



CANADIAN
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The Dynamics of the Canadian IT Market, Cloud Adoption Rates, and the Status of the Channel

November 1, 2016



The following research report was jointly funded by the Canadian Channel Chief Council (C4), C4 member organizations, and the Ontario Centre for Excellence TalentEdge Internship Program. Research and analysis was conducted by Ryerson MBA student, Alex D'Alfonso, and supervised by Professor Ron Babin, Ryerson University, and Brendan Rouse, IDC.

EXECUTIVE SUMMARY

With the advent of cloud technology, many markets across the globe have seen significant disruption across multiple industries. Based on interviews with numerous channel chiefs, Canada has been identified as a particularly nuanced market as there are a number of factors that are unique to the Canadian channel in terms of drivers and inhibitors to cloud adoption, decision making, and vertical adoption.

The Canadian market generally lags behind other developed markets, particularly the United States, in cloud adoption. There are however, a number of indicators that the Canadian transition to the cloud is a matter of 'when, not if', with the expectation that the gap in acceptance will close within the next five years. Cloud is expected to grow across a wide range of verticals, with industries such as financial services and public sector leading the next phase of cloud growth, initially focusing on non-critical business units for large organizations.

The Canadian market appears to be unique due to the high proportion of small and medium-sized businesses, which make up over 99% of the total number of active businesses in Canada. This, combined with the perception of a regulated environment regarding data sovereignty and governance, indicates that Canada is a unique market that cannot be catered to in the same manner as other developed markets, such as the United States. While small and medium-sized organizations make up a large proportion of the total number of potential users, large businesses still make up a majority of the total IT spend, and vendors approach selling the cloud with a focus on the enterprise segment.

A majority of those interviewed have identified regulatory requirements as a major inhibitor to cloud adoption in Canada as there is a focus at many organizations on large businesses (500+ employees) which would be subject to government regulations. These perceived regulatory limitations have been found to be over stated, and can be overcome with an emphasis on education and understanding of the conditions organizations are facing. Interview participants identified Canadian enterprise clients as particularly risk averse and unwilling to commit to a completely cloud-based strategy, instead opting for a hybrid approach. In the near term, small and medium-sized businesses have shown a tendency to adopt a purely cloud strategy, and as such can be targeted specifically as areas to drive cloud growth.

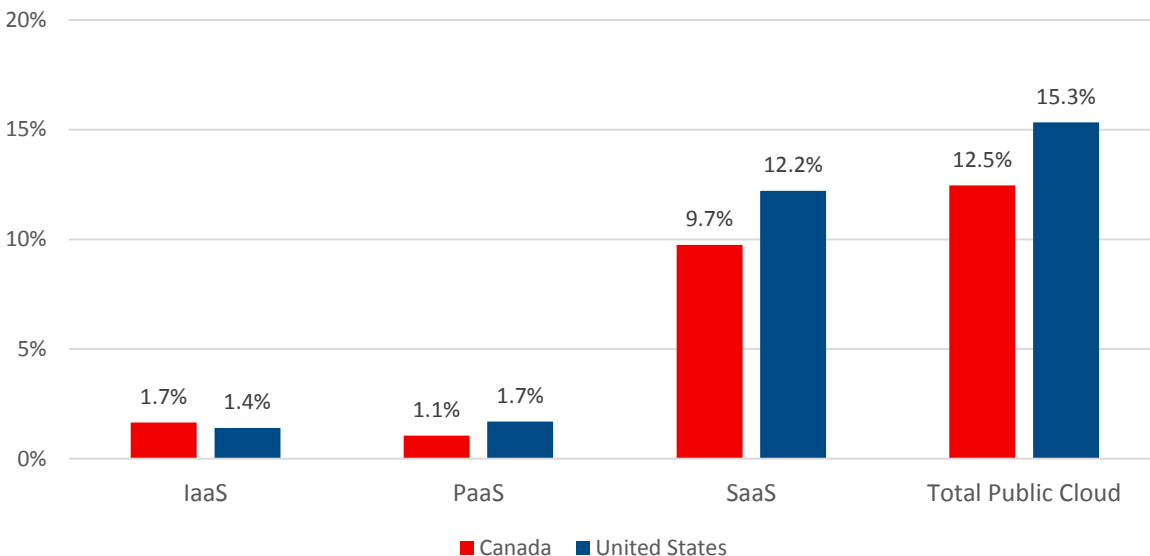
All aspects of the distribution channel are expected to be affected by the cloud, as distributors and solution providers focus on growing competencies around innovation and the cloud in particular. Canada's limitations regarding market size have made it difficult for firms to offer highly specialized services, and instead sell more generic offerings to maintain revenue growth. Distribution intermediaries must work with technology vendors to continue to further develop market relevance. They must focus on educating potential end users and identify the specific needs of customers as well as the complex business requirements of vendors to offer a highly specialized and customizable product that benefits all aspects of the distribution channel.

