



Cloud Channel Trends, 2013 To 2014

by Tim Harmon and Jonathan Silber, February 28, 2013

KEY TAKEAWAYS

Channel Partners Are Embracing A Mix Of Cloud Reselling And Provisioning Models

Tech vendors need to nurture the latter carefully, as channel partners' cloud services provisioning businesses can compete with those of vendors.

Fewer Channel Partners Are Willing To Invest In The Professional Services Business

The number of channel partners offering professional services in two years is projected to decline significantly. While this will bode well for SIs and VARs that rebuild their professional services skill sets for cloud, the aggregate reduction in cloud-oriented professional services companies will result in a gap in supply and customer demand.

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A Critical Mass Of Channel Partners Are Embracing Cloud

by [Tim Harmon](#) and [Jonathan Silber](#)
with [Peter O'Neill](#) and Tyler Otte

WHY READ THIS REPORT

Forrester recently surveyed channel partner company executives on their business model plans with respect to cloud computing. What we learned: After much gnashing of teeth (over marginalized profitability and disrupted cash flow) and dragging of feet (on the decision to reinvest in and remake their businesses), channel partners have finally begun to adopt — and build — cloud solutions into their solutions portfolios in a big way. Tech vendors need to understand how the channel is changing in order to keep their partners in their fold. The key will be to think of them as equal go-to-market partners and not as links in a supply chain.

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In preparation for this report, Forrester interviewed leading technology marketing vendors for their insights on cloud channel trends. Forrester also used data from two surveys conducted in the past 18 months.

Related Research Documents

[How Customers Value IaaS Cloud Channels](#)
September 5, 2012

[Market Overview: Managed Service Providers, Part 1](#)
May 9, 2012

[Channel Partners' Needs In The Era Of Cloud](#)
January 14, 2011



THE CHANNELS FOR CLOUD SOLUTIONS CONTINUE TO GROW

There was a time not long ago when both tech vendors and channel partners thought (or feared) that cloud computing would provide tech vendors with a more direct route to market, cutting out the channel — in essence, that vendors would disintermediate the intermediaries. To be sure, many channel partners have been slow to take up the cloud reins — and some vendors have been reticent to hand those reins to the channel.¹ But the tide is beginning to turn: Early channel partners to the cloud have matured to a commanding size and stature, and more and more latecomers are getting on the cloud bandwagon.

But there is a great deal of variety (there being a great number of options) in how channel partners are taking up the cloud — and in their needs and expectations of vendors in terms of enablement (see Figure 1):

- **VARs and SIs are rising to the cloud opportunity.** Classical value-added resellers (VARs), in representing cloud solutions, can choose to stay on the resell treadmill — although those that do so are finding that their product margins on cloud solutions pale in comparison to those for on-premises enterprise-license products (and thus skew their salespeople's behavior). Systems integrators (SIs) are taking advantage of the more complex configuration and customization needs that customers of cloud solutions call for.
- **MSPs and CSPs are expanding their services portfolios.** “Born in the cloud” managed service providers (MSPs) and cloud service providers (CSPs) are reaping the fruits of their early investments and reinvesting in expanding into a broader set of cloud and managed services. Moreover, many VARs have added or are planning to add managed/cloud services to their solution portfolios and, in so doing, represent the new hybrid partner type, which vendor channel professionals must accommodate.

Figure 1 Channel Partners' Business Models/Revenue Stream, Current And Planned



Base: 116 channel professionals at companies with 1,000 or more employees

Source: Q4 2012 US And European Channel Partner Business Model And Loyalty Online Survey

90001

Source: Forrester Research, Inc.

