to put time and effort into integrating new functions into an on-premise PABX or UC system, are now able to consume such features for no extra effort or risk, as part of a cloud UCaaS solution.

Mobility and fixed/mobile integration is a current trend of interest as well as more sophisticated collaboration solutions such as contact centre and collaboration (chat, video, etc).

An alternative or complementary strategy is to add chargeable features to a base UCaaS solution as part of a roadmap. This can leverage the additional value to increase ARPU over time, and to keep ahead of the competition. Figure 6 shows the feature/service split depending on when they are bundled at no extra charge, or sold as a value-added service by the Service Provider.

[10] Source: Cavell

Figure 6[11]



Summary

In this White Paper, we have looked at the dynamics of the UCaaS market, and the opportunities for Service Providers.

Market research data shows that the opportunity is large and growing, and that penetration is low. UCaaS offers Service Providers an opportunity to move "up the value stack" with value added services that provide quantifiable business value to their customers, and enriches the customer relationship. UCaaS is therefore a key opportunity for SPs, as the UC market is shifting to the cloud, and offers an opportunity to increase ARPU from existing subscribers, and potential to drive new subscribers. It also allows a richer feature set to drive more intimacy with the customer and "stickier" subscriber relationships.

However, success in taking UCaaS to market does create new challenges. The technical and go-to-market effort is riskier and more complex, and the customer intimacy and sophistication of the solution makes customer support more onerous.

Deciding on the right operating model is therefore critical: to go it alone by building your own solution, partnering with a vendor or a Service Provider with an existing system, or acquiring another Service Provider. These models are not however mutually exclusive, and other Service providers have taken hybrid routes in which they offer different models to different market segments, or move from one model to another depending on their own readiness and market dynamics.

[11] Source: Cavell

nTwine Global UCaaS from PCCW Global

Your clients want to grow their global business? Our UCaaS infrastructure is already there.

Serving the international UCaaS needs of mid-market and larger organisations is proving to be very difficult for many service providers. Large businesses that move their communications infrastructure to the cloud cannot be limited by regional or national boundaries.

PCCW Global, the international operating division of HKT, Hong Kong's premier telecommunications service provider, has a long history in serving global organisations with best in class communications services. We operate our own resilient global fibre network spanning over 3,000 cities and 150 countries and have bi-lateral relationships in place with 200 operators around the globe.

Our nTwine solution is a feature rich UCaaS platform which has been deployed across the globe. It is a complete, integrated, easy to use solution for voice, video and collaboration across any device, any location. Delivered via the Cloud, the service helps organisations improve productivity, reduce costs and completely transform their communications without the need to make large upfront investments.

For service providers wanting to deliver their own UCaaS service it providers a completely integrated solution for deploying unified communications including an automated back office to build, deliver, manage and charge for service offerings.

Plug in to our global nTwine service and instantly serve your International customers without the hassle and the cost of building your own platform and support infrastructure. nTwine is a global platform built on our highly-resilient data network and centres, that are strategically located across the globe to ensure the highest resiliency, adherence to country-specific data sovereignty requirements and advanced security. Through a single interface we can support all options of the 'build', 'partner'and 'extend'models to serve all your domestic and international UC requirements:

- Full suite of communication and collaboration tools
- Complete solution to sell, deliver, manage and invoice
- Online portal for simple provisioning and management
- Global MPLS network and data centres – 150 countries
- Local delivery and support
- Local numbers, porting and regulatory compliance
- Domestic and international voice termination
- Consolidated billing
- 24/7 support.

For more information contact us at: uc@pccwglobal.com.