CANADIAN IT MARKET

The Canadian market has many unique factors regarding market size, overall spend, and various customer segments in addressing cloud adoption and channel partnerships. Proportionally, the total Canadian IT spend lags behind the US market when compared to other industry segments. The difference in spend is further underscored when looking at the cloud. As can be seen in Figure 1, public cloud spending represents a far lower proportion of total IT spend in Canada than in the United States.

FIGURE 1

Public Cloud Revenue as a Percentage of Overall Infrastructure and Software Spending



Sources:

Cloud Revenue: Worldwide and Regional Public IT Cloud Services Forecast, 2015-2019 (IDC #US40709515)

Overall IT Spending: Worldwide Black Book V2, 2016 (IDC #US41686816)

This contrast between geographic markets bears a close relationship with the prevailing sentiment regarding Canada's classification as a laggard by the majority of interview participants. Canada's identification as a laggard could be due to a number of factors. Some interview participants identified a lack of cloud infrastructure as a leading cause for cloud's slow rate of adoption in Canada; other causes listed include a more risk averse end-user community, as well as a generally slower decision-making cycle among IT buyers.

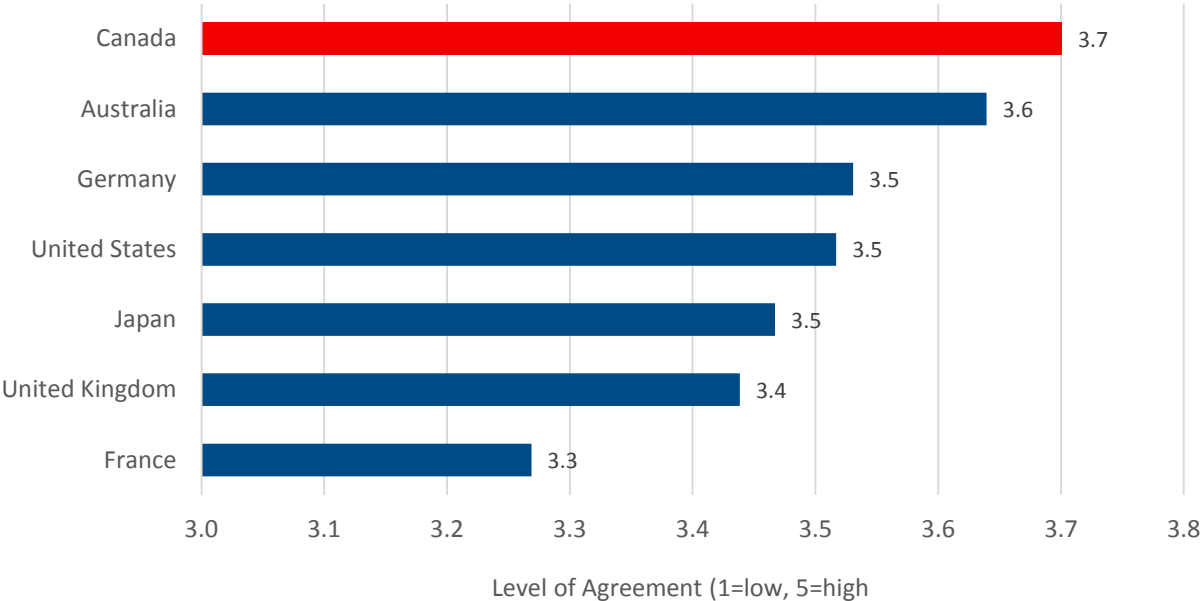
The lack of cloud infrastructure in Canada has historically been a deterrent to cloud adoption. However, recent commitments by major cloud providers and trusted brands such as Amazon Web Services (2016) and Microsoft (2016) to growing cloud offerings in Canada, are expected to help drive cloud adoption across multiple customer segments. Despite Canada's classification as a laggard in cloud adoption, a number of factors suggest that the gap in cloud adoption will narrow in the near future. The observations of C4 interview participants, the sentiment among Canadian IT buyers, and the measure of uptake in current and projected cloud spending, all point to strong Canadian cloud growth.

According to IDC's Cloud Adoption Global Benchmark Survey, IT decision makers in Canada indicate that the cloud is the long-term platform of choice, ahead of all other surveyed markets (see Figure 2).

FIGURE 2

Public Cloud as the Long-Term Platform of Choice

Q. My organization views Public Cloud as our dominant, long-term platform strategy for meeting IT needs. (1 - Strongly disagree, 5 - Strongly agree)

