



cutting through complexity

Remaining Competitive in the Technology Industry

*Implementing growth
strategies in the
new realities of the
tech industry*

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Driving and maintaining growth continues to be a top-of-mind issue for Boards, CXOs, and investors in the Technology industry. Technology companies and the chain of services supporting them are facing profound business challenges resulting from three significant factors that in combinations are unique to their industry:

- 1. The explosive rate at which companies and the industry are growing**
- 2. The amount of growth that is driven by innovation in technologies, value propositions, products and services**
- 3. The clock speed at which these innovations need to occur in order to drive growth**

Given these circumstances, technology companies need to focus on innovation and agility to capture the business value of their growth strategy. To capture and realize the value they intend, technology companies need to continuously evaluate their capabilities, operations, organization, talent, infrastructure, and measures of success to make sure their planned growth strategies are aligned with their operating models.

In practice, companies often face significant challenges as they try to implement their strategy by pivoting their operating model to align with the growth strategy, for instance:

- Failure to create a seamless connection between strategic growth aspirations and operations execution
- Lack of a systematic and repeatable approach for creating effective operation models to support innovation efforts and other growth strategy plans
- Misalignment of assets and capabilities to growth aspirations and excessive complexity that can lead to sluggish performance
- Insufficient transparency on goals and expectations for all stakeholders

To succeed, technology companies need to deploy an integrated strategy-through-execution approach that will help them to take these important steps as they respond to a rapidly changing business environment. Such an approach is critical if companies are to realize their strategic goals, create and grow business value for stakeholders and stay competitive in a rapidly changing marketplace.

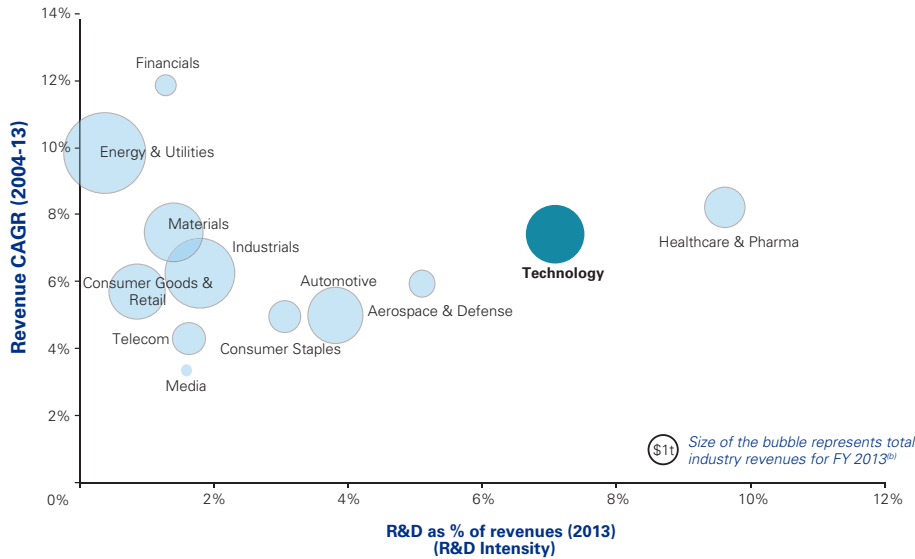
This paper describes how the technology industry is evolving and how executives are responding to the challenges they face. It also explains a phased approach to linking strategy with execution that can help companies to ensure they realize business value from their plans for growth.



02 Technology Industry Landscape

A variety of interrelated developments have led to current conditions in the technology industry. During the past decade, the technology sector has grown 7%, and R&D spend has been outpaced only by that of the healthcare & pharmaceuticals industry.

