Design for digital
A business vision to prepare communications
service providers for the cognitive era

IBM

4. New business models for CSPs

There are many different views on what a "business model" is, but at its simplest it is a description of how a business makes money.

For CSPs for over a hundred years this was actually a relatively simple model. CSPs controlled networks that cost a lot to build. They sold the ability to make telephone calls. The marginal cost of the calls was almost zero, so CSPs made a lot of money selling telephone calls that enabled them to make good profits, some of which they invested in the next generation of networks. From the customer point of view it was pretty simple too. The customer wanted to make telephone calls so needed to buy the service from the CSP. Typically this was either a monopoly provider or one of a small number of competitive operators. The customer did not have a lot of choices to make.

Many CSPs are still stuck in the same mind-set but the digital environment has brought radical changes. Perhaps the biggest change is that CSPs no longer sell exactly what customers are buying. In the original model CSPs sold the ability to make calls. Customers bought the ability to make calls. In the digital environment CSPs sell data. But customers don't buy data. Customers do not wake up in the morning and think "After I've had my first cup of coffee I am going to consume some data". What customers buy are movies, video clips, games, healthcare monitoring, home security monitoring, and the ability to buy and sell shares and manage bank accounts. To do all these things they need a data pipe that they buy from the CSPs just like they need electricity to power the many devices they consume these services on.

One of the impacts for CSPs is that they have lost the link between the volume of what they sell, in other words the number of megabytes of data, and the money they receive from the customer. As a result the volume of megabytes sold can double or treble in a year while revenues remain flat or fall. Worse still, CSPs are still carrying the load when it comes to the high cost of building out networks without any certainty that those cost can be recovered. Worst of all, they are rapidly losing their emotional connection with their customers.

The first choice CSPs must make is whether they want to be primarily a utility provider of network services, or a provider of digital services. Those that choose to be utility providers will need a "lean and mean" business model focused on driving cost out of operations and promoting maximum efficiency in delivery of service. For those that choose to be digital services providers there are three main challenges:

- Finding new sources of revenue to replace falling revenues from traditional voice, messaging and data
- Providing a customer experience that matches or exceeds their customers' increased demands
- Doing the first two things while dramatically cutting operating costs

In addition, CSPs must figure out how to manage the legacy products and processes (and underlying systems) that have brought revenues in for many years and will continue to do so at a reduced rate for some years to come.

So what will be the main characteristics of the DSP business model?

There is no established model for the digital service provider. Most CSPs are experimenting with different approaches, some radical and some evolutionary. IBM believes certain themes are emerging that are starting to answer the three challenges:

New sources of revenue: digital products have certain things in common. They require some form of network connectivity and they usually have a significant non-Telecom component. Mobile health monitoring requires the network but it also requires a healthcare component; mobile banking requires a financial industry component, and so on. Digital products also tend to have a much shorter lifecycle than traditional products. Time to market is critical and the pace of innovation is accelerating. It is hard for a CSP to know where to focus. Many are adding TV service as they seek to draw customers in through product bundling via triple-play and quad-play offers. This can be successful but it is really just an extension of the traditional way of doing business – making the pipe bigger to handle more services. It is as vulnerable as other services to becoming a utility business in the medium term.

More interesting developments are where digital service providers (DSPs) are seeking to develop broad ecosystems to 'capture' a definable chunk of the digital market such as the connected home or the connected car. The aim here is to become the supplier of choice in these domains. It involves a significant change in brand image but if successful it allows the DSP to own a market in much the same way as Amazon owns a significant share of the online retail market. For example, if the aim is to "own" the connected home then the ecosystem can include security companies, home appliance manufacturers, heating and air conditioning vendors and a whole emerging range of items in the home that have one thing in common – they can be controlled by a single mobile device. Once the market position is established then it becomes reasonable to expect consumers to buy household items, normally unrelated to Telco, from a DSP – probably through an app on their mobile device.

It is relatively easy to imagine DSPs becoming dominant in the connected home because there is no obvious rival for the position. It is more difficult in other areas such as the connected car, mobile finance or healthcare. Automobile manufacturers will compete for dominance of the connected car and banks or healthcare providers will do so in finance and healthcare. In these markets branding becomes critical. Will consumers prefer to buy mobile services from the DSP or from the providers of the underlying service? This is a critical question since the dominant brand will be in a position to extract the most value from the customer.

A new approach to customer experience: the new business model has to be designed from the customer point of view with the aim of creating an environment where it is easy and enjoyable for the customer to do business with the DSP. As such, the model has itself to be agile and innovative so as to be able to adapt to ever changing customer demands. A few things are clear though. The customer experience should be online, mobile, personalized and real-time. This requires a new approach to products and processes that are currently call centre/retail store focused and emphasize the efficient batch processing of bulk customer transactions. This new approach is discussed in more detail in the next section.

New operating models with dramatically lower operating costs: one of the characteristics of many companies with high levels of customer satisfaction and customer advocacy is that they are low-cost operators, For example, two of the highest rated retailers in the USA, Costco and Trader Joe's, are renowned for their different approaches to low cost operations. An excellent customer experience is not achieved simply by throwing money at customer service. If the existing processes and systems are not designed from the customer point of view, then simply spending money on them will not improve customer experience. This is at the heart of why so many IT driven 'transformations' of CRM systems or billing systems have failed to deliver expected business benefits. Doing

the wrong thing more efficiently is not a recipe for success. Designing operations so that customers can self-serve in an easy, enjoyable way can have the double benefit of increased customer satisfaction and lower operating costs. This is a lesson most CSPs have yet to learn.

The legacy world

What to do about legacy products, processes and systems is a challenge facing most CSPs. There is no single way of approaching this but IBM strongly recommends that whatever approach is taken, the new agile customer oriented DSP business is protected somehow from the legacy world. We recommend that legacy be managed separately with a focus on cost reduction and operational efficiency. One way of achieving this separation is to adopt a Mobile Virtual Network Operator (MVNO) model for the launch of digital products. In this way back office legacy systems for functions such as provisioning or trouble ticketing can be kept in place, while customer facing functions such as commerce and campaigns can be redesigned for the digital market.

The MVNO model separates network infrastructure from sales. Operators may need to consider whether the traditional vertically integrated model will be most effective for tomorrow's digital service provider. In Australia, for instance, the National Broadband Network (NBN) is developing a national, open access data network that will sell its capacity to retailers who then sell on to businesses and consumers. Could this model be adopted elsewhere or are other new models possible?