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Response to Updated Issues Statement and Working Papers – CMA Cloud Services Investigation

Introduction

Thank you for extending the deadline for stakeholder responses to the CMA's Cloud Services investigation. This paper is our response to the CMA's updated Issues Statement and related working papers – particularly the working paper relating to Committed Spend discounts. We appreciate the CMA's ongoing examination of this critical sector and offer the following observations.

Conflating Data Sovereignty and Data Residency Compounds Market Concentration.

The Competitive Landscape working paper makes several observations that data sovereignty requirements will, for some customers, be a factor that drives a customer's choice of cloud provider – in particular a cloud provider that can provide a local cloud infrastructure. Notably, paragraph 2.53 (c) states:

"Data sovereignty requirements: the majority of customers considered compliance with data localisation, privacy and protection regulations to be very important and one considered it to be important. Some customers said that almost all providers can support customers' usual requirements around data protection and sovereignty".

The primary research undertaken by Jigsaw did ask respondents whether data sovereignty was a factor driving a choice of cloud provider. And clearly for some customers, it is.

However, Jigsaw did not define data sovereignty and CMA has, within the Competitive Landscape working paper, conflated data sovereignty with data residency. This is problematic:

- while data residency focuses on the physical location of data storage, data sovereignty refers to the legal frameworks governing the data. This distinction is crucial for understanding the impact of cloud services on data control;
- this distinction is largely ignored by the hyperscale cloud providers. As the world destabilises, data sovereignty is becoming increasingly important on the global basis. Whilst both AWS and Microsoft claim to offer "sovereign" cloud services, they in are reality anything but given that neither of the hyperscalers or the customer data being processed and stored by the hyperscalers

(irrespective of location) can escape the legal framework and controls of both AWS and Microsoft's US HQs.

- The lack of rigour around differentiating between data sovereignty and data residency was brought into sharp relief recently when Microsoft recently admitted that it could **not** guarantee the data sovereignty of Police Scotland's data, despite Police Scotland's legal obligations to ensure this.

The CMA's cloud investigation is critically important and attracting international interest. With Jigsaw failing to define data sovereignty, the CMA has allowed the subjects of its investigation to continue to exploit the common misunderstandings between sovereignty and residency to their own advantage.

This then perpetuates the continued concentration of the market onto AWS and Microsoft. Smaller cloud providers, that can and do provide genuinely UK sovereign services are put at a severe disadvantage, facing yet another barrier to entry: the smoke and mirrors that is cloud service "sovereign wash".

The Impact of AI on the Cloud Market and Smaller Cloud Providers

The Updated Issues statement discusses the impact of AI on competition in cloud services, noting that it is still assessing whether this will provide fresh opportunity for smaller cloud service providers or whether AI will prove to be another barrier to entry.

If the CMA's current thinking that the necessity of significant infrastructure investment is a barrier to entry for smaller cloud providers proves to be true, it's highly unlikely that AI will provide opportunities for smaller cloud providers, given AI's dependence on cloud and massive compute resources.

The hyperscalers are actively competing in the AI market which will fuel the growth of their cloud infrastructures nd, consequently, their market share. Both the CMA and the European Commission are looking at the relationship between Microsoft and OpenAI, including OpenAI's exclusive use of the Azure platform. The consequences of the relationship could have significant ramifications for the ongoing competitiveness of both the AI and the cloud services markets.

As the AI and cloud services markets coalesce on just two providers, it will become increasingly difficult, if not impossible, for smaller cloud providers to secure the inward investment needed to develop the scale of infrastructure needed to compete in either of the markets.

Just one small example of this, is the UK Governments own incubator for artificial intelligence https://ai.gov.uk/ where open roles are regularly advertised requiring only AWS skills.

Committed Spend Discounts and Cloud Credits

The CMA's investigation into committed spend discounts and related Cloud Credits, is a positive step. Deeply discounted cloud services can have detrimental effects on competition and affordability.

Even if customers, according to the primary research, are happy to receive a discount, this does create more barriers to entry for smaller cloud providers: first because the prospective business is no longer portable, effectively locked up for a year-on-year term; and second, because smaller cloud providers cannot afford to offer the same level of discounts.

Cloud Credits are inhibiting fair and open competition

Limiting the investigation only to cloud credits that relate solely to committed spend discounts or negotiated alongside them is insufficient. If the CMA was to look at this aspect of cloud service business, it would see, as Ofcom noted in its final report that one of the hyperscalers primary objectives is to bring on new business, including (and especially) start-ups through inducements such as cloud credits. AWS activate is a case in point, as is Microsoft's Startup Founders Hub.

The level to which hyperscalers will go to win the business of new tech companies reached a new high (or low, depending on your point of view) with AWS's recent announcement that it is offering $500,000 worth of credits to startups wanting to build generative AI products. AWS is hoping to embed the next generation AI on AWS cloud, supported with AWS AI tooling.

It is very common for similar sized cloud credits to be offered to enterprise customers looking to adopt the cloud, often on a multi-year basis.

Smaller cloud providers simply cannot compete with these levels of discounts and are put at a severe disadvantage. Not only are they starved of the new customer win and associated revenue, but they also cannot get capital funding to provide the infrastructure needed to provide these high levels of free service. Hence they are again placed at a competitive disadvantage which will deepen and grow as the stakes get ever higher as the hyperscalers try to outcompete with others for the nascent cloud and AI markets.

The start-ups may be grateful for the opportunity, but face lock-in and dependence on hyperscale for their own survival.

Conclusion

We hope that the CMA will take our observations in the spirit in which they are intended, to help inform and widen the scope of the CMA's investigation. The CMA is commended for taking on a highly complex topic that is critically important to each and every one of us, as consumers and as taxpayers.

Lack of competition in the cloud market has profound and wide-reaching consequences – on the UK's security, resilience, digital capability, economy and, by no means least, the global environment.

We would be happy to discuss these views further if required.

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