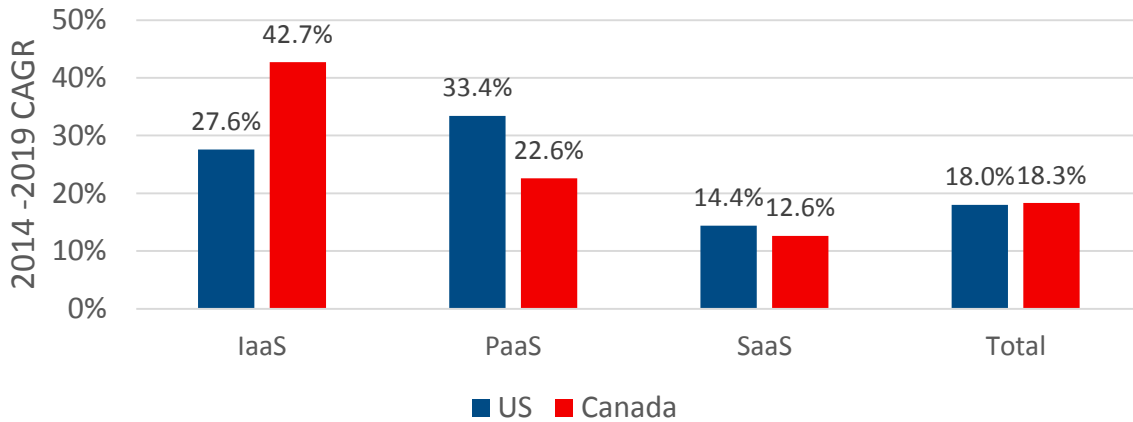


Source: IDC Cloud Adoption Global Benchmark: The State of Cloud in Canada (IDC #CA40623016)

Additionally, IDC forecasts stronger growth in Canadian cloud adoption when compared to the United States (see Figure 3). This narrowing of the adoption gap will be largely driven by adoption of infrastructure-as-a-service. Based on interview and survey responses, as well as forecasts, it can be surmised that the cloud will be a significant driver of IT spending growth in the near future in the Canadian market.

FIGURE 3

Public IT Cloud Services 2014-2019 CAGR (%) by Category

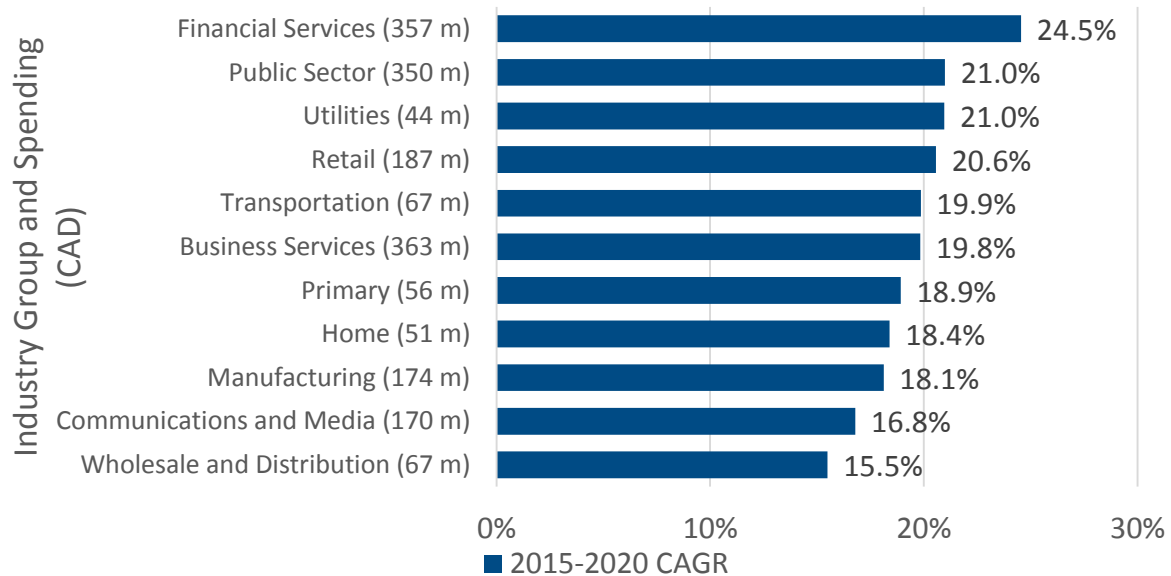


Source: Worldwide and Regional Public IT Cloud Services Forecast, 2015-2019 (IDC # US40709515)

Regarding cloud adoption by vertical, interview respondents identified financial services and the public sector as the two industry verticals most likely to see an acceleration in cloud adoption going forward. However, a wide array of industries, including manufacturing, healthcare, energy, and telecommunications were raised as possible verticals that will benefit from further cloud adoption. A current IDC market model supports these expectations, indicating expected cloud growth across all measured verticals, with financial services and the public sector leading the way (see Figure 4).

FIGURE 4

Public Cloud Growth by Industry Group



Source: IDC Market Model, 2016

Despite proportionally low IT and cloud spend when compared to the United States, the Canadian cloud market is expected to see a significant uptick in cloud adoption thanks to commitments by major global cloud providers and expected development of cloud infrastructure across Canada. Although Canada has been identified as a laggard regarding the cloud, survey data indicates that Canada's sentiment towards long-term acceptance of the cloud is positive. Additionally, interview results regarding expected industry vertical uptake align closely with survey results, indicating financial services and the public sector as the industry verticals most likely to see significant growth in the near future.

