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COST-OUT INITIATIVES:

The “Running Game” of Network Transformation

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ISG WHITE PAPER

INTRODUCTION

The most effective network strategies combine the blocking and tackling basics of operational improvement and tactical cost-cutting, along with implementation of transformational change.

Many successful football teams rely on a combination of a pound-and-ground running game complemented by timely passes. This approach consistently produces wins, but it requires strategic commitment and tactical patience. Coaches who yield to temptation and abandon the run too early in favor of long bombs and trick plays often find themselves on the losing end of the scoreboard.

There's a lesson here for CIOs managing networking in the era of digital transformation. Driving cost savings from traditional services contracts represents the "running game" of network operations. While effective, it can take time and is not terribly glamorous, especially when the allure of digital transformation beckons. But traditional services and digital-enabling technology such as cloud-based delivery, X-as-a-service and software-defined everything are not an either/or proposition. Basic cost efficiency and contractual discipline remain essential to network operations, and savings can affect the bottom line or fund critical transformation initiatives.

The most effective network strategies combine the blocking and tackling basics of operational improvement and tactical cost-cutting, along with implementation of transformational change. This ISG white paper explores how using savings from contract renegotiations and network improvement programs to invest in new and innovative technologies allows CIOs to build a powerful business case for disruptive change.

Enterprises should nurture a multi-provider relationship environment that fosters healthy competition.

Prep for Contract Negotiation

Many enterprises don't adequately prepare for network services contract negotiations. They wait too long to begin the preparation process and/or ignore subtleties that can be key to a successful negotiation. The first step is to understand the timing and profile of the existing contract mix. While most companies track when major agreements expire, they have no idea of the termination dates and terms surrounding smaller contracts for niche services. Moreover, they lack insight into the timing of rate reviews or the tracking of commitment retirement, which are essential to an effective renegotiation position and potential leverage for investments with the same provider.

Preparation also requires establishing and developing solid executive-level relationships that go beyond the account rep and that can be utilized during contract negotiations, such as the providers offering management/pricing groups and legal resources. Finally, the ability to compile an accurate inventory of services is becoming a growing problem for many enterprises, especially for those extending services and service management into expanding global markets. A quick upfront baseline assessment that identifies how to access detailed data can provide invaluable support to a negotiations strategy.

Introduce Competition

Many large enterprises maintain single-sourced relationships with major network providers and fail to take advantage of competitive dynamics offered by multi-provider arrangements. Moreover, when they do initiate a multi-provider RFP, clients often are surprised by the response. Rather than rushing in to win their business and displace the incumbent, network providers are reluctant to invest scarce resources on an opportunity in which they lack a foothold or established relationships.

Enterprises should nurture a multi-provider relationship environment that fosters healthy competition. Today's market is shifting from the legacy one-provider approach (a 90-10 mentality) to a more balanced enterprise network landscape with a 70-30 or 60-40 split, and potentially even a third provider for specific services such as network management. This mindset allows a savvy CIO to engage global providers in a continual advance-and-retreat strategy over the course of the contract terms and renewals. Providers must remain on their toes, as the client moves traffic and services between providers for emerging technology maturity, pricing, availability and other reasons.

Determining how to split the network is another imperative. The key strategic sourcing decisions focus on the primary data network and network management that keep a company operating. At a secondary level, less-strategic voice, conferencing, colo, back-up data and other related service elements can be used to create pricing compression and competitive threat. This delivers financial benefit while protecting the client's most important network asset – the primary data network and managed services.

In terms of timing, clients should begin to co-terminate their largest network contracts within a six-to-twelve month expiration window whenever possible. Combined with a mid-term rate-review provision and other market-leading business terms, this approach maximizes leverage and the potential for a sizable cost-reduction event every 18 months – whether or not major network changes are required. An additional benefit: contracts are never too far out of date and are more likely to reflect continual changes in pricing and margin priorities.

If a company can establish market-based guidelines and comparative standards – and a consistent, leveraged approach – negotiations can be a meaningful dialogue for both parties.

Challenge Contracts for Custom Services

While most network services are based on validated rates for standard services and well-defined business terms and conditions, in some cases, buyers require specialized, custom services such as private and high-bandwidth connections. Such services typically require providers to invest in special equipment and expertise, which means higher rates to underwrite the upfront capital costs. However, companies often continue to pay above-market rates long after providers recoup their investment and have significantly lowered their internal monthly costs.

One problem is that specialized services typically are wrapped in larger agreements, which means they aren't directly negotiated, so the higher rates get pushed into the next contract. In addition, market-based comparators for custom services are hard to find, so clients have little market insight. Enterprises can address these challenges by focusing on custom services as a separate discussion item. Even without like-for-like market-based pricing comparisons, general rules regarding margins and payback period for custom access and special builds can be applied. Evidence of install dates, service location and private route paths gleaned from other contracts can build an effective case for lowering monthly rates.

If providers push back, claiming that the complexity surrounding custom services requires special support on an ongoing basis, companies should demonstrate a willingness to put the service out to bid. Because custom services generate significant margins for providers, even a revised contract with lower monthly costs will remain a profitable deal for them.

Demand Clarity in Pricing

Obtuse pricing is a tried-and-true tactic some network providers employ to muddy the waters and gain an edge at the negotiating table. If clients lack insight into pricing, they struggle to understand how Provider X's apples compare against Provider Y's oranges, and whether either offering is aligned with competitive market standards. Amid this confusion and uncertainty, clients often leave money on the table. This has become even more true with varying approaches to network-as-a-service, hosted unified communications, and emerging offerings like software-defined network (SDN) and network function virtualization (NFV).

