

GenAI: A Growth Catalyst for Cloud Evolution in 2024 and Beyond

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For all the challenges that cloud vendors faced in 2023, there was a promising sprout of opportunity that developed quite rapidly with generative AI (GenAI) technologies. The pace with which GenAI gained not only awareness but also real investment and usage in the market was notable, and we expect end customers' real investments in the solutions to continue to grow and develop in 2024.

However, GenAI solutions on their own will not overcome the headwinds that worked against the market throughout 2023. Many of the forces that caused revenue growth rates to slow precipitously for nearly every major cloud vendor remain in place heading into 2024.

The general macroeconomic conditions remain uncertain, wars continue to threaten global stability, IT buyers remain cautious about spending, and cloud has reached a saturation point in many IT organizations. So, while we do not expect GenAI technology to return the market and leading vendors to their pre-2023 pace of revenue expansion, it will serve as a small yet rapidly growing segment in 2024 and should become a significant market in 2025 and beyond.

We also expect the intensity of AI-focused strategies during 2024 to reflect the importance of the technology to long-term growth. AI could reset the cloud leaderboard for the next decade, so incumbents like Amazon Web Services (AWS) and Salesforce will be keen to protect their large customer bases against mounting AI competition from the likes of Google, Microsoft and SAP.

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GenAI and the Cloud Revolution in 2024

Prediction: Cloud Growth Is No Longer Enough

Trend: The cloud landscape will become segmented between vendors that can sustain high rates of growth and expansion and those that cannot in 2024.

Drivers: Simply providing cloud services at scale is no longer enough for vendors to gain cloud market share. More complex strategies will define the cloud leaderboard in 2024, such as effectively monetizing next-generation features, expanding addressable markets, and orchestrating multivendor partnerships.

Result: Delivering AI-enabled next-generation capabilities and nurturing ecosystems will garner investment despite the slower market growth and macroeconomic uncertainty.

Heading into 2024, the cloud market has been on a more than 15-year growth trajectory that rewarded leaders for establishing scale above all else. Early-to-market vendors, like AWS in infrastructure and Salesforce in SaaS, capitalized on the consistent market expansion to establish themselves as not only some of the largest cloud providers but also the largest vendors in their market segments across all delivery methods.

However, those firms also experienced some of the most dramatic slowdowns in revenue growth as the market softened in 2023. Part of that slowdown is undoubtedly the “law of large numbers,” meaning growth slows as size increases, but it also reflects a broader market shift toward growth created by new features, capabilities, and go-to-market programs.

In 2024 We Expect Vendors that Successfully Implement the Following Strategies Will Become Growth Leaders in the Cloud Market

AI monetization: While the market for GenAI and AI solutions more broadly is still developing, the investments from end customers appear to be very real and meaningful. Despite the intent to invest and spend, there are many hurdles for vendors to clear to start recognizing the revenue opportunity. These hurdles include identifying and articulating use cases, measuring benefits and returns, implementing pricing models that work for both vendors and customers, and developing an ecosystem to support all these tactics. Vendors that make progress tackling these challenges stand the best chance of realizing AI-led growth in 2024.

Ecosystem development: The benefits of an ecosystem have been clear for decades, but for many IT and cloud vendors, the changes to their business models have been too significant to overcome. However, in an environment where cloud vendors are experiencing slower growth and still trying to control expense levels, the ecosystem model is even more impactful. Proficiency in orchestrating service partners, ISVs, resellers, and joint solution alliances around core offerings will be another growth driver for vendors in 2024.

Account base management: Managing a customer base that spans traditional legacy solutions and cloud-delivered ones has been a challenging task. To date, it has been simpler and easier for born-on-the-cloud providers to use a disruptive model to sell a simplified set of offerings to establish their position in the market. However, there is now an advantage for multimode providers in controlling the transition to new solutions and delivery methods in a slower-growth environment. SAP is the clearest example of this advantage, as it has been able to sustain growth in 2023 even as its more cloud-dependent peers have experienced the impacts of the market slowdown. The maturation of AI opportunities will also play a role in this advantage, as customers may end up with data models stored in a variety of places within their IT landscape, based on performance and security requirements.

Prediction: IaaS Will Become More Tailored to Workload and Regulation

Trend: The days of general-purpose computing are gone, and vendors are customizing their global infrastructure with dense, metro-level facilities for edge computing and isolated cloud regions for sovereignty.

Drivers: The proliferation of data and more demanding workloads, including AI, will necessitate low-latency processing, while a changing regulatory environment in Europe will shape vendor investments in sovereign cloud.

Result: Raised capex budgets lead to new global infrastructure that is specialized for a customer's specific workload or regulatory environment.

IaaS is not one size fits all, and vendors will continue to adapt their cloud infrastructure to address a client's workload- or industry-specific requirement, such as a retail customer that needs to run a system on their sales floor to analyze traffic patterns in real time. Or the client could require a country-specific data center to restrict data flow, comply with local laws, and build trust with customers.

