

RESPONSE TO ISSUES STATEMENT

CCIA response to public cloud infrastructure services market investigation issues statement

Background

The Computer & Communications Industry Association is a not for profit international tech trade association, which has multiple members competing vigorously in the cloud sector. Those members have diverse views on the issues raised in the issues statement for the Cloud Services Market Investigation.

Cloud services provide huge value to business customers, with particular benefits in terms of supporting competition by allowing smaller businesses to enter new markets, access cutting-edge IT services and infrastructure, thereby grow and face fewer fixed costs as they scale. Establishing these services and the quality of service, security and support enterprise and public sector customers expect in order for public cloud to provide a credible alternative to on-premises solutions is a major and ongoing effort for the companies involved. It is important to maintain the incentive for such investment.

Surveys of Cloud customers suggest that the sector is healthy overall, as often sophisticated existing Cloud customers and opportunities to attract customers coming into the sector create an incentive for cloud providers to compete with attractive prices, service quality and innovation.

- 71% of businesses use two or more cloud infrastructure providers (Public First, Q19)
- The most common reasons why businesses chose a certain cloud service provider were service quality (32%), value for money (29%), proposed level of security (24%) (Public First Q20)

To the extent that some customers still find it difficult to switch, the right intuition is therefore that problems are most likely where there are legacy constraints. The most important barrier to switching and multi-cloud is software licensing constraints artificially created by legacy providers, as assessed in Ofcom's cloud market study report (chapter 9). These constraints result from customers' pre-existing relationships with enterprise software providers who push customers towards their own nascent cloud services through restrictive licensing practices. As a result these will reflect decision-making in (i) less-competitive enterprise software environments; where (ii) customer decisions are made without an awareness this would restrict their future choices as cloud customers.

Theories of harm

As noted above, of the four hypotheses one (restrictive software licensing) seems by far the easiest to reconcile with customer experience in the sector.



Theory of harm 1: Customers often find workarounds to technical barriers that can be inherent to the technology, or a natural consequence of vigorous competition. Widely available cloud-based open standards and software are designed in a way that preserve safety, privacy, and security. As a result, cloud-enabled organisations can flexibly move workloads between different providers and the number of tools required to support cloud environments is reduced, which ultimately supports integration of existing business systems with the cloud. In a survey considering technical limitations to switching,

- 26% indicated they had switched cloud infrastructure provider in the past (Public First
- 51% reported that it was likely they would change one of their main cloud infrastructure providers in the next few years (Public First O35)
- Of those that did not report they would switch, 80% reported it was because they were satisfied with their current main cloud infrastructure provider(s), against 11% that thought it would be too complicated and 8% that thought it would be too expensive (Public First Q36)
- 62% reported it would be easy to add and integrate an additional cloud infrastructure provider in their current setup against 15% that thought it would be difficult (Public First 055)
- 56% thought it was likely they would do so (Public First Q56)
- 29% of those who reported switching cloud infrastructure providers in the past switched to an on-premises solution (Public First Q31)

Theory of harm 2: In its cloud market study, Ofcom adopted a broad definition of egress fees, which would include network service costs, for example. The export of complex and extensive workloads from a given cloud provider to any other IT environment, including on-premise, involves operational costs for any cloud vendor, as also noted by the 2020 Switching Cloud Providers and Porting Data's (SWIPO) portability code. In particular, the code recognises the need to allow providers of data processing services to charge customers for network charges, and associated costs, incurred.

To the extent that the CMA is intervening in a fundamentally competitive sector, it could mean that providers, which are no longer able to recover the operational costs of switching, are less able to support switching customers, raising the internal financial or non-financial costs of switching - which are often greater than external costs. This could result in unintended negative effects on competition.

- 79% of those switching reported using dedicated features that support switching provided by their cloud infrastructure provider (Public First Q32)
- Of those that did not, the most common reason (46%) was that the features were not helpful for their business, although others reported those features were not offered (40%) or were too expensive (31%) (Public First Q33)
- Of those that had switched, 54% reported that the majority or vast majority of costs in switching cloud provider were internal and a further 25% reported that internal and external costs were around equal (Public First Q34)
- Those proportions are similar in terms of the expectations of those considering switching (Public First Q37)



Theory of harm 3: Committed spend discounts can provide a mutual benefit to the extent that they allow Cloud firms making large investments in infrastructure to increase the utilisation of those assets, allowing them to improve the overall proposition to their customers. The current outcome is that such discounts are valued by customers that use them, but many do not use them, suggesting that they are not essential to receiving good value. This seems like a healthy outcome that could easily be worsened by regulatory intervention.

- Businesses were around evenly split, 47% of businesses reported receiving a committed spend discount and 45% not (Public First Q78)
- 45% of those receiving such a discount reported that it was important to their company and 44% reported that it was very important (Public First Q79)
- 78% consider the practice somewhat or very positive (Public First Q77)

Theory of harm 4: Software licensing restrictions, on the other hand, often relate to decisions that were made by companies choosing (to the extent practical alternatives were available) between different providers of productivity or enterprise software, without being able to anticipate that this would be used as a rationale to limit their choices in the cloud infrastructure sector. There are strong grounds for intervening to ensure that software licensing does not create customer lock-in, impair the ability of on-premise productivity and enterprise software customers to migrate into the cloud and choose freely between different IaaS providers.

- Of IaaS customers who have considered switching, 40% said existing licensing terms prohibit their companies from taking on-premise licences to another vendor (Savanta)
- One of the biggest reasons IaaS customers reported choosing their provider was because of discounts due to existing software licences (42%) with 48% stating their existing relationship with Microsoft would drive purchasing decisions despite expecting it would be a more expensive option (Savanta)

Sector outcomes: prices and profitability

The CMA will need to consider a range of factors that make the cloud sector distinctive in assessing prices and profitability. These include, but are by no means limited to:

- High fixed costs compared to marginal costs across the industry might mean apparently large mark ups, despite multiple firms competing and innovating.
- Rates of return will be hard to assess with extensive intangible assets and should not be expected to always equal the WACC.
- To the extent product turnover / innovation is materially higher than in other sectors (as the role of Cloud providers is to bring the latest innovations to a broad range of customers) that could affect technical elements in the calculations.



Given these and other complications, and given evidence of competition between providers, unless this analysis is conducted with enormous care it may obscure more than it reveals.

Potential remedies

CCIA understands that the CMA is outlining a broad range of potential remedies at this stage. However, to the extent that this investigation might in itself affect incentives for cloud providers, it should move as soon as possible to rule out interventions that seem to fail the principle of proportionality versus the technical barriers described in the theories of harm.

Prolonged uncertainty could affect investment decisions that depend on long-term policy stability and have material wider economic importance. For example, some of the cross-cutting interventions such as structural, divestiture measures or price caps seem clearly inappropriate and the CMA could reassure the sector by making that clear as soon as possible that these are unlikely to be its preferred options.

Notes

"Public First" refers to a survey by Public First, the fieldwork for which ran from 25 May to 1 June 2023 and reached a sample of 1001 UK senior business decision makers with an online survey.

"Savanta" refers to a survey of 1,241 IT decision-makers across five countries (UK, France, Germany, Netherlands and Spain)