BY MARTIN VILABOY

The Downstream

DSL's New Groove in Indirect Channels

It's been estimated that 95 percent of the 3.9 million small and medium businesses (SMBs) operate with 20 employees or less, a market segment made up largely of firms with dial-up connections or no Internet access at all. So as broadband access surpasses 60 percent penetration of online business desktops, there is a growing market of under-served small businesses with needs that fall somewhere between the cost and bandwidth offered by T1-based access technologies and the limitations of dial-up connections.

Major competitive and incumbent carriers such as BellSouth, Verizon, Sprint, Covad and New Edge Networks certainly see the window of opportunity. And the newer business-grade digital subscriber line (DSL) services, such as symmetrical lines scaleable to 1.5 Mbps, multiple static IP addresses, virtual private networks (VPN) and service level agreements, conceivably push DSL well past the 20 employees and under portion of the market.

Of course, the investments have led to some aggressive sales forecasts. "Expectations of the carriers are going up," says one carrier consultant. "Quotas are going through the roof, and [managers] don't know how to hit them."

One important way will be through indirect channels, and a maturing deployment process extends the distribution channel beyond wholesale Internet service providers (ISPs) and traditional telecom agents to firms that may specialize in cabling, private branch exchange, network consultancy or software services. In many ways it's because these types of channels represent one of the most cost-effective ways to reach the perceived prime targets of business DSL services.

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Due largely to its focus on second and third tier metro-area markets, New Edge relies "almost exclusively" on its indirect selling partners, says Moffat. The company's DSL footprint covers more than 360 small cities and towns across 29 states, and therefore simply "can't afford to have retail sales people located in all those markets," says Moffat.

New Edge distributes primarily through a network of almost 300 wholesale ISP partners, which in turn look to an array of agents, value-added resellers (VARs), integrators, consutants and software service providers. And at that level in the value chain, even the small margins commonly attributed to DSL, though this is increasingly an issue with only residential-based services, become more appealing, as distributors can always rely on the recurring revenue of their core services offering.

In other words, unlike past attempts at hitting the business market, nobody is going to live or die by DSL alone.

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New Edge Network's DSL Financial Model

	Consumer Service	Business Service
Average retail revenue	55.00	115.00
Value added services	5.00	12.50
Total revenue	60.00	127.50
Loop costs (average)	40.00	55.00
Billing and support costs	2.00	2.00
Bad debt (2 % of revenues)	1.20	2.55
IP upstream costs (80 customers per meg for consumers, 40 customers per meg for business, $200 per meg)	2.50	5.00
Total variable costs	45.70	64.55
Variable margin	14.30	62.95
Other costs (Ag circuit, 110 users per DS-1 for consumers, 75 users per DS-1 for business ($600 MRC for pipe)	5.45	8.00
Monthly margin (at fully subscribed ag and IP upstream)	8.95	54.95
Sales compensation	165.00	285.00

Source: New Edge Networks

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"The best margins come when parties build or sell an application, say a video application for example, and they partner with us for transport," says Moffat.

"We would probably not bring an agent on board that would sell only DSL," says Lee Priest, director Sprint Business indirect/channel partners. Sprint recently announced new wholesale DSL products and plans to add a "multi-meg" solution to indirect channels within the next few months. Of course, Sprint can be expected to encourage agents to bundle its long distance service with the high bandwidth DSL to mimic an integrated voice and data offering served up through a T1 connection.

For telecom agents and the more traditional resale networks, the growth in business-class services means DSL increasingly will emerge as the most logical and affordable way to address a customer's specific wants and needs. So for distributors that look to sell "solutions to their customers' problems" rather than "product for the sake of the product," DSL becomes a key tool in the shed.

Business DSL Lines

2000 Q3	2000 Q4	2001 Q1	2001 Q2	2001 Q3
569,000	704,000	787,000	867,000	994,000

Source: Telechoice

"Often, you've got to have it to get in the game,"says Rob Hunter, president and CEO of Alliance TeleSolutions. "And you better have a few other things behind it."

We're not saying that DSL is necessarily a "loss leader" here, as the business model that New Edge presents shows healthy enough margins, at least for business access. But once again, as Hunter points out, DSL in indirect channels works best as a piece, and not necessarily the starting point, of a well-rounded portfolio. "I don't have guys out there trying to sell DSL," he says. "I've got guys using DSL as part of an arsenal."

So while DSL, and broadband access in general, is often necessary "to win the client," says Hunter, "it is not all that I am going to sell. And I'm surely not going to run a blitz on DSL access, because all my people will be doing is paperwork taking orders."

In the Loop

Certainly, many of the well-known regulatory and technical challenges that have handcuffed DSL so far are still very much present. Some won't soon go away. "But as an industry, we have made great strides in provisioning, so it is much less painful for VARs, agents and partners to get involved," says Sal Cinquegrani, New Edge's executive director corporate communications.

"It's not necessarily getting less complex, it's just becoming more familiar," says Dahman. Which means ordering and provisioning processes have become more predictable, and install times have lessened significantly. For the fourth quarter of 2001, for example, Covad reported average installation times for business-class services of approximately 23 days, a 39 percent improvement over completed orders in the fourth quarter of 2000.

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"All parties understand the hand-off points and overall process much better," continues Dahman.

Albeit, it's not as if DSL automatically becomes "easy," with clearly defined market segments and margins that allow it to be delivered to any pre-qualified business that is willing to pay the price. The good news is, SMBs are readily adopting broadband access and seem to believe they are better off for it.