Figure 1: 10 Year Revenue Growth vs. R&D Spend by Industry

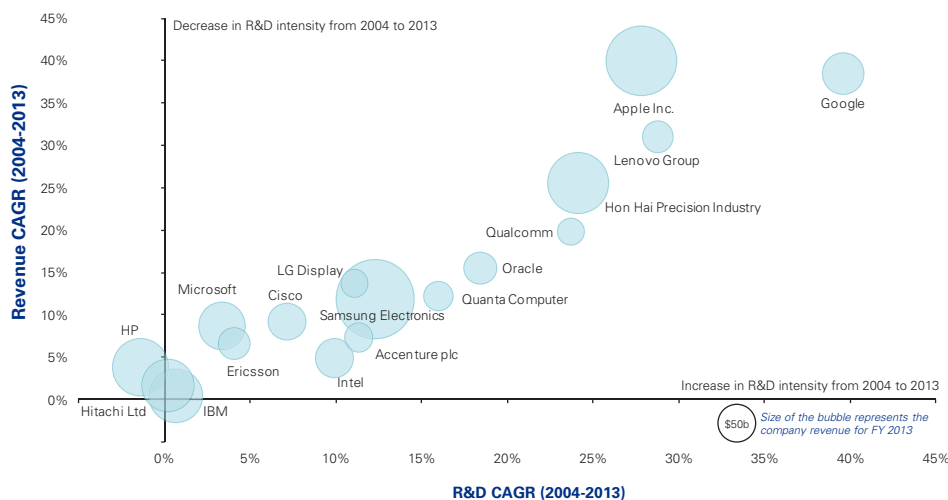


Source: Capital IQ, accessed September 2014.

Investment in innovation has fueled technology growth. Analysis of a sampling of the largest publicly traded technology companies has shown a strong correlation between increases in R&D spend and revenue.

Companies that continue to invest in new products and services (including through acquisitions) have been able to sustain growth, while those with slower R&D investment growth have become stagnant. Technology companies with annual R&D growth over 20% have outperformed their peer group 4:1 in revenue growth.

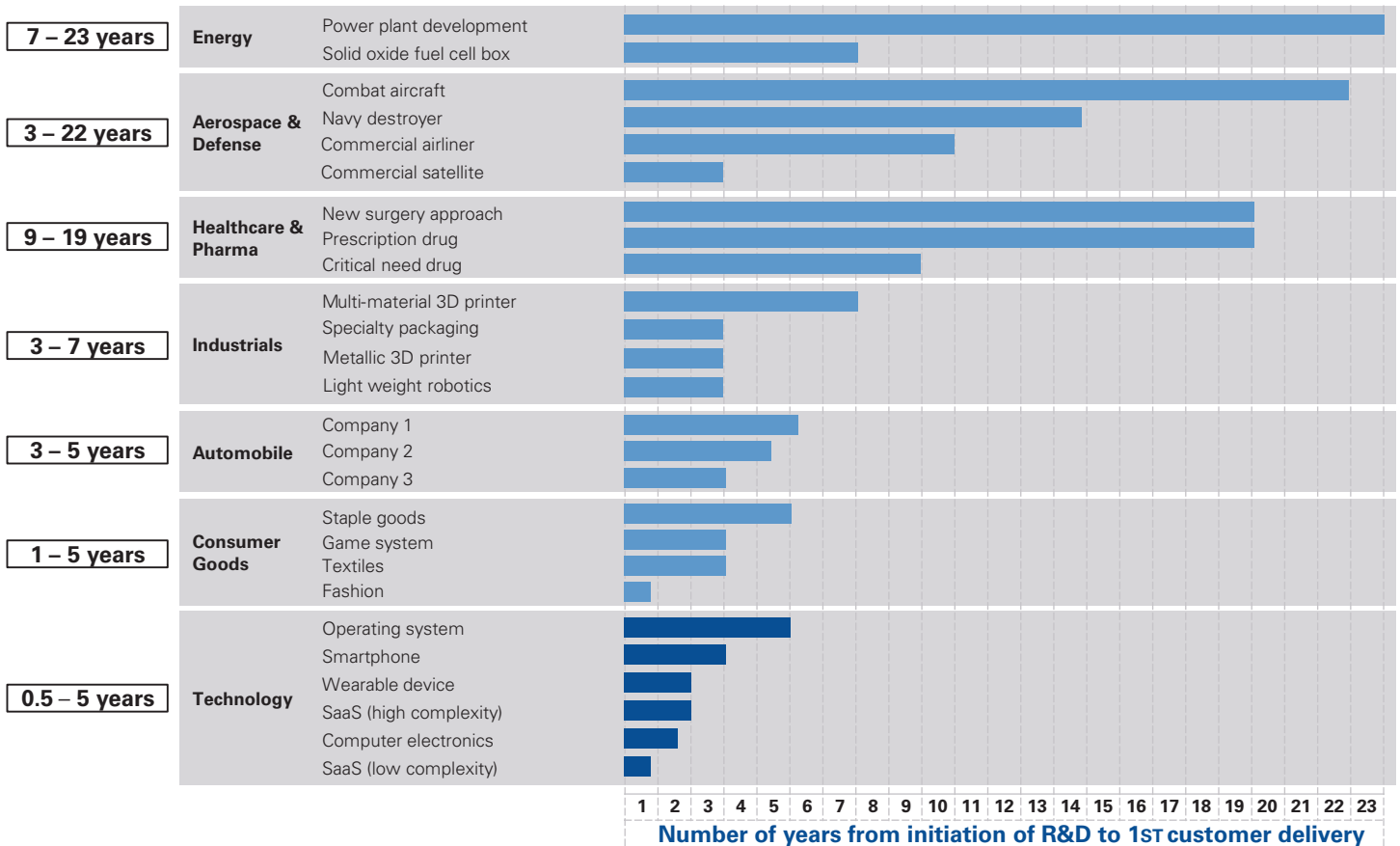
Figure 2: R&D and Revenue Growth by Technology Company



