

The Subscription Economy – a Case for Cloud Innovation

A CloudSense Report

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The purchasing habits of both consumers and businesses are going through a period of rapid change. Just a few years ago the majority of products and services were bought on a standalone basis. A consumer wanting to buy music, for example, would purchase an individual album; similarly a business requiring accountancy software would buy an out-the-box software solution. This was the case for physical products too: a commuter who wished to cycle to work would have no option but to buy a bike. Today purchases, however, are increasingly likely to be transacted online and provided as a subscription service.

Driven by the rise of online subscription services, today's music lover is just as likely to sign up to music streaming from Spotify, while many businesses are looking to conduct their accounting over SaaS-based services such as Freshbooks. The modern commuter meanwhile can subscribe to a bike share scheme, removing the need to buy a bike for themselves. Such services are being transacted over converged devices and often consumed that way too, including smartphone and tablet platforms which are acting as access points to the multitude of services stored on the cloud.

These changes will have wide ranging implications for how businesses implement their ordering process to the extent that they will have to look to cloud-based services that are rapid to deploy and easy to change in order to maximise the opportunities afforded by the new subscription economy.

Drivers behind the Subscription Economy

There are several core drivers behind this shift in purchasing behaviour.

- **Demand for more choice.** Consumers and businesses are increasingly asking more of the goods and services they consume. In the past consumers were faced with a continual cycle of obsolesce for the goods they bought. One year's 'must have' phone, for example, would be outdated in a handful of months. Consumers, therefore, prefer the subscription model which allows them to refresh products as new versions become available.

- **Change in approach from businesses.** Businesses have gradually moved from a product-centric to a customer-centric view. Today's businesses worry less about how many units of a product they ship and more about securing an ongoing relationship with a customer – one that will deliver ongoing revenue. The subscription model is ideal for delivering ongoing customer relationships and delivers tangible bottom line benefits to businesses. Digital subscriptions to FT.com, for example, increased by 34 per cent in the first half 2011, according its half year results. This rise was largely credited with delivering three per cent underlying growth in profit for the business
- **Reduced cost.** The subscription model provides the same amount of choice but at a reduced cost. A bike, for example, will cost many hundreds of pounds, versus a small subscription fee for services such as 'Boris Bikes'.
- **Consumer disaffection with advertising.** There is evidence that consumers will often subscribe to a service in order to reduce their exposure to advertising. Hulu, for example, has responded to a number of Tweets complaining about high levels of advertising by looking into offering a premium subscription site with reduced advertising levels.
- **'Digital Natives'¹ coming of age** – Those born in the latter stages of the 1980's grew up with a greater inherent understanding of technology, having interacted with it from a younger age to previous generations. They are demanding a more flexible approach to the consumption of goods as well as more personalised and immediate services and they don't expect explicit charging for each service. They have grown up with free content services funded by adverts. The subscription model is ideal for providing this – the service may change within the subscription.

The subscription economy is with us today and set to gather pace. Already we are seeing physical goods that would once have been bought as a one off capital expenditure, move to the subscription model. Birchbox, for example, sends monthly boxes of beauty products to subscribers in a similar business model to snack providers such as Graze – goods that would once have been bought in a super market are now delivered over subscription. ZipCars, meanwhile, has demonstrated that even large scale consumer items, such as automobiles, can be elegantly delivered over the subscription model.

The convenience of this system for the consumer is easy to see, what is less understood is the huge impact this will have on the back office ordering process systems of businesses looking to make the most of the subscription economy.

The impact on business processes

Businesses must look to modernise their back office systems so that they can more effectively cater for this new paradigm. IT decision makers should look to model their approach to ordering process on the subscription economy itself. By reflecting the way in which consumers buy services, businesses will find they have a much more efficient, powerful and productive back office stack. In this approach, businesses will subscribe to a set of cloud-based services that would be able to address the key areas of pricing, quoting and ordering while integrating all cloud applications and infrastructures and being flexible enough to deliver rapid change.

¹ The term 'digital native' was coined by Mark Prensky in *Digital Natives, Digital Immigrant*, 2001

Research commissioned by CloudSense in August 2011² clearly demonstrates that businesses are already looking to move their applications over to subscription-based purchasing models. The majority of respondents (58 per cent) stated that they have already migrated all or some of their applications to a subscription-based purchasing solution, with a further 17 per cent stating that they were planning to do so.