CLOUD SOLUTIONS RESELLING: PARTNERS ARE EMBRACING THE INEVITABLE

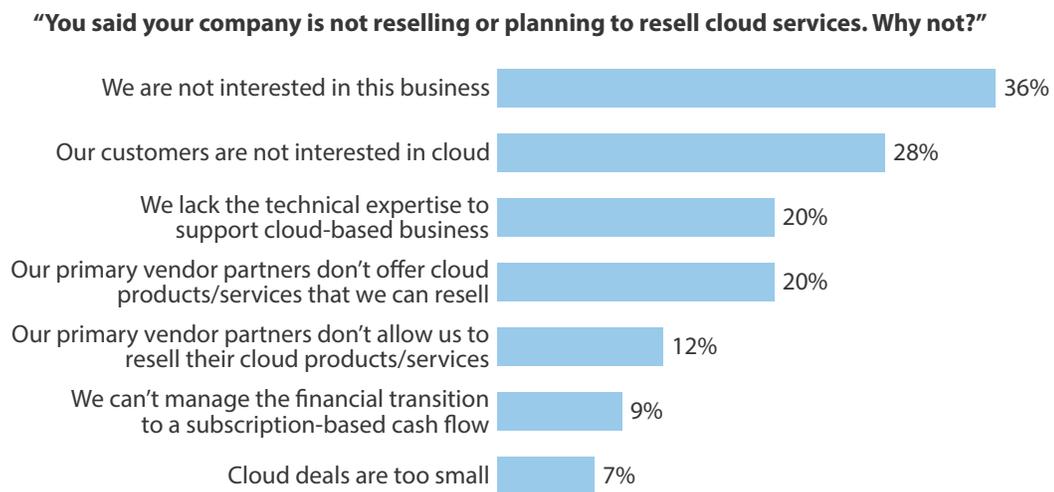
As much as tech vendors, per their cloud solutions, may like to cut out the middleman, customers value the relationship intimacy and support they get from VARs (and VARs do everything they can do to sequester that customer relationship for themselves!). That relationship dynamic (and value) isn't going away anytime soon, so despite the fact that VARs see diminishing margins on cloud resell, the market for cloud solutions is growing healthily. And VARs are realizing that they either have to meet that demand or cede the opportunity (and customer relationship) to vendors. In that context, the choice is clear. And the numbers bear out the fact that VARs are looking to get into the cloud resell business in a big way, albeit somewhat begrudgingly: Reseller numbers for cloud infrastructure services, cloud software services, and cloud virtual desktop infrastructure (VDI) services are projected to rise dramatically.

But Some Still Have Their Heads In The Sand

Still, there is a goodly number of channel partners that refuse to see the cloud writing on the wall (see Figure 2). Whether it's a matter of close-to-retirement owners, hardware "box pushers" unwilling to reinvest in their businesses, or business executives simply resistant to change, many partners:

- **Have a huge blind spot when it comes to cloud.** The No. 1 reason that channel partners cite for not embracing cloud solutions resell is that they "are not interested in the business" (diagnosis: fear of the unknown). The second highest response is that their customers "are not interested in cloud" (diagnosis: denial). The latter is particularly confusing, in that this sentiment runs directly counter to customers' aggressive plans for and interest in cloud computing. This point will be reconsidered in another context later in the report.
- **Are abandoning the professional services business, indicating a future void.** The projected decline in the number of channel partners offering professional services should be disconcerting to (and a wake-up call for) tech vendors. As customers look to invest in cloud solutions, they are searching for — but often not finding — solution providers that can do the configuration, customization, and integration that their hybrid business technology (BT) environments necessitate. If not addressed, this situation could even constrain the overall growth of the cloud market. Most SIs have invested in developing or acquiring cloud skill sets, but many VARs have not and remain ill-equipped. Because VARs dominate the channel in terms of pure number of partner companies, the overall number for professional services businesses is going down.

Figure 2 Channel Partners' Reasons For Spurning Cloud Resell



Base: 69 channel professionals at companies with 10 or more employees
(three responses accepted)

Source: Q4 2012 US And European Channel Partner Business Model And Loyalty Online Survey

90001

Source: Forrester Research, Inc.

Channel Partners Need Help To Prosper From Cloud Reselling

Channel partners face a multitude of challenges in getting into the cloud reseller business: smaller margins, radically different cash flow, and marketing and selling (of a service [as opposed to a product]). What does that mean for vendor channel professionals? Well, they need to step up and:

