CMA Submission

This submission is made by Blackbox Hosting, a UK-based private cloud hosting provider, in response to the CMA's Provisional Decision Report.

<u>About BlackBox</u>

1. BlackBox is based in London and supplies clients primarily in the UK and EU with private cloud services, PaaS and IaaS, enabling its clients to provide SaaS to their customers worldwide. Blackbox's services are a managed alternative to the public cloud offerings of AWS and Azure provided by Amazon and Microsoft. Its services including dedicated VPS Servers typically outperform and cost less than most public cloud solutions in the market.

2. BlackBox's own clients are some of the biggest software companies in the UK.

<u>Cloud Services Market</u>

3. BlackBox competes for customers both with other private cloud suppliers and also with the large public cloud providers (although the potential for this competition is being reduced by the pricing behaviour of AWS and Azure). We note that in para 21 of its Updated Issues Statement, the CMA found that private cloud services are "out of market constraints":

4. "*While some large customers of public cloud service may be able to react to a price increase by switching to private cloud or traditional IT, the evidence to date indicates that, even for large customers, any such switches would be unlikely due to the specific reasons they place workloads on public cloud*[1] *and the costs and time associated with doing so. Therefore, our emerging view is that traditional IT and private cloud should be considered as out-of-market constraints where applicable*."

5. We do not agree with the CMA's view that private and public cloud providers do not and cannot compete for customers, although we do agree that switching is artificially restrained by egress fees. It is technically possible even for large cloud customers to switch providers, and BlackBox offers technical support to do so. BlackBox's sales and marketing team targets AWS customers; a copy of a BlackBox marketing pitch is attached to this submission. BlackBox has already demonstrated that it can successfully support the very significant loads of its own clients' SaaS customers, as referred to in paragraph 2 above.

6. The primary benefits offered by BlackBox vs the public cloud are:
    - Lower costs
    - Greater security
    - Greater speed
    - A fully managed service

7. Actual and potential competition between the private cloud providers and AWS and Azure potentially can occur for SME customers, both for customers moving to the cloud for the first time, notably start-up ventures, and for existing cloud customers moving from one provider to another. However, Azure and AWS are distorting actual and potential competition in this market. In paragraph 21 of its original Issues Statement, the CMA referred to four theories of harm, but it did not include the practice of offering free credits to the start up market. We believe that AWS and Azure's behaviour in this regard is significantly harming competition in this customer segment and the purpose of this submission is to draw the CMA's attention to this in addition to the four theories, on which the CMA has already taken wide ranging evidence.

<u>Free Credits to start ups</u>.

8. The AWS Free Credits are set out here: [Get AWS Activate Credits - AWS Startups]. The CMA will note that AWS has partnered with venture capital and other investors in start up companies, and that the free credits that AWS offer are primarily aimed at start ups backed by these funds:

   "Credit eligibility is based on your startup funding stage and affiliation with Activate Providers, which are thousands of accelerators, angel investors, venture capital firms, and startup enabling organizations around the world. Review the requirements below to select the package that's right for your startup today. AWS Activate works with hundreds of accelerators, angel investors, seed/venture capital firms, and startup enabling organizations across the world, whom we call Activate Providers. Some notable providers include Sequoia, Andreessen Horowitz, Y Combinator, Greylock Partners, Carta, Brex, and more. Startups associated with an Activate Provider are able to apply for the Activate Portfolio package using the provider's organization ID."

9. In addition to the free credits, the AWS offer also includes third party offers: "Offers are exclusive savings available only to AWS Activate members. Take advantage of incredible discounts through our global network of relationships with dozens of software providers."

10. This is a further incentive for funders to become Activate Providers, and partner exclusively with AWS. Smaller, private cloud providers do not have the market power of AWS to be able to partner with third party software providers in the same way.

11. The effect of this is that start ups who are funded and backed by an Activate Provider will have no choice but to choose AWS as their cloud provider. This means that other cloud providers, public or private, are effectively locked out of the market for start up ventures.

Azure credits

12. Azure also offers a programme of free credits to its Partners. The Microsoft StartUps Founders Hub "provides free access to leading AI models through Azure, including OpenAI GPT-4o, up to $150,000 in Azure credits, one-on-one guidance from Microsoft experts, and so much more. Open to founders ready to build" [2]

What is the value of the free credits to start ups?

13. The AWS and Azure free credits have real commercial significance to a start up. By way of example, a typical start up may have one server a month. An offer of $100K in free credits would cover hosting costs for some years, even assuming that the new business grows rapidly and increases its requirements.

