

Contract undercutting the new black?

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Maintenance contract undercutting is now commonplace in the telecommunications industry. For those that are suffering losses of clients through the practice, it spells disaster for the sector as profit margins are rapidly eroded and the ability to reinvest in skills is depleted.

However, despite accusations of subsidisation of maintenance contracts, for those that use the method to gain new customers it can be extremely profitable; not only do they gain new clients quickly, they also have a captive audience with spare cash for reinvestment in new kit.

Andy McDougall, managing director at Central Telecom, has been accused of maintenance undercutting in the past. However, he claims that his company is simply responding to the demands of its customers. McDougall says that as customers have been spurred into reducing company overheads by the tough times of recent years, they have learnt to look closer at the actual costs charged by others to help them run their businesses.

He comments: "The facts of life, whether we like it or not, are that customers are looking for savings, especially those in hard pressed sectors that are highly commoditised. Procurement directors perceive that old fashioned maintenance is money for old rope. They are starting to demand more transparency and for added values, such as regular reviews of the performance under the contract and market intelligence, from their service contractors. Technological advances provide us resellers with remote services, which offer a quicker response at reduced costs. The old flat rate way of charging for support on the recommended retail price of the system has gone, so companies are out there using different tariffs to price up services; if one tariff works out cheaper than another, do you call this a discount?"

He goes on to defend Central's use of cheap maintenance contracts, stating that the company is not subsidising its lower charges: "If Central Telecom did not have a financially sound pricing policy, it would not maintain its healthy profits. As resellers, we are not helping ourselves, our customers or industry regulators if we insist on having a protected marketplace in which every dealer charges the same for maintenance. This is anti-competitive and is not even worth discussion."

John Cousins, managing director at Intech Telecom, thinks little of the companies that use maintenance contract undercutting as a means to gain new customers: "I'm sick to death of people going in there and slashing maintenance. The people that undercut maintenance contracts are companies that cannot sell products or look after customers any other way. They go for short term, big buck gain, by giving away the maintenance contract to customers to get them on board, then trying to get the customer with other products to re-coop the losses they've made on the maintenance contracts."

He adds: "I think the industry needs to wake up and smell the coffee. We are being squeezed enough from outside our industry and now we're squeezing ourselves on maintenance contracts, which is bloody stupid."

Kevin Stevens, managing director at Genesis Telecommunications, agrees: "There are obviously a few companies out there trying to buy business at any price. While prices can normally go down by 10 or 20 per cent, these companies slash it by 40 to 50 per cent. We have gone in on a £500,000 contract, only to get someone else come in at £120,000. It's difficult, when a competitor says it'll drop the maintenance price by 25 per cent below whatever we offer. It's devaluing the services the channel offers and ultimately the customer loses out."

Tony Parish, managing director, G3, says that it is a shame that so many dealers are undercutting maintenance contracts. He comments: "This undercutting has vastly eroded what you can make over time on a contract; I'd say what you can charge has gone down by a third over the last four years. When I face undercutting, I have to take a view on whether I'll match the price, which may be up to half of what I might have wanted to charge."

Adding value to the deal with a customer is the only way for resellers to prevent their customers from leaving them for a cheaper contract, Parish says: "We have to work on added value. A customer might say to me that they've got quite a compelling new quote on the table, but then they say that we're the company with the value. They want us to help them out by meeting them halfway so they can justifiably stay with us."

Yet cheaper maintenance contracts are often passed off as providing the same quality of service as those they are attempting to depose. It is not always apples for apples, Stevens states. Genesis has created a new level of maintenance contract, designed at a lower level to match the contracts generally offered by cut price maintenance dealers. Stevens says: "When you're up against a Central Telecom or

another competitor that's going in cheap, we will offer this new level of maintenance contract that is less than our normal levels, but is equal to those that are undercutting."

These service omissions of many cheaper maintenance contracts are costing the resellers that use this method of gaining new customers in the long term, Parish states: "We seem to be picking up a lot of contracts, perhaps one or two each week, that without exception are customers of tier one dealers that are providing them with poor service. They say they things like they have no idea who their account manager is, he never calls or he only calls when he wants to sell something."

Cousins loses approximately two customers each year to cut price contract merchants, yet he occasionally wins them back again because of his company's superior service. He outlines one such example: "Our clients get offers all the time. One of my customers left me for a half price maintenance contract and a shady company. They told the client that there were things wrong with their telephony system that don't actually exist, then said they needed to buy new cards for £500 to repair the fault as only labour, not parts, were included under the new terms and conditions. We retain our clients through high levels of customer service."

Continued cut price maintenance contracts use in the industry will lead to a differentiation in resellers, Cousins claims. He says there will be a higher echelon of professional dealers on the market that provide a high level of service to maintain their customer base. He says that to tie in customers and prevent the competition from stealing them, resellers have to start selling products and services in bundles that combine telephony systems maintenance with fixed line, mobile phones, voice mail, Web design and hosting, IP and broadband support. An increase in bundling will force cut price maintenance companies to increase skill sets to compete, so will increase maintenance prices as these businesses seek to raise investment for new skills.

However, Scott Russell, managing director at Network Europe Group, is hard nosed. He claims the resellers most affected by maintenance contract undercutting are those that offer poor services: "This is something weak dealers are scared of. If a customer wants to leave you in the first place, you haven't done your job properly. Weak dealers with weak contractual tie-ins and no value added services on their maintenance contracts should take note."

Stevens has the last word: "We're slashing the profits out of our maintenance and that's what worries me. Once you're used to paying £1 for something you used to pay £2 for, you're never going to pay £2

again; that value add is gone. If you're not making profits, you're not going to be able to reinvest, and this is coming at a time when convergence means new skills are needed."