According to research from Nielson/NetRatings, for example, the at-work broadband population increased 42 percent to 25.5 million in January 2002, compared to 18 million office workers the year prior, as broadband connections not account for 63 percent of the Internet office population. Conversely, the number of unique at-work narrowband connections fell 23 percent in the same time period.

Even at the low end, "very small businesses" (VSBs) are paying more for Internet connections, argue Yankee Group analysts, and the top reason why SMBs churned their ISP in 2001 was to get broadband.

Furthermore, Yankee Group found that 47 and 33 percent of

A Majority of Small Businesses Lie Within Two Miles of CO in Many Markets

Metro Area	Number of SBs (2 to 99 Employees)	SBs Within Two Miles of CO	Percent of Total
Billings, Montana (Top 5 COs)	2,645	1,235	46
Dallas (Top 10 COs)	20,774	12,896	62
Grand Rapids, Michigan (Top 10 COs)	10,296	4,997	49
Honolulu (Top 10 COs)	8,916	8,501	95
Indianapolis (Top 10 COs)	28,084	15,558	55
L.A./Long Beach (Top 10 COs)	23,677	18,227	79
Portland, Oregon (Top 3 COs)	7,495	5,680	76
Reno, Nevada (Top 5 COs)	4,742	3,651	77
Stamford, Connecticut (Top 3 COs)	3,218	2,894	90

Source: Jetstream Communications, 2001

broadband VSBs purchase Web hosting and firewall/VPN services, respectively, from their service providers, compared to 27 and 17 percent of dial-up VSBs. Yankee surveys also show that 80 percent of SMBs with broadband agree that Internet access has "improved overall business productivity."

"People keep saying the killer application for broadband is not here, and that may be true for consumers," says Moffat. "But businesses are inventing them right under our noses."

A New Edge partner in Pueblo, Colorado, for example, reports to seeing more electronic data interchange (EDI) connections, which typically are found within large enterprises, now taking place within small businesses. "You have insurance companies that are linking together and realtors that are linking to title companies that are linking to appraisers," says Moffat.

Still, a small company with high-speed wants and needs does not always translate into a positive return for customer-facing service providers. And the common notion that businesses with 2 to 19 employees constitute the "sweet spot" for DSL is largely true, but many customers in that segment are better off left to direct retail channels.

One big reason is that many of the smallest businesses don't have managed information systems or computer experts on staff, so agents end up configuring multiple desktops, hooking services up to local networks or setting up mail servers in order to facilitate the full installation and implementation. "You end up doing all this for basically free just to get the darn thing working for a $150 commission," says one agent.

Of course, more and more, agent programs are available whereby service, support and technician visits are handled by underlying carriers; that is assuming distributors are willing to share customer ownership

But unlike residential service, business-class DSL access and applications rarely will be accomplished through self-installation or level-one phone support, says Peter Tripoli, vice president for integrated services at Danet, a technology and strategy consultant for telcos. Tripoli points to a CLEC customer that "does a truck roll on every DSL implementation, by choice," he says. "Because they found that the customer satisfaction is lower if they don't."

Obviously, happy customers are paramount to a model that involves leveraging an agent's, a VAR's or system integrator's "trusted advisory relationship with its customers." So a scenario that entails bringing the circuit to the demarcation point, hooking up the router and walking out the door simply won't fly. "That is not what the small business market needs," says Hunter. "They need someone to actually connect it to their network, make it work and settle them down." It's surely a better recipe for encouraging future upsells.

The Up and Down

Probably most important to any discussion of DSL and indirect channels is the debate over whether very small businesses need and will absorb the higher cost of symmetrical DSL access. On one hand, there is the sentiment that 256 kbps is sufficient to serve up to 20 users, and most of the smallest companies, with servers hosted off-site, care little about upstream bandwidth. So for all but the most data-oriented VSBs, the lower price point of ADSL (at $50 to $100 a month less than comparable SDSL service) is enough to make up for the difference in reliability and performance.

On the other hand, some providers argue that businesses simply won't be happy with ADSL, since it typically comes with no service guarantees, mean times to respond and repair that are measured in days rather than hours and less ability to be upgraded or layered with enhanced services. As is often the case, the final conclusion rests in the hands of the individual end user and the intended use of applications.

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For reseller agents, the choice is clear. Quite frankly, ADSL resale typically pays a flat commission, such as a one-time referral payment of $150 to $200, while SDSL often represents an opportunity for residual commissions or a percentage of total monthly recurring revenue.

Fortunately, there are applications, even beyond the 2 to 19 employee segment, where symmetrical bandwidth becomes necessary. Along with the EDI scenario, another such example lies within mid-sized to large companies with multiple locations or a large remote workforce, as one location's upstream is the downstream of another. Likewise, "if you are doing any kind of serving, you really need an upstream and downstream pipe that are of equal size," says Dahman.

DSL also can be used to get around corporate access networks. Take the case of online training and counseling via video services, where a provider's customer base may already have T1 access, but the firewalls and security behind it make it a burden to turn up video quickly enough. "For an extra $200 a month, that video services provider can get around the problem and get up and running without having to deal with the MIS department," says Hunter.

At the other end of the market, incumbent and competitive carriers finally seem ready to take ownership of installation and support, so even one-time referral payments for turning up a current customer can be worth the effort. And in theory, the broadband access creates a more valuable customer for all involved.