BUYER BEHAVIOUR

A number of drivers and inhibitors must be taken into consideration when selling and customizing cloud solutions for the Canadian market. Interview respondents identified cost as the most significant driver towards adopting cloud solutions over traditional on-premise infrastructure by a wide margin. All interview results aligned closely with IDC end-user survey results looking at cloud drivers. Figure 5 indicates drivers of adoption, ranked by frequency of response.

FIGURE 5

Cloud Adoption Drivers

Rank	C4 Findings	CloudView Survey (Public Cloud)
1	Cost	Reduce the total size of IT budget
2	Redistribution of IT resources	Improve IT staff productivity/redeploy IT personnel for other business processes
3	Scalability	Improve time to market
4	Speed to market	Improve resource utilization
5	Customization	Support business, marketing or other business related programs
6	Quality	Improve our internal service delivery levels and business agility

Source: Ryerson/IDC C4, 2016, n=11; CloudView Banner Book, 2016, n=72

In addition to cost, organizations are looking to increase efficiency by redistributing their IT resources across other processes to improve productivity. Although interview results indicate a wide number of drivers, the top two drivers were by far the most frequently cited. This indicates a need among organizations to better control their IT costs and increase efficiency.

Regarding inhibitors, it may seem counterintuitive to see cost as both a significant inhibitor and a significant driver of cloud. When asked for clarification, interview respondents that cited cost as an inhibitor explained that, since costs associated with the cloud are typically generated through usage or consumption, there are many scenarios in which transitioning to the cloud could prove to increase costs rather than reduce them, especially over an extended time horizon. Other major inhibitors can be seen in Figure 6.

FIGURE 6

Cloud Adoption Inhibitors

Rank	C4 Findings	CloudView Survey (Public Cloud)
1	Regulation	Security concerns
2	Security	Reliability concerns in terms of service availability (response time & user downtime)
3	Cost	Worries that our network infrastructure (routers/switching/ bandwidth) limits our use of the on-demand model
4	Privacy	Loss of operational control
5	Complexity	We don't have the IT skills to implement Private Cloud, or manage Public Cloud services
6	Lack of skills	Vendor lock-in
7	Lock-in	Hard to integrate with in-house IT systems and management
8	Performance	Will cost too much to change to or build Cloud services to be worth the benefit

Source: Ryerson/IDC C4, 2016, n=11; CloudView Banner Book, 2016, n=72

Many inhibitors indicated in interview findings are related to a fundamental lack of cloud awareness among Canadian buyers. In many cases, outcomes related to the above list of concerns would be improved by implementing cloud-based solutions. As awareness builds, the headwinds that have dampened cloud adoption in Canada will subside.

Based on C4 interview findings, regulation was the top inhibitor, but ranked outside of the top six inhibitors in IDC's end-user survey. IDC research indicates that data residency regulation varies across provinces and industries (a full list of impacted verticals can be found in the appendix of this report). The most significant regulatory issues regarding data residency appear in provincial government as well as healthcare, where the privacy and security of data plays a significant role in limiting the viability of public cloud.

Although regulation was emphasized in the interviews as a major impediment to adoption, and likely aligns closely to buyer sentiment, the legal and regulatory limitations imposed on the transmission and storage of data appear to be overstated. In support of this finding, one interview respondent cited 'the perception of regulation' as the barrier to cloud adoption, rather than the actual terms to regulatory oversight. The broad-based view that regulatory concerns impede cloud adoption is correct, yet the frequent misinterpretation of such covenants on behalf of the buyer must be stressed.

Interview results also indicate that Canadian buyers engage in a longer decision-making cycle than their American counterparts. This lag in decision making is compounded when Canadians are faced with the decision to transition to the cloud. IDC research shows that the median Canadian sales cycle is approximately three months, which lags slightly behind American counterparts. While a longer sales cycle is not necessarily indicative of weaker sales capabilities, based on interview feedback surrounding drivers and inhibitors, the longer sales cycle could be attributed to a lack of knowledge and understanding regarding the risks and benefits of the cloud, indicating a need for education and knowledge sharing.