Rates are contained in a variety of formats that include contracts, amendments, addendums, schedule of charges, service-order attachments, tariffs, service guides, discount tables, promotions, credits (both one-time and recurring) and individual quotes. Invoicing and billing are similarly convoluted, with different names and descriptors for usage types that don't always match terminology in the contract.

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In this environment, the onus is on the enterprise buyer to understand the contract, reference actual pricing included in the agreement and define a true contract rate as the basis of negotiation. But within this challenge lies an opportunity – if a company can establish market-based guidelines and comparative standards – and a consistent, leveraged approach – negotiations can be a meaningful dialogue for both parties , rather than a distrustful exercise with smoke and mirrors and a protracted no-win battle. And while providers may not relish the thought of a more-level playing field, increasing transparency and consistency will ultimately facilitate an honest, mutually beneficial relationship.

Demand Insight into Provider Plans and Options

Network provider plans, programs and options change on a quarterly basis, as do variations between small, medium and enterprise business offerings. Network provider financial objectives are similarly fluid, forcing client-impacting changes in pricing strategy and flexibility, service and technical support models and long-standing personal relationships. Understanding current offerings and market nuances can have a significant impact on pricing and the overall contracting environment. For example, enterprise buyers typically aren't eligible for less expensive small-business wireless plans. However, we've seen instances in which providers make an exception to keep a client happy. Exploring these options can yield results.

At a broader level, a company should leverage awareness of market changes and provider behaviors to remain ahead of the curve, not to mention set high expectations for network providers to communicate the status of new services coming on line, as well as established offerings being slated for retirement. While the opportunity varies, a rigorous contract negotiation and services management strategy can yield significant savings for a Fortune 1000 enterprise.

Tactical Cost Savings and Strategic Transformation

While many of the benefits from more-effective management of network services are obvious, we observe top-performing organizations integrating cost reduction initiatives with transformational change programs, so they can use tactical savings to support broader strategic objectives.

By aggressively mining savings opportunities for commodity services, CIOs can apply savings to cloud initiatives and maintain a healthy budget.

Enterprise buyers have many opportunities to use negotiated network reductions to fund other, critical transformative initiatives, such as SDN, NFV, cloud peering, higher/commodity bandwidth, contact center outsourcing, unified communications and various cloud-based services. The challenge is that IT leaders typically don't come from a network background and can lose site of the value that cost-out initiatives can deliver. A savvy CIO stays continually focused on network services and the potential size of the prize of network savings and how they can support transformation initiatives.

A typical "running game sets up the passing game" scenario unfolds as follows: An enterprise sourcing group starts a renegotiation with a major network provider by stating a desire to migrate the network, overhaul the WAN and increase capacity. Quick hits from existing contracts for legacy services are identified, and the conversation shifts to how the savings can be reallocated to implement new technologies and services.

Consider this example: a large enterprise transitions its decentralized global WAN to a SDN, leveraging global peering points, WAN acceleration, cloud peering and optimization of the current global bandwidth utilization by 30 percent. The initial implementation requires some upgrades to existing networking equipment and the company moves to a managed services environment to ensure a successful delivery and ongoing operational stability. While the bandwidth optimization brings savings, the one-time costs and increased management costs absorb some of it. During the development of the upfront business case, the buyer assessed the cost for bandwidth of the existing providers and determined it to be off market by $800K annually. As a result, those agreements were renegotiated prior to the transformation. This is the "running game." When coupled with the transformative event of moving to SDN, the company was able to drive down the costs for the circuits prior to making the technology change and offset or "fund" the one-time costs and add managed services, achieving the full net benefit of the bandwidth optimization. The result is a net annual operational savings of $800K post transformation.

In a recent client engagement, ISG conducted a provider rate review (running game) to take cost out of existing fixed-cost network services. By coupling a transition away from the existing end-of-life telecom environment and moving to a fully managed UC solution, annual net costs were reduced by $1M.

The model of reinvesting savings from cost-out initiatives is less straightforward with regard to cloud or as-a-service models. By moving from a mix of opex and capex to a recurring "all in" price, cloud-based delivery models raise some budgetary implications by increasing opex expenditures into the equation. Moreover, cloud initiatives increase the technology set and require significant investments, often with performance benefits that don't readily lend themselves to a straightforward budgetary tradeoff. That said, the cost-out "running game" can still be applied, and by aggressively mining savings opportunities for commodity services, CIOs can apply savings to cloud initiatives and maintain a healthy budget.

As variable cost solutions like cloud and X-as a service continue to gain momentum, CIOs should recognize that budgetary proportions will inevitably shift with declining network infrastructure costs and proportional increases in other areas. In this environment, rigorous oversight of commodity contracts that drives savings is critical.

Bottom line: Enterprises typically cite a lack of funding as the reason they don’t invest in new technology. An effective running game that takes cost out of existing network infrastructure can free up the resources to help address future requirements.

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Katharine brings more than 17 years of IT and telecommunications experience in advisory, account management, sales and service delivery. She helps clients determine and execute strategies that align vendor solutions with emerging technology, operational and service needs. Katharine provides executive sponsorship with key clients, supports the development of the client relationship, and oversees programs such as complex IT outsourcing and telecom sourcing events, assessment of technology design and roadmaps and business cases for technology transformation events. She has worked with numerous Fortune 500 and global enterprises including ADP, BNSF, Pfizer, First Data Corporation, EFH, Men’s Wearhouse, WellPoint, CBRE, PG&E, Wells Fargo, Kaiser Permanente, Humana, Office Depot and Newscorp.

ABOUT ISG

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