The research also made clear that there is now good awareness amongst senior IT managers about the range of benefits that the subscription based purchasing model will deliver. The main benefits perceived by the respondents were:

- More tightly controlled costs (59 per cent)
- Faster speed of implementation (50 per cent)
- Avoiding costly infrastructure so we can focus on innovation and value added IT (50 per cent)
- The provider is more accountable (36 per cent)
- Ability to scale up and down as our business changes (32 per cent)
- Reduction in space and energy costs (26 per cent)

These well reflect the reasons why businesses are increasingly migrating to cloud-based subscription purchasing models. As this approach frees organisations from the need to focus on R&D, or to invest in infrastructure, costs can be more effectively managed. Moreover, the subscription model removes the need for businesses to purchase according to a costly refresh cycle. As new features become available, businesses can upgrade just as easily as a consumer can upgrade their phone, without the need for a complete overhaul of their solutions infrastructure.

Speed of implementation is also a notable driver. Enterprise projects which would have once taken years to complete and cost in the millions can now be deployed within months and at a greatly reduced cost and against a profile of ongoing, incremental change. This allows businesses to come to market more quickly with new propositions and achieve a competitive advantage. It also frees up considerable in-house resources, formerly allocated to establishing and running ordering process systems, to concentrate on core revenue-generating business activities.

Scalability is also of great importance. The traditional purchasing model was rigid, meaning that businesses often had to invest in solutions that were not well suited to their stage of development. This could result in having to invest in software and services that were too complex for their business, leaving businesses paying a premium for features that they did not actually need. The subscription based model allows businesses to subscribe only to those products and services that they actually need at a given time, providing a highly flexible architecture that can grow – or shrink – as they do.

Cost Savings and the integrated approach to IT solutions

When it comes to the cost savings that will be enabled by subscription-based purchasing models, the respondents to the survey demonstrated high-levels of optimism over just how much could be generated. 76 per cent of respondents were clear that the subscription model

² The research, carried out by Vanson Bourne, interviewed 100 Senior IT Managers in UK Enterprises (minimum 1000 employees)

would generate savings for their IT budgets to a greater or lesser extent. Only 5 per cent of that group thought the savings would be minimal - £5,000 per year. The majority of respondent's demonstrated belief that the cost savings will be substantial: 23 per cent believe it will deliver £50,000 savings per year, 24 per cent believe it will deliver £10,000 savings per year and 24 per cent recorded that they think it will deliver £100,000 or more in savings per year. For CloudSense this demonstrates strongly why businesses are increasingly migrating to the subscription-based purchasing model.

It also seems clear that a key reason why businesses believe the subscription model will deliver such strong cost savings is that it allows them to integrate their technology solutions to a greater degree. When asked whether, from their own experiences within their organisations, they believed a lack of integration in technology solutions can lead to increased operational cost of IT management, the respondents were quick to agree. In fact, 95 per cent of the senior IT managers polled agreed that lack of integration is responsible for increased operational costs for their businesses.

Today, enterprises have an ever more complex mix of products and services often delivered using 3rd party partner components. Using an integrated subscription-based software stack based in the cloud, complex solutions can be easily bundled and configurations including pricing, quoting and ordering can be unified and standardised across the business, helping to improve order fulfilment and cut fat from operational processes.

But successful implementation is not without its complications. In fact, integration can be the most challenging part of a distributed multi vendor IT estate. Businesses looking to migrate to an integrated cloud stack should look to partner with organisations that can show them how to successfully integrate their IT systems and start to realise the efficiency benefits from the outset.

Conclusions

The subscription economy has arrived. It has revolutionised the way in which goods and services are bought and consumed and CloudSense fully expects this new environment to gather pace in the next few years. This is an overhaul that will have profound impacts on the businesses that provide goods and services today. Those businesses that can successfully evolve their ordering process to be flexible, integrated and responsive enough to react to this new purchasing paradigm will benefit greatly from the subscription economy. Those that don't may quickly find themselves being left behind.