- **Rework margin model to accommodate partners' smaller margins.** The competitive scramble for cloud market share, combined with continuing slow economic growth, has compelled many tech vendors to bring their cloud solutions to market at a “bare-metal” price. This dynamic doesn't leave much of the list-price dollar for channel partners and squeezes their profit margins. Some vendor channel professionals offer much bigger discounts to their channel partners for their cloud offerings, particularly in the first year or two of customers' service subscriptions. For example, NetSuite has been very innovative in offering its channel partners a choice of discount margins: a 50-point margin for customer-lifetime subscription revenues or a 100-point margin for year-one subscription revenues.
- **Offer a financial engineering solution to partners' cash flow dilemma.** One of the problems that channel partners face in transitioning to cloud offerings is the hit to their cash flow — instead of the enterprise-license “big deal” upon which they've come to depend, a corresponding cloud deal's revenue is a stream spread out over 12 to 36 months.² Vendor channel pros should take a chapter out of the factoring industry book (where third parties buy up a company's accounts receivable at a discount) — and offer to “buy back” their partners' portion of the subscription revenue stream, giving partners their cut upfront. Microsoft instituted a program of this nature for its Microsoft Office 365 partners in 2012.
- **Reorient their marketing enablement program to target line-of-business customers.** Partner marketing enablement is all the rage in the tech industry (think of the power of 10,000 companies amplifying your marketing voice). But a lot of that marketing prowess for which vendors are enabling their partners is pointed at the IT buyer. But Forrester's data shows clearly that, particularly for cloud solutions, the buying center is shifting from the IT organization to the line of business (i.e., from the IT decision-maker to the business decision-maker).³ But most channel partners' marketing content and sales pitches are oriented to the technical buyer (i.e., the IT organization). Vendor channel professionals need to teach and equip their partners to: a) market and sell service values (service levels, on-demand variability accommodation, etc.), and b) market and sell to the business decision-maker (business value, business outcome, economic model, etc.).

CLOUD SERVICES PROVISIONING: THE GOLD RUSH IS ON

The average channel partner company supports 7.6 unique revenue streams today. Rather than add new revenue streams in the near term, channel partners are choosing instead to swap out underperforming business models for more profitable ones (e.g., dropping managed services resell to become a MSP, dropping cloud infrastructure-as-a-service [IaaS] services provisioning and getting into cloud VDI services provisioning). By the end of 2014, the hybrid channel partner revenue mix is expected to skew toward the provisioning of:

- **Managed services.** Channel partners are embracing integrated managed services and hybrid managed/cloud services — focusing on networking and telecommunications, IT infrastructure, applications, and security — as they move toward a recurring revenue business model. Remote management and monitoring (RMM) vendors like Kaseya and LPI Level Platforms are to some extent responsible for making this the fastest growing new revenue stream in the mix today.
- **Cloud VDI services.** As hosted desktop initiatives moved to the top of many BT organization's wish lists this past year — primarily as the result of VDI becoming an IT tool to support heterogeneous user devices and preserve application security — channel partners have been quick to capitalize on this cloud infrastructure services opportunity. With VDI adoption expected to spike in 2013, expect more and more channel partners to ride this wave.
- **Cloud software services.** Cloud software services are among the hottest growth areas in the cloud space today, and channel partners are progressively adding collaboration/application software-as-a-service, hosted email, unified communications, or enterprise resource planning (ERP) to their portfolios. Growth is expected to be strongest for channel companies with 1,000 or more employees.

Add this all together, and tech vendors will recognize that an increasing number of partners cannot conform to the strict segmented partner programs that many of them still maintain — major surgery is required in many tech vendors' partner program T's and C's (terms and conditions).

Many Channel Partners Are Surprisingly Resistant To The MSP Opportunity

Despite the enormous revenue potential of managed services and the fact that MSP growth now outpaces the rest of the IT industry, some channel executives lack the motivation to get into the game or see real challenges navigating their way through it (see Figure 3):

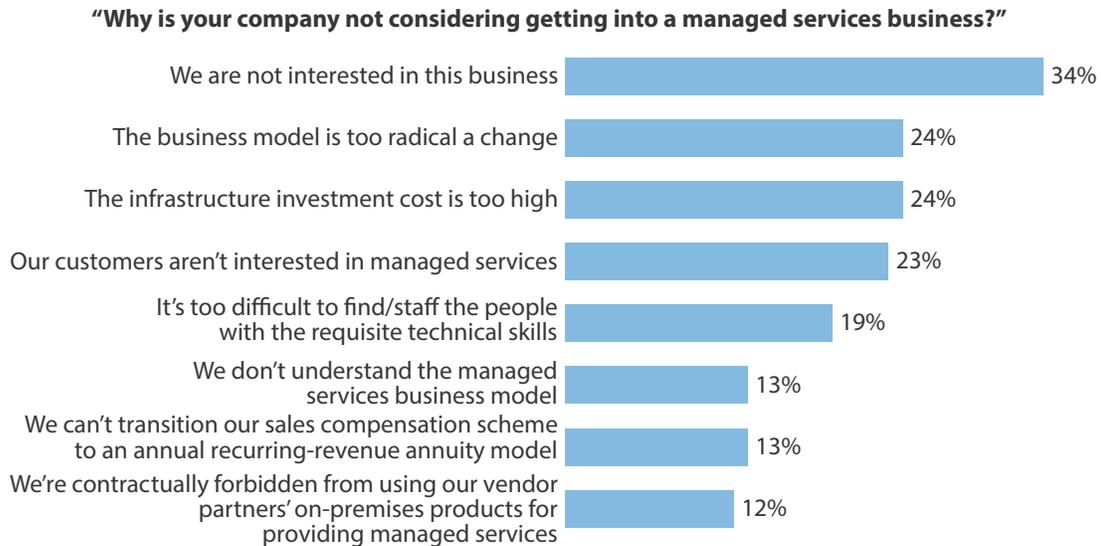
- **“We are not interested in this business.”** The No. 1 reason why channel companies do not enter the managed services space is because they are not interested in the business. This is startling because the managed services market is big and is getting bigger. As a whole, the top 100 MSPs grew 28% year over year from 2010 to 2011, and the best-performing MSPs continued to generate double- and triple-digit growth in 2012. Moreover, 62% of channel company