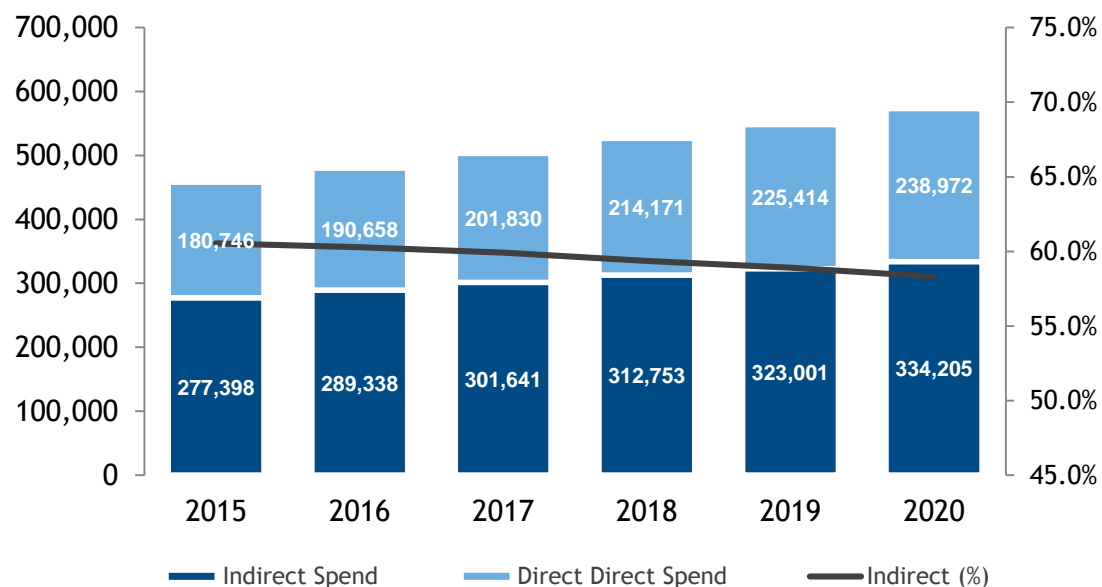
PARTNER ECOSYSTEM

Interview respondents indicated an existing and growing significance on the channel, whereby over 85% of respondents stated that indirect selling represented over 50% of their total revenue. In multiple cases respondents indicated that all new business is funneled through the channel. This shows that cloud computing has not reduced the channel's value-add, and instead has spurred a growing need to offer more comprehensive and specific solutions to users that leverage cloud's inherent customizability and agility. Although cloud delivery has affected the need for traditional distribution capabilities, sales and relationship management capabilities are growing in importance due to the proven need to drive education among the end-user community in Canada.

As seen in Figure 7, North American software and hardware indirect spending actually appears to be declining slightly. This is largely due to the growing segment of original design manufacturers (ODM) selling directly into hyperscale web farms, rather than a decreased emphasis on the channel by major vendors. Overall, both indirect and direct spending are increasing, but the expansion of public cloud offerings is fueling the growth of ODM direct sales, and slowly eating into the indirect share of spending. Although there is variation across the various hardware and software segments in terms of the revenue share that goes through the channel, the indirect-direct splits are expected to shift only modestly over the next five years. What is more pressing, for both vendors and the channel, is overall spend trends within the technology segments (e.g., the overall growth in demand for x86 servers or the rapid decline desktops PCs).

FIGURE 7

North America Software and Hardware Direct/Indirect Spending 2015-2020 (\$M)



Source: IDC, 2016

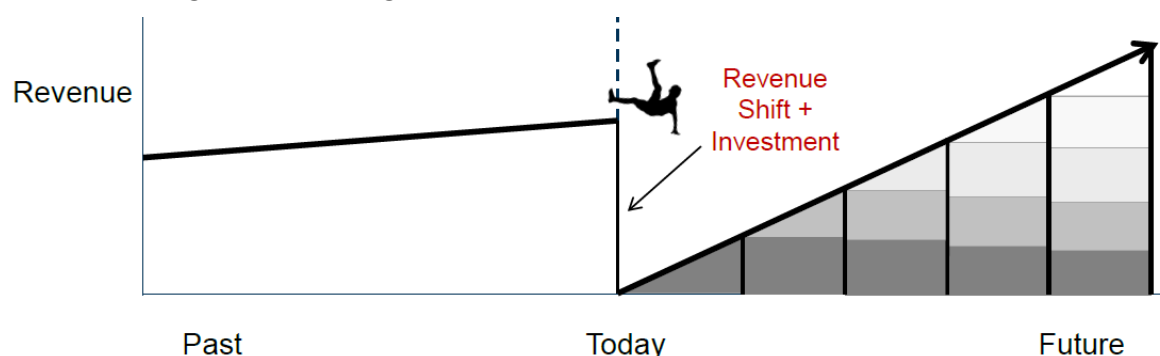
When considering the channel sentiment towards recurring billing, almost all interview respondents indicated generally positive feedback. The interviewees indicated that both partners and end users typically prefer a transition away from high up-front cost capital expenditures. Although responses were generally positive, the negative implications primarily focused on two areas. The typically slow decision cycle among Canadian buyers is further slowed due to the increased complexity of solutions, taxing the available time and resources of partners. Additionally, these channel partners need to further develop

cloud implementation skills. Additionally, channel partners' sales strategies appear to be only partially aligned to cloud offerings, primarily due to confusion regarding sales compensation strategies. All sales organizations must align sales compensation with the transition towards long-term recurring revenues.

Despite the generally positive response alluded to by interview respondents, it is important that vendors maintain awareness of the potential challenge faced by partners transitioning to cloud business models, particularly among smaller partners. Figure 8 visualizes the potential shift in revenue stream as a result of the move towards recurring revenue. In addition to incenting the salesforce, partners must also drive usage and consumption, develop new delivery capabilities around cloud, and grow recurring revenue streams at a rate that mitigates a possible cash crunch in the absence of large up-front fees. Vendors must help the ecosystem along this journey by providing guidance around finance, sales, and delivery capabilities to help partners overcome these obstacles.