Two Key Initiatives IaaS Vendors Will Focus on in 2024

Hyperscalers prioritize edge: Edge computing remains somewhat ambiguous and is still not widely accepted by the large enterprise. Regardless of the market's hype, we cannot deny there is value in running workloads closest to the data-generation source. This source could be in a customer's premises or a location near the access layer of the network for a range of use cases across healthcare, manufacturing and retail. For many customers, migrating to the cloud is top of mind, with edge as more of an afterthought. However, the rise of big data and AI, and the need to harness data in the most compute-efficient way, may cause customers to evaluate cloud and edge hand-in-hand. Specifically, a cloud-out approach, where customers migrate to the cloud and extend workloads to the edge, may be a winning strategy, particularly for those with a cloud road map already in motion. Hyperscalers recognize this trend and will continue to invest accordingly. AWS will continue to invest in Local Zones across 16 countries, while Google Cloud will turn to its partner ecosystem and ensure ISVs can monetize edge offerings on Google Cloud Platform (GCP).

Sovereign cloud moves from marketing tactic to niche delivery method: Over the past five years European businesses have been adjusting to a changing regulatory and cultural landscape around data privacy, ownership and sovereignty. Specifically, the European Union's (EU) requirement that companies must host data in the same country in which they operate has led IaaS vendors to establish new cloud regions. These sovereign clouds are clearly marketed to EU-based enterprises and governments and consist of isolated data centers that operate independently of other European cloud regions and offer special data residency guardrails, governance policies and security controls. Most notably, the data centers can only be accessed by EU-resident employees. Microsoft and Google Cloud led the sovereign cloud charge in 2022, and even Oracle, which is trying to play catch-up in IaaS and position itself as the fourth major hyperscaler, brought two sovereign cloud regions online in Madrid and Frankfurt this year. IaaS leader AWS recently announced plans to launch a sovereign cloud region in Germany. AWS' entry into the space is a good indicator these dedicated environments are resonating with customers that need a completely isolated environment for their critical workloads, not just some bolt-on encryption features and services. While AWS' new sovereign region is not yet available, we view this as a necessary step for AWS to address customer requirements and keep pace with peers, as local governments and customers may have been evaluating other clouds. In 2024 we expect vendors will open new regions in other EU countries and will develop new partner strategies to extend sovereign cloud protocols within EU borders to other commercial cloud regions across the globe.

Prediction: SaaS Vendors Promote Multiproduct Sales with Generative AI

Trend: For years, SaaS leaders have pursued multiproduct sales to grow revenue within their existing install base. As the realities of GenAI adoption set in, these leaders will gain a new way to encourage enterprises to consolidate their software procurement strategy.

Drivers: GenAI is coinciding with a persistent trend toward cloud cost rationalization, yet many enterprise leaders will prioritize AI adoption out of a fear of being left behind at a critical technology inflection point.

Result: Enterprise customers will look to offset AI spend by cutting costs elsewhere and promoting the role of volume-based discounting in software procurement.

GenAI Hype Will Meet Enterprise Adoption Realities

While the conversation around GenAI in 2023 has been exciting, the amount of work that needs to occur before the technology can reach its full potential will be put into focus for 2024. Some may use this opportunity to decry GenAI as just another overstated hype cycle, but this would be missing the point. Adjusting to innovation takes time, often more time than desired.

While GenAI's ability to automate content generation directly in workflows is undeniably valuable, reaching the output efficiency, quality and accuracy sufficient for many enterprise use cases will require customers first develop mature data postures. Once data frameworks are in place, large language models (LLMs) will need to be trained on workflow-specific data and outputs will need to be tuned around the use case to limit the need for manual manipulation.

Further, this technological inflection point has arrived amid shaky economic footing. While consumer spending is sustaining U.S. gross domestic product (GDP) growth at a healthy level, tightening credit markets and persistent wage inflation continue to cast a shadow over the economic outlook, especially as geopolitical tensions in the Middle East and eastern Europe drive up energy prices. This has prompted many enterprises to undertake cloud cost-rationalization strategies over the past year, many of which remain ongoing. Many cloud vendors are seeing the impacts roll through their quarterly financial results, citing elongating deal cycles as a cause of decelerating revenue performance.

GenAI Will Promote Vendor Consolidation

When we consider that boardrooms face the opposing forces of keeping pace with innovation while limiting new spend, the path forward for enterprises will require many to rethink their stance on IT procurement; TBR suspects vendor consolidation will be one of the more impactful outcomes. Even prior to the emergence of GenAI, TBR's customer research has indicated that enterprises' expectations for vendor quantity are noticeably moderating.

According to TBR's *1H23 Cloud Applications Customer Research* study, 52% of enterprise buyers expect the number of SaaS vendors they work with to increase over the next two years, yet this number is down from 60% compared to our 1H22 study and 64% in our 2H21 study. As GenAI becomes a priority, the technology will be a catalyst for consolidation as enterprises seek out cost efficiencies and greater IT simplicity. Consolidating software vendors will make it easier for enterprises to centralize data from separate workflows for the sake of model ingestion, improving their ability to train LLMs on a wider variety of business data.

Recognizing the role of data platforms, many SaaS vendors, including Salesforce and SAP, have made a lot of progress in developing native platform capabilities. In the case of Salesforce, these investments, mostly the acquisition of MuleSoft, have made Data Cloud the company's fastest-growing cloud suite to date.

These platforms will unlock the necessary synergies across application suites to build environments where customers are able to connect their LLM assets to multiple workflow areas. This will make it simpler for enterprises to consolidate their software procurement around their LLM, which vendors can further encourage by offering volume-based pricing discounts. By promoting bundled software around GenAI, vendors will alleviate the cost concerns associated with GenAI and support their install bases' journeys toward AI maturity.

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