executives expect that their managed services revenue will increase in 2012, with more than 15% estimating that it will jump by a whopping 20% or more.⁴ Whether the lack of interest arises from the abundance of lifestyle businesses, box-pusher shortsightedness, or a reluctance to navigate the labyrinth of business model transformation, the message is loud and clear: One-fifth of respondents have no plans for investing in innovative business models. Channel marketers will have little luck convincing these channel partners to think outside the box.

- **“The infrastructure investment cost is too high.”** Nearly 25% of the MSPs we surveyed indicated that they invested more than \$1 million in network operations center (NOC) infrastructure to manage their managed services businesses.⁵ This capital expense alone is restrictive for many cash-strapped channel companies, and it does not even account for other mandatory expenses — for instance, investing in data center infrastructure, training a new managed-services-adept sales force/technical staff, and purchasing annuity-based payment software. Some vendors are helping channel partners that want to add managed services to their solutions portfolio but are disenfranchised by the large capex costs. For example, in October 2012, IBM introduced a financial plan specifically designed for MSPs that offers financing options specifically targeted to those MSPs that want to invest in their business without paying large upfront cash payments.⁶ The company is now adding more than 100 net new MSPs to its partner program per month. Other vendors have tinkered with underwriting some or all of the funding a partner needs to hit the ground running.

- **“The business model is too radical a change.”** It is often easier for companies to continue “as is” than to transition to a managed services business model: Change is disconcerting for a lot of companies, but it offers a huge opportunity. While some vendors simply ignore those partners that resist change, others well understand the realities partners face every day, take their pain both seriously and personally, and work hard to address the radical challenges for the partner. Microsoft is a great example of a company doing just that — it is enabling channel partners to get into the managed services business through a unique set of business model workshops, partner training and events, and online tutelage instructed by business consultants, not technologists. Moreover, when it comes to the value vendors can bring to channel partners with regard to MSP enablement, 36% of partners said that they value business model training for moving to a MSP business model (e.g., sales, hiring, operations, financial modeling).⁷

Figure 3 Channel Partners' Reasons For Spurning Managed Services



Base: 104 channel professionals at companies with 10 or more employees
(three responses accepted)

Source: Q4 2012 US And European Channel Partner Business Model And Loyalty Online Survey

90001

Source: Forrester Research, Inc.

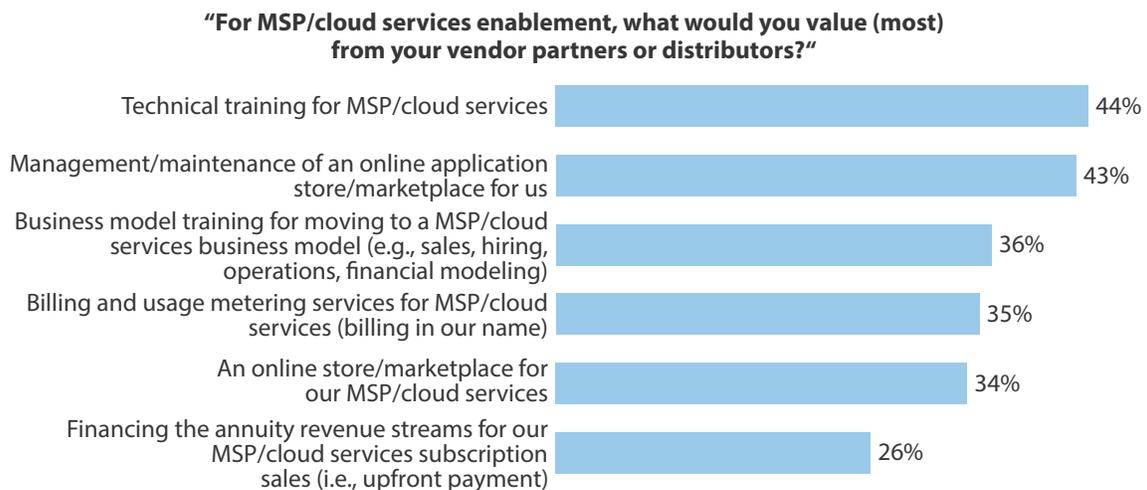
Channel Partners Covet Managed Services Enablement