FIGURE 8

Transitioning to Recurring Revenue



Source: Canadian Channel in the Cloud: Learning from Success and Failure, (IDC #CA41630216)

PARTNER PROGRAMS

While some channel programs allow for specific flexibility in the Canadian market, all programs share a framework with larger markets. Typically, Canadian partner programs share the same frameworks as their US counterparts with lower tiers to address the smaller Canadian market. The general sentiment is that these lowered tiers are often still too high to deal appropriately with the unique Canadian market, which differs from the United States in terms of customer size, relative IT spending, and current cloud penetration. Respondents with greater autonomy around partner program attributes and formal mechanisms to escalate issues, were generally more optimistic in terms of program effectiveness.

In order to appropriately leverage partner programs in the market, a number of factors must be considered. Previous US-oriented research on the channel indicates that the top three reasons for partners to engage with vendors as their primary hardware brand are:

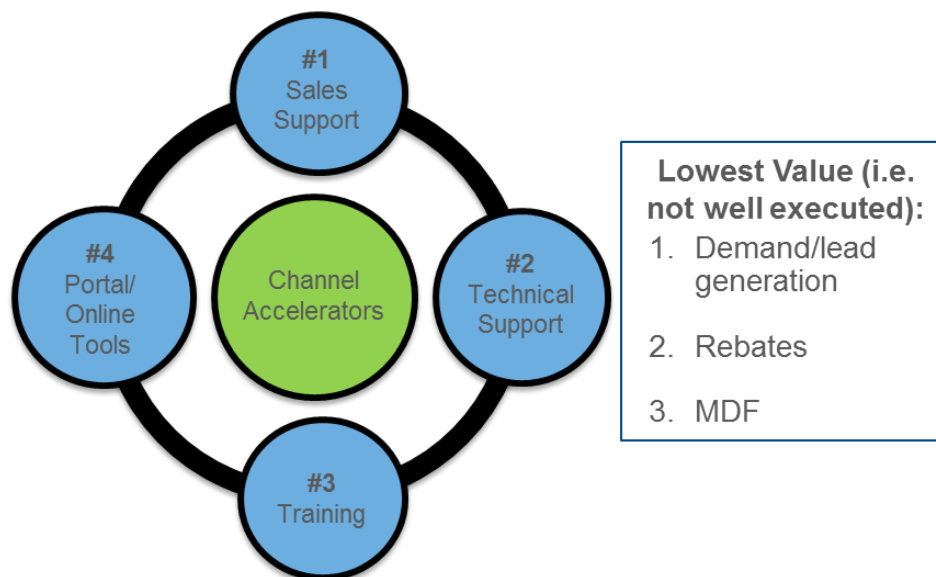
1. Technology
2. Market/Customer Demand
3. Ease of Doing Business

Additionally, as seen in Figure 9, the value of partner programs is derived from a number of influences. Currently, the highest value factors include sales support, technical support, training, and online tools. These are considered high value because they are both useful to partners and are well executed by vendor organizations. IDC research has also found that the lowest value (not well executed) channel factors are demand generation, financial rebates, and market development funds. These findings indicate potential areas on which to continue to focus in order to drive value, or areas that need improvement to provide more holistic value across all features indicated by channel partners. Again, the above findings

are based on research oriented around US-based channel partners, and may not reflect the sentiment of the Canadian channel.

FIGURE 9

Channel Valuation of Partner Program Attributes



Source: IDC, 2016

VENDOR GUIDANCE

In analyzing the interview responses, a number of common themes appeared over a majority of responses. There are three key findings from the interviews:

- Unique market factors in Canada impact cloud adoption, and the future outlook for cloud adoption is strong.
- Many cloud adoption inhibitors are related to a lack of knowledge or capabilities around cloud technologies.
- Expected ongoing importance of channel distribution partners.

These key areas indicate that, although cloud is having a major impact on a large proportion of Canadian businesses from an operational perspective, there is a lack of understanding regarding how best to leverage the disruptive technology from both a supply chain and sales perspective. In many cases, interviewees identified specific gaps in their knowledge and were looking for help. Essential guidance includes taking steps to measure and improve overall cloud maturity across the channel, shorten the sales cycle, and define the impact of regulation and privacy law for end users.

