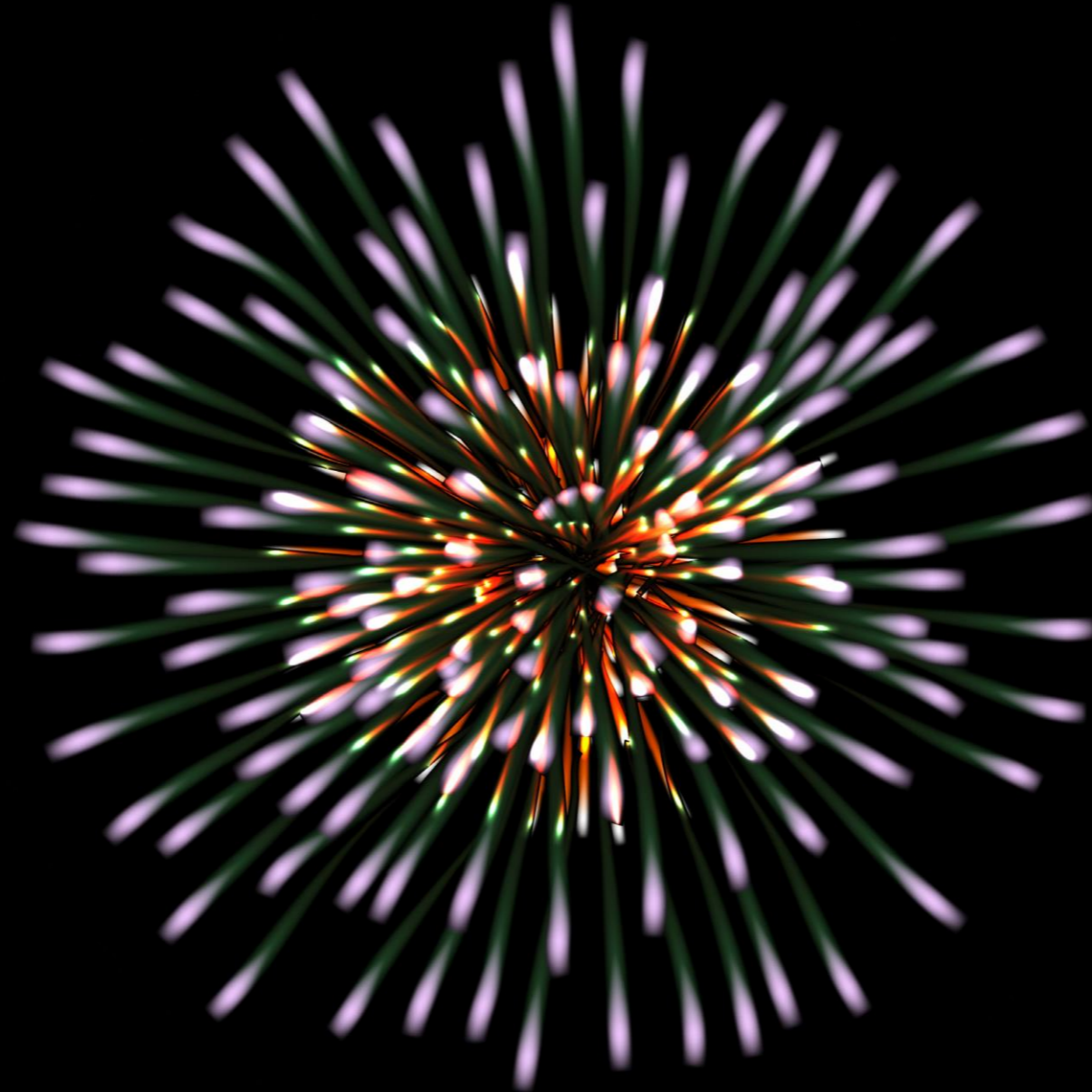


**Deloitte.**



# **Subscription business models**

Driving growth through the right pay-per-use business models

# Transitioning to consumption-based models requires more than answering a few high-level questions about your business

Companies in the technology, media, and telecommunications (TMT) industry are undergoing profound shifts in how they sell and deliver their products and services.