14. In its 2023 Market Study on Competition in the Cloud Sector, the French Competition Authority found:

"*Cloud credit programmes target customers at a time when they are making long-term structural choices. The imbalance in the attractiveness of different providers' offers "would deprive [smaller] providers of fair access to the market for startups in the creation or growth stages". Part of the customer base would therefore be inaccessible to smaller players, limiting the entry and expansion of competitors. As a result, hyperscalers' credit programmes can lead to an increase in the time horizon required for a competing cloud service provider's business to become profitable.*"[3]

Deep pockets

15. AWS and Azure are the most profitable parts of Amazon and Microsoft, and have extremely deep pockets. The cost to them of offering a free credit programme is insignificant, but smaller, private cloud companies such as BlackBox simply

[2] Microsoft for Startups Founders Hub
[3] Para 412.

cannot afford to offer free credits, and they are therefore unable to complete for the business of start up ventures on a level playing field. Again, this was noted by the French Competition Authority in its 2023 Market Study:

"*According to one hyperscaler, the future income generated by the cloud credits granted to customers far exceeds their initial cost. It claimed that credit programmes are "profitable and generate a positive return on investment in the medium term (generally three years), if not sooner". However, it is not certain that a new entrant to the cloud sector, which is as efficient in terms of variable costs as the hyperscalers, but does not enjoy the same scale and range effects as the established providers, will be able to make such a discounted sales policy profitable in such a short space of time.*" [4]

<u>Switching</u>

16. Once a start up has exhausted its free credits, private cloud providers should in theory be on a more equal footing to compete with AWS or Azure for their business, absent egress fees. For some customers in particular, the greater security of a private vs public cloud is key – for example, legal tech or HR accountancy services processing sensitive and financial personal data. The technical barriers to switching are not insuperable. One of the value add propositions of BlackBox, as a private cloud provider, is that it offers a fully managed service and can manage the move from AWS to BlackBox on behalf of its clients, for a relatively modest set up fee. This is particularly valuable for the smaller customer who may not yet have its own in-house IT resource capable of managing the move.

17. However, the egress fees are a very significant disincentive to switch, as AWS and Azure charge customers both to access their data and switch it out from the public cloud. These egress fees are part of a commercial strategy to lock customers in. They are not necessary. BlackBox itself does not charge its customers egress fees should they want to switch to another provider.

18. AWS and Azure also provide free training to customers to use their platform, and so this acquired know how, which is specific purely to the public cloud, is a further disincentive that Azure and AWS have put in place to discourage customers from moving.

[4] Para 414

19. Together, the free credits and egress fees are preventing and distorting competition and stifling the potential growth of new entrants to the market. Again, to quote the French Competition Authority:

    "*The granting of cloud credits could be part of a more global strategy of locking in customers. This is because cloud credits are reserved for the use of the provider's products and services for a period of up to two years, against a backdrop of technical and price barriers to migration (see - b below). In the words of one provider, "cloud credits are not just about testing their platform or offsetting migration costs, but about buying their customer base and locking in the market". The financial costs of change associated with the specific investments made by customers previously attracted by disproportionate credit volumes would then lock them into the ecosystem of the major providers. One customer found that "once a cloud provider has been chosen, a company has to invest to make it work and be able to use the cloud. It is therefore not easy to invest again to change provider." For a customer, the cost of changing provider after using the credits offered would be proportionate with the investment made and therefore depend on both the amount and the duration of the credits offered*."[5]

20. BlackBox's service should be a genuine competitor to the public cloud services, of particular value to customers for whom security is a key concern, and for those without the in-house IT resource that large customers enjoy and who need the managed service BlackBox can provide. It should be able to more than hold its own against Azure and AWS competing for start up ventures. However, the market is unnaturally distorted by the free credits that AWS and Azure offer to start ups, which lock the smaller private cloud providers out of this customer segment, together with the unjustifiable egress fees they charge that disincentivise customers from moving once their free credits have been used.

The CMA's Provisional Decision

21. BlackBox notes that the CMA has provisionally found that there are AEC's arising from certain features in the cloud services market, and in particular that it has provisionally found that the presence and magnitude of egress fees reduces the ability of, and/or incentives for, customers to switch and/or multi-cloud to other cloud providers. The CMA has not made any findings on the impact of free credits, but in BlackBox's views, free credits both worsen the anti-competitive effects of egress fees and cause a standalone AEC.

[5] Para 421

22. BlackBox notes that the CMA's provisional view is that it could use its powers under the Enterprise Act in relation to ban egress fees, and that a ban rather than a cap would be the most appropriate intervention. However, the CMA is proposing to recommend that the CMA Board use its new digital powers under the DMCC Act to address egress fees (and other market features). Our concern here is timing and the ongoing impact of these problems; the CMA will not issue its final decision under the current market investigation until July 2025, and were the CMA to then start to commence SMS investigations, any intervention by way of a CR or PCI would be take at least another 9 months.