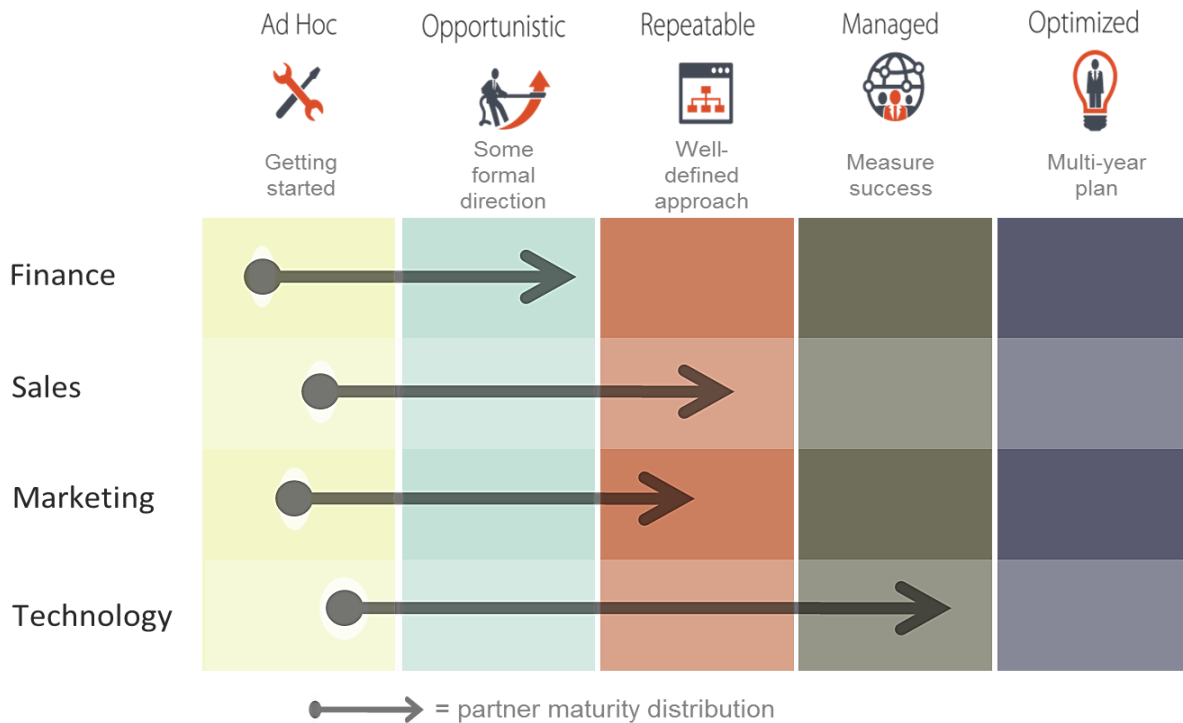
1) Play an active role in advancing cloud maturity in the channel

Partner cloud maturity is highly correlated with both top-line and bottom-line revenue growth. It is therefore important to continue to help advance the channel along a number of areas of partner maturity, including training and assistance on cloud technology, rethinking financials and investments, marketing, and selling cloud. As seen in Figure 10, the Canadian channel is most advanced in its approach to the technology side of cloud, but there is significant opportunity for development across marketing, sales, and especially finance. The bulk of Canadian channel partners lie in the Ad Hoc and Opportunistic stages in

the finance domain, suggesting that the challenges faced when transitioning to recurring revenue may impact many organizations in the partner community.

FIGURE 10

Channel Cloud Maturity in Canada



Source: IDC, 2016

Channel maturity can be facilitated through open lines of communication, monitoring and development of KPIs, and comprehensive development paths for both vendors and partners. It is important to participate in partner listening and understand which partner program attributes help drive business in the Canadian partner ecosystem (remember the high-value program attributes in Figure 9 are specific to US research). Vendors and partners must work together to identify the attributes that are found to be highly valuable, and which attributes require improvement.

2) Shorten sales cycles through education and marketing attempts

As discussed, the decision making cycle among Canadian IT buyers is slightly longer than in the United States. The longer cycle is not necessarily indicative of poor sales performance, but channel partners (and vendors) can employ a number of strategies to help shorten the sales cycle improve the efficacy of a sales team. These four recommendations, which appear obvious in many ways, map to a few critical buying trends in today's market:

1. Invest in marketing
2. Focus on business outcomes
3. Sell solutions that are easy to buy
4. 'Land and expand'

Line-of-business (LOB) is included increasingly in the IT buying decision, and decision makers are investigating solutions online and are much further along the sales cycle before engaging with a salesperson. Rich digital marketing material is essential to reach buyers who self-educate online. Case

studies geared toward a target market are a good start. Many buyers are looking beyond technical specifications with business outcomes in mind, and this is especially important if LOB is your audience. Not only should marketing material be geared towards specific business outcomes (e.g., increasing revenue, decreasing costs), but salespeople should be equipped to have these conversations with LOB managers too.

"Each cloud implementation is an interview for the next piece of business"

Camillo Speroni, Oracle

Part and parcel of the cloud deal is recurring revenue, usage-based consumption, and an ongoing relationship with the customer. Many high performing partners have met with success by first focusing on securing an account, and then later identifying ways to add value to the customer by expanding the offering. Leading the sales effort with a small, easy to buy solution is an effective way to initiate a relationship. Clearly defined solutions, those that lead to very predictable and measurable outcomes for the customer, make it easy for the decision maker to say 'Yes'. After delivering on the first implementation, partners should look for new opportunities to add value in the account.

These four recommendations hang together the help shorten the sales cycle, both at the front end and at the back end of the transaction. Rich digital marketing that speaks to business outcomes bring the buyer further along the purchasing cycle before engaging a salesperson. Small, well defined offerings simplify and help close the deal earlier, and with a perpetual relationship, the door to later expand the account remains open.