Increasingly, customers are demanding that they be able to consume offerings—from media content to technology infrastructure and enterprise software solutions—in a flexible, scalable, and secure manner. Customers want to be able to choose where, how, and how much they consume and pay for.

Flexible consumption requires an entirely new business model that fundamentally alters how products and services are sold and to whom.

Moving to a pay-per-use business model may call for changes to business capabilities, operating models, and enabling technology platforms. In order to make the transition from a more traditional

model, executives first need to determine what this “new” business model should look like. It all starts with understanding where you are currently—and then determining where you need to be in order to respond best to customer requirements and market shifts.

However, getting that level of clarity requires more than asking whether it’s time to switch to a subscription model or to start unbundling your current offerings. You need a clear understanding of how your industry is evolving, where competition is most likely to surface, and where disruption could happen. Then you need to kick the tires on every aspect of your future business model to make sure it’s going to get you where you want to go.

Difficult? Yes. Worth doing? Absolutely.

# Key observations



## What will we sell? Offerings, packaging, and delivery get a makeover:

Technology companies are quickly moving into the more complex territory of selling solutions—a combination of hardware, software, and services.



## To whom will we sell? Appealing to empowered buyers:

As companies reconfigure their products and services, it presents an opportunity to sell to other customers they may not have actively served in the past.



## How will we sell? Changing roles for sales and channel partners:

Companies need to decide what role they want partners to play in the future and how that role will change.



## How will we monetize? Sorting through the options to generate value and maximize revenue:

Deciding on an appropriate model depends on a number of factors, including: industry, product or service offering, the company's risk appetite, competitive landscape, and customer preferences.

# What will we sell ? Offerings, packaging, and delivery get a makeover

Technology companies are quickly moving into the more complex territory of selling solutions—a combination of hardware, software, and services. Companies in other businesses such as industrials, automotive, and medical devices are increasingly shifting to technology and software-driven offerings. Advances in cloud-based computing have also increased both the feasibility and the attractiveness of hosted solutions, in an as-a-service model. These trends are quickly changing the nature of offerings that companies bring to the market.

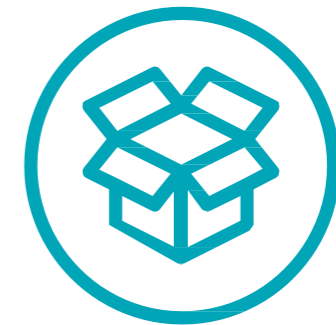
The Internet of Things (IoT) is a compelling example of a rapidly growing market that is forcing companies to seek flexible consumption business models as a way to stay competitive. Consider a company that once had a business model selling \$2 lightbulbs. The company may now sell a smart lighting system that offers consumers the ability to control the lighting in their connected homes through a smartphone or wearable device app. The company may also offer 'lighting as a service' solutions to enterprise, commercial, and public sector customers such as cities to manage every

light point across their network. This has the potential to totally transform how the company conducts its business.

For most companies, the challenge is to figure out what portfolio of offerings will be most compelling to customers under a flexible consumption model. Generally, they will need to make this determination on a product-by-product basis, based on customer needs and competitive offerings.

As offerings become more software and data-driven, companies may have to set up entirely new channels and partnerships to take them to market. They also need to think about how the offerings would be delivered: Will they take the form of physical or digital goods or both? Will the software/services be hosted on the customer's premises or in the cloud? Should the company invest in building its own cloud infrastructure or host the solution via a third-party provider? Software companies may want to consider offering cloud-based flexible consumption solutions, while retaining their traditional models for customers that prefer to continue to consume the product in that way.

Packaging is also important because it provides customers with the configurability and scalability they need for flexible consumption. Companies are packaging a combination of hardware, software, and services to more effectively cater to customer needs and deliver value. Packaging has become a core focus for the media industry, where bundling and unbundling of content has taken on a new meaning. While some media and entertainment companies are unbundling content packages, others are offering customers the option to configure their own offerings by picking and choosing cable and streaming over-the-top (OTT) channels to accommodate their personal viewing tastes.



Technology companies are quickly moving into the more complex territory of selling solutions—a combination of hardware, software, and services.