Forrester has worked with several tech vendors and distributors that enable channel partners to quickly and confidently transition their business to managed services. One effect of this transition is that partners quickly place greater value on the vendor's enablement programs, channel business systems, and support.⁸ In fact, good channel partners are specifically seeking out vendors that promise to equip them with the knowledge and tools to support the changes they have to make to get into the managed services market. This typically includes a comprehensive portfolio of enablement services (e.g., technical, marketing, business development, sales, training) to help organizations reap the measurable economic benefits that can be achieved from successful managed services implementations. Channel partners tell Forrester that the two standout services are to:

- **Center your enablement program on technical training.** As technical services become increasingly sophisticated and specialized, the No. 1 value for service channel partners has become technical training (see Figure 4). Vendor channel professionals should provide in-person and online workshops led by technical experts to help channel partners build knowledge in solution areas across the managed services domain (e.g., remote management, security services, backup/recovery services). Technical conferences, webinars, videos, podcasts, virtual training, and one-on-one consulting are also popular training mediums to explore. Cisco Systems, IBM, and Microsoft offer some of the best technical training programs in the industry today.

- **Offer to manage/maintain an online application store on a partner’s behalf.** Vendor-sponsored app stores are the second largest channel for sourcing software of companies with fewer than 100 employees, which is a core customer-size class for MSPs. The importance of vendor-sponsored app stores is even more influential when you consider that just two years ago, app store on-premises software sales only represented half this figure. Naturally, MSPs want a piece of this bottleneck growth (and revenue opportunity) and are looking to tech vendors to manage or maintain online application stores or marketplaces on their behalf.⁹ After listening to the needs of its partner community, SAP revamped its vendor-sponsored app store in 2012 — and made it the relatable and attractive “Amazon-like” shopping experience partners requested — to win the support of its burgeoning managed services and cloud partner community.

Figure 4 Channel Partners Seek Wide-Ranging Enablement Support



Base: 104 channel professionals at companies with 10 or more employees (three responses accepted)

Source: Q4 2012 US And European Channel Partner Business Model And Loyalty Online Survey

90001

Source: Forrester Research, Inc.

WHAT IT MEANS

THE CHANNEL “IT IS A-CHANGIN’”

A lot of traditional reseller channel partner companies are now utilizing cloud computing advances to add to or remake their businesses — as hosters, integrators, syndicators, and service providers. Gone are the days when tech vendors can view the channel with a siloed eye. “Hybrid” is the new norm, as it applies to channel partners’ business models — and tech vendors and channel partners are going through a lot of relationship re-engineering, both with each other and with their mutual customers.

1. **For VARs transmogrifying to cloud solutions providers.** They are on a path to success, because they can give customers what they want: options regarding technology solution deployment/consumption models. The keys for them will be to: a) bolster their technical skills with financial modeling skills, and b) get savvy on hybrid cloud integration.
2. **For VARs refusing to embrace cloud — R.I.P. (rest in peace).** Without some stake in cloud solutions, their businesses are going to decline and lose value. Hardware resellers are particularly vulnerable.
3. **For SIs.** They will prosper by filling the void left by VARs that are not making net new investments in cloud-oriented professional services.
4. **For MSPs/CSPs.** Many are proving, from the other end of the spectrum (services versus resell), that hybrid is the new norm, by adding traditional resell to their business models. They will also be aggressive on the investment front in adding new services to their portfolios, as the number of MSPs/CSPs continues to increase.
5. **For distributors.** Some are searching for the right formula that will make them as successful as service provider enablers as they have been reseller enablers. But they face a new slew of competitors in the form of the telcos and service-provider technology platform enablers (Level Platforms, Kaseya, Parallels IP Holdings, SaaS MAX, Verecloud, etc.).
6. **For SaaS vendors.** Software-as-a-service (SaaS) vendors in particular need to realize that there now exists a willing and increasingly capable channel for cloud solutions and that many customers are going to prefer to continue to source from their trusted advisors (i.e., channel partners). For those that haven't done, the time is right for an amalgamated direct/channel go-to-market model.