3) Overcoming regulatory concerns

The regulatory environment in Canada poses both real and imagined barriers to cloud adoption. Because regulation and privacy were raised as key inhibitors to cloud adoption, overcoming the perceived barriers has high upside potential. Based on existing IDC research, data sovereignty and privacy are considerations that play a larger role in decision making than they probably should. It appears that the cautious Canadian has adopted many of the provincial or federal restrictions imposed on the public sector and healthcare industry.

To overcome these inhibitors, vendors must help equip the partner ecosystem to manage regulatory related objections to cloud. Vendors with a stake in partners selling and delivering cloud solutions should explore data limitations by province and industry. Similarly, if your solutions sets are built around traditional on-premise, private cloud, or hybrid solutions, your partner ecosystem will still benefit from improved capabilities around regulation.

This knowledge should be communicated to the partner ecosystem along with a structured methodology or toolkit that partners can use to help identify legal and contractual obligations on a customer-by-customer basis. Vendors grapple with the same issues, and should consider a joint effort in examining the regulatory landscape, seeking external legal counsel, and assembling partner enablement resources.

APPENDIX

Industry	Regulations Applicable to Cloud Computing	Impact
Federal Government	<ul style="list-style-type: none"> • PIPEDA (privacy) as well as Alberta, PQ & BC's privacy acts where federal government has operations • Security of Information Act 	<ul style="list-style-type: none"> • Little regulations concerning the residency of data • Strong advocates of in-Canada with very little offshore activity • Security & privacy concerns around the public IaaS
Provincial Government	<ul style="list-style-type: none"> • Privacy regulations (PQ & BC are very restrictive) including FIPPA, PIPA (for provincial bodies) & MFIPPA (Municipal Freedom of Information and Protection of Privacy Act) • Corporate Operating Policy on the Protection of Personal Information (Ontario) 	<ul style="list-style-type: none"> • Some provinces are more restrictive than others (BC, which impacts vendors to the province, Alberta and Nova Scotia) • As with the federal government, provincial bodies are concerned about security, potential breaches and negative publicity • Certain crown corporations may not be under the same restrictions
Healthcare	<ul style="list-style-type: none"> • PHIPA (Personal Health Information Protection Act) • There are various provincial & federal regulations (for example, the Personal Health Information Act) 	<ul style="list-style-type: none"> • The healthcare vertical has been very cautious in adopting cloud computing • Advocates face the uphill task of dealing with various stakeholders and addressing the risk of breaches in data
Banking	<ul style="list-style-type: none"> • OSFI outsourcing guidelines (B-10 & E-4A, E-4B) • OSFI (Office of Superintendent of Financial Institutions) Cybersecurity guidelines • Various credit/commerce industry oversight 	<ul style="list-style-type: none"> • OSFI sets out certain guidelines concerning the auditability (location and access of data) of the service • B10 makes it challenging to use cloud's multitenant model • Regulations are open for interpretation, so that banks have been cautious about cloud • In IDC's survey, 50% of banking sector respondents believed SOX was very to extremely important
Life Insurance	<ul style="list-style-type: none"> • Under many OSFI regulations • Life Insurance Act • Privacy regulations 	<ul style="list-style-type: none"> • Impact on life insurance companies is similar to those in the banking sector (carriers are regulated under OSFI)
Retail	<ul style="list-style-type: none"> • Retailers are provincially regulated • Privacy regulations • Self industry initiatives (PCI for commerce, mobile) 	<ul style="list-style-type: none"> • Minimal barriers to leveraging cross-border cloud solutions • Retail has been an early adopter of cloud, yet is cognizant of the security issues (which impact in-house and external providers) • 47% of IDC's survey see PCI compliance as very to extremely important
Oil & Gas	<ul style="list-style-type: none"> • Privacy regulations • Health & Safety • Environment 	<ul style="list-style-type: none"> • In general, IT infrastructure is not seen as strategic and has relatively small budgets • With minimal regulatory impact, oil & gas companies have begun to shift from internal to cloud-based solutions
Utilities	<ul style="list-style-type: none"> • Some are heavily regulated (crown corporations) and some are less so • Privacy regulations • Significant others involving environment, health, safety • Some are under heavy government influence (including union influence) 	<ul style="list-style-type: none"> • Regulated utilities are compensated to own assets, which is counter to cloud computing models • Regulated utilities are under heavy public scrutiny, non-regulated much less so
Manufacturing & Resources	<ul style="list-style-type: none"> • Privacy regulations 	<ul style="list-style-type: none"> • Minimal inhibitors to leveraging cross border cloud solutions
Source: Buyers Guide: Canadian Data Centre Services, (IDC #CA40624215)		

About C4

The Canadian Channel Chiefs Council (C4) is a not-for-profit organization that serves as the voice of technology channel professionals in Canada. Membership consists of IT vendors, solution providers and distributors that are on the front lines of solving major IT business challenges. C4 is dedicated to advancing the growth of channel professionals through education, research, events, and advocacy.



About IDC

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