# To whom will we sell ? Appealing to empowered buyers

Many businesses, particularly in the software and hardware space, have been selling to specific customer segments and enterprise buyers for years. As they reconfigure their products and services to offer more flexible consumption options, it presents an opportunity to sell to other customers they may not have actively served in the past. For example, large enterprise information technology (IT) vendors are accustomed to selling multi-million dollar software implementations to corporate IT departments of major corporations. Now, with the move to flexible consumption, customers can pay as they go for cloud-based services; they no longer need to shell out large amounts of money up front for licenses and on-premise installations or upgrades.

They can create on-line accounts and sign up for specific services without the need for major vendor involvement.

This creates a far broader universe of potential clients for solution providers. For instance, a pay-as-you-go model fits within the smaller budgets of business-unit IT departments, and increasingly these groups are making purchase decisions about software that meets their specific needs. Small-to-medium-sized businesses are also within reach. With the simple self-service, no-touch model that characterizes flexibly consumed cloud solutions, providers can sell more cost effectively to these smaller customers.



As companies reconfigure their products and services, it presents an opportunity to sell to other customers they may not have actively served in the past.

# How will we sell? Changing roles for internal sales and channel partners

Expanding to a broader range of customers raises questions about the role of a company's existing sales force, as well as its channel partners. Many companies have traditionally sold through channel partners because they may not have the infrastructure or the internal sales force coverage to sell to thousands of enterprise, commercial, and small-to-medium business clients. If those same companies begin selling directly to customers, or offering their solutions to customers on-line, this could cause friction with channel partners that feel they are being cut out of the equation.

Companies need to decide what role they want partners to play in the future and how that role will change. They need to look for ways to keep partners engaged and incentivized to sell their products and services. The same logic pertains to an internal sales force, which may have to be reorganized to sell flexible consumption offerings. Companies also need to think about how to tailor sales compensation and align sales incentives with the recurring revenue model for flexible consumption—otherwise they may find their new offering fails to gain traction with the sales teams and consequently with customers.



Companies need to decide what role they want partners to play in the future and how that role will change.

# How will we monetize? Sorting through the options to generate value and maximize revenue

Flexible consumption models come in a wide range of flavors, from subscriptions to pure pay-per-use (see sidebar). Deciding on what model is most appropriate depends on a number of factors, including the industry, the product or service offering, the company's risk appetite, the competitive landscape, and customer preferences.

Companies have to think about what model will help them address customer needs while maximizing revenue. If there is an expectation that customers will keep increasing their consumption of the service, for example, then offering a fixed subscription for unlimited content may leave money on the table. Transitioning to another type of monetization model can be difficult once customers become used to an unlimited offering.

Revenue risk is another important consideration. When companies transition from their traditional sales model to a flexible consumption model, they are usually moving from a fixed to a recurring revenue stream.

One benefit of recurring revenue is that it

is fairly predictable. But in some cases—for example, with the cancel-anytime incentives used to entice customers—a certain amount of revenue is at risk, and this needs to be incorporated into revenue projections.

Pay-per-use models are less predictable than subscriptions, and are often subject to such factors as seasonality.

Another potential revenue risk occurs when consumers start as heavy users and then drop off. Companies that move to flexible consumption models need to stay consistently relevant and imbue their offerings with market-leading features to drive continued customer adoption and usage.

Interestingly, one accounting development has made this an opportune time to revisit go-to-market strategies: the new accounting guidance for revenue will be judgement-based rather than rules-based, which may allow entities to bundle or price offerings in ways that previously might have resulted in an inability to recognize revenue separately for each offering.

## Examples of Monetization models

**Unlimited subscription:** Subscription plan with unlimited quantity, features, devices, etc. for a set period

**Predefined subscription:** Subscription with access to a specified quantity of the product or features for a pre-defined period, generally with a minimum commitment

**Subscription plus overage:** Subscription with access to a predefined amount for a specified period, with any overage billed based on actual usage

**Freemium:** Access to basic services for free, while charging a premium for advanced or special features

**Consumption-based:** Monetization on a pay-per-use basis, generally with no minimum purchase or commitment

**Outcome-based:** Monetization based on value delivered to the customer, measured as quantifiable outcomes

# Let's talk

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