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SmartSpend™ Bulletin

To Maintain Buy-side Leverage After IBM's Upcoming 2021 Split, Enterprise Customers Must Prepare Now

IBM has a long history of game-changing divestitures – the most recent being its decision to spin off its IT services business so it can focus on a trillion-dollar hybrid cloud opportunity. While this disruption will likely create cost risk for customers accustomed to "fast-pass" volume purchasing, it will also create opportunity for better pricing visibility and leverage. Preparation is key, particularly for customers renewing with IBM in 2021.

In October 2020, IBM surprised many in the IT industry when it announced the spin-off of its IT services business into a new public company (NewCo). NewCo will focus on infrastructure modernization, while a leaner IBM will be laser-focused on hybrid cloud – a sizeable $1 trillion opportunity where it currently lags behind players like Amazon Web Services and Microsoft. The divesiture is expected to be complete by end of 2021.

At the time of the announcement, IBM CEO Arvind Krishna provided insight into why the company is taking on such a substantial change in the current business climate. Client buying needs for application and infrastructure services are diverging as adoption of the vendor's hybrid cloud platform accelerates. Krishna commented further:

"Now is the right time to create two market-leading companies focused on what they do best. IBM will focus on its open hybrid cloud platform and AI capabilities. NewCo will have greater agility to design, run and modernize the infrastructure of the world's most important organizations. Both companies will be on an improved growth trajectory with greater ability to partner and capture new opportunities – creating value for clients and shareholders."[1]

Demand for infrastructure modernization services isn't going away anytime soon, a point the company has noted. Based on current valuations, NewCo will be twice the size of its largest competitor on Day 1 with $19 billion in annual revenues. Customers will include over 4,600 enterprises across the globe including 75 percent of the Fortune 100.[2]

It's important to note this divestiture isn't an anomaly in IBM's behavior. The company eliminated its networking business in the '90s, followed by PCs in 2005 and, most recently, semiconductors. After spending its early years spanning many IT subcategories, Big Blue now continues to refine its value proposition and focus. Today, that focus is squarely on hybrid cloud.

Customers should anticipate – and prepare for – **contractual disruption and erosion of leverage** ahead of IBM's split.

IMPLICATIONS FOR CURRENT ENTERPRISE CUSTOMERS

The split will create internal challenges for customers where IBM is deeply embedded into the IT ecosystem – particularly for those that use both IBM's cloud and mainframe systems. Customers should anticipate and prepare for contractual disruption as their existing IBM enterprise agreements approach renewal.

Enterprise customers will need to negotiate new contracts and master agreements with IBM and NewCo. This will likely expose them to new pricing (and possibly higher cost) as legacy and cloud products are decoupled from longstanding discounts based on combined spend.

The split also will also force customers into a new sales cycle with NewCo. That may be a positive if the outcome yields better pricing, but it could also be a headache for customers accustomed to fast-pass volume purchasing.

NPI advises IBM customers begin preparations now by doing the following:

- Gain line-item visibility into pricing to establish price benchmarks. IBM is notorious for bundling license and maintenance fees together to keep details hidden. Visibility into line-item pricing and competitive benchmarks will be key to negotiating favorable pricing once the split becomes official. NPI typically finds material savings potential when performing IBM price benchmark analysis for clients.
- Determine which areas of the IBM estate should be put out for competitive bid. Without the leverage of a combined legacy/cloud footprint, customers may be able to secure more competitive pricing and terms from other vendors – there are very viable replacements for some elements of the typical IBM enterprise estate and NPI's clients have achieved six- and seven-figure savings from these shifts. Plus, IBM's transformation may distract it from serving customers at a critical juncture in their own transformation initiatives (more on this below). For these reasons, customers should evaluate competitive alternatives to ensure both solution pricing and quality align with current and future-state requirements.

A WORD ON TIMING

The timing of IBM's announcement is noteworthy. Many of the vendor's customers are still reeling from the impact of the global health crisis, which has fundamentally changed how many businesses operate. Enterprises are reprioritizing IT initiatives (and spend) to accommodate accelerated transformation that will increase resiliency and prepare against future unknowns.

As IBM realigns its value proposition and focus, its customers have an opportunity to realign their investment with changing business and technical requirements. They also have an opportunity to demand greater pricing transparency and more flexible business terms and conditions. While disruption is to be expected as the planned divestiture becomes reality, careful navigation will allow customers to get more value out of their investments with both IBM and NewCo.

ABOUT NPI

NPI is an IT sourcing consulting company that helps enterprises identify and eliminate overspending on IT purchases, accelerate purchasing cycles and align internal buying teams. We deliver transaction-level price benchmark analysis, license and service optimization advice, and vendor-specific negotiation intel that enables IT buying teams to drive measurable savings. NPI analyzes billions of dollars in spend each year for clients spanning all industries that invest heavily in IT. For more information, visit www.npifinancial.com.

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