SUPPLEMENTAL MATERIAL

Methodology

Forrester's Forrsights Software Survey, Q4 2011, was fielded to 2,438 IT executives and technology decision-makers located in Canada, France, Germany, the UK, and the US from small and medium-size business (SMB) and enterprise companies with two or more employees. This survey is part of Forrester's Forrsights for Business Technology and was fielded during November 2011 and December 2011. LinkedIn Research Network fielded this survey online on behalf of Forrester. We have provided exact sample sizes in this report on a question-by-question basis.

Each calendar year, Forrester's Forrsights for Business Technology fields business-to-business technology studies in more than 17 countries spanning North America, Latin America, Europe, and developed and emerging Asia. For quality control, we carefully screen respondents according to job title and function. Forrester's Forrsights for Business Technology ensures that the final survey population contains only those with significant involvement in the planning, funding, and purchasing of IT products and services, those who use a PC or smartphone at work for at least 1 hour per day, and those with direct oversight of their team's or group's budget. Additionally, we set quotas for company size (number of employees) and (industry, job function) as a means of controlling the data distribution (and establishing alignment with IT spend calculated by Forrester analysts). Forrsights uses only superior data sources and advanced data-cleaning techniques to ensure the highest data quality.

We have illustrated only a portion of survey results in this document. To inquire about receiving full data results for an additional fee, please contact forrsights@forrester.com or your Forrester account manager.

Forrester's Q4 2012 US And European Channel Partner Business Model And Loyalty Online Survey was fielded to 265 channel professionals located in the US, France, Germany, and the UK at SMB and enterprise companies with 10 or more employees. Exëvo fielded this survey online in November to December 2012 on behalf of Forrester Research via its online panel of channel partners. Survey respondent incentives included a choice of cash, research time, and/or a summary of the research results. We have provided exact sample sizes in this report on a question-by-question basis.

In addition to sampling error, one should bear in mind that the practical difficulties in conducting surveys can introduce error or bias into the findings of opinion polls. Other possible sources of error in polls are probably more serious than theoretical calculations of sampling error. These other potential sources of error include question wording, question ordering, and nonresponse. As with all survey research, it is impossible to quantify the errors that may result from these factors without an experimental control group, so we strongly caution against using the words "margin of error" in reporting any survey data.

We have illustrated only a portion of survey results in this document. For more information about this data, please contact inquiry@forrester.com.

ENDNOTES

- ¹ For more information about why there continues to be a cacophony of marketing noise from technology vendors about their cloud strategies, while the announcements sometimes include messaging for their channel and many partners are still unsure of their future role in the industry, check out Peter O'Neill's — a Forrester Research analyst's — blog post. Source: Peter O'Neill, "The Tech Industry Channel Is Cloud-Confused; Colt Technology Services Is Well Into It," Peter O'Neill's Blog, October 25, 2012 (http://blogs.forrester.com/peter_oneill/12-10-25-the_tech_industry_channel_is_cloud_confused_colt_technology_services_is_well_into_it).
- ² This affects not only the channel partner company but also the partner company's salespeople's commissions.
- ³ Source: Forrsights Software Survey, Q4 2011.
- ⁴ For more information on how tech vendors can harness the revenue potential of MSPs through a new makeup, service offerings, market fluctuations, competition, business models, and delivery modes, see the May 9, 2012, "[Market Overview: Managed Service Providers, Part 1](#)" report.
- ⁵ Source: Q4 2012 US And European Channel Partner Business Model And Loyalty Online Survey.
- ⁶ IBM is offering MSPs financing options through IBM Global Financing (IGF). MSPs can now acquire new technology solutions and services with payment plans including 12-month 0% loans for IBM systems, storage, and software. MSPs also have the ability to access IBM-certified preowned systems and storage solutions. Furthermore, IBM is offering trade-in credit to end users for no-longer-needed equipment.
- ⁷ Source: Q4 2012 US And European Channel Partner Business Model And Loyalty Online Survey.
- ⁸ For a deeper dive into enablement programs and support, see the January 14, 2011, "[Channel Partners' Needs In The Era Of Cloud](#)" report.
- ⁹ Source: Forrsights Software Survey, Q4 2011.

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