Source: Capital IQ, accessed September 2014.

Research also shows that technology companies are continuing to increase R&D spend and accelerate the rate of acquisitions. What's more, these companies have one of the fastest innovation cycles compared with other major global industries including Health, Automotive, and Consumer Goods.

Figure 3: Innovation Cycle Time by Industry (Concept to Launch)



Source: KPMG LLP (US) analysis of industry articles and reports, 2014.

Note: Innovation cycle time varies significantly from product refresh cycle, e.g., for smartphones, innovation cycle time is 3 years while product refresh cycle is 9-12 months.



Executive Challenges and Reaction to the Market

Speed of growth and innovation has created opportunities and complexities for the industry and its leaders. Today, most large technology company executives are faced with the market expectation to rapidly bring a wide range of new value propositions, products and services to the market in ever increasing clock speed. Meanwhile, fierce competition and new entrants are commoditizing these new values at an increasingly rapid rate. The combination of increased speed of innovation and intensity of competition creates great opportunities and innumerable complications for companies.

Thus, companies are not limited by lack of new innovation ideas, but instead are challenged on how to deploy growth strategies in a timely and effective manner. Some companies have communicated to investors via company financial statements their lack of confidence in their execution capabilities.

Nonetheless, a 2013 survey by The Economist found that 88% of technology executives believe strategic execution is essential or very important to companies' competitiveness. However, 52 percent of these same executives rate their success in implementation as fair to somewhat poor.¹ At the most basic level, these executives are asking, "How do I evolve my operating model and build the necessary capabilities to support my new growth strategies?"

Some examples of the challenges technology companies are facing include:

Monetizing the cloud has emerged as a principal theme for technology companies in recent years, with the question shifting from "Should we participate in the cloud space?" to "How do we participate, and/or how do we scale our cloud offering?" Companies are challenged to create a differentiated cloud experience for customers to continue to grow revenue and achieve their strategic and financial imperatives. Because cloud deployment has not become a core competency for most large technology organizations, many of them struggle to change an existing, successful business model to accommodate cloud capabilities. Increasingly, however, integrating cloud deployment will be a key aspect of optimizing a go-to-market strategy and sales infrastructure to align with customer needs.

Data and analytics initiatives have resulted in significant investments yet limited returns to date for the larger technology organizations. Select organizations have chosen to utilize their data internally through business analytics, driving more targeted products and services to consumers, while others have monetized their data through direct sales to customers. Whatever the choice, executives have been challenged to create a profitable operating model in which they can appropriately monitor and measure performance (when using data for internal purposes) and develop an organizational structure and governance model (when targeting products to customers).

Business model shifts are another pervasive theme and challenge within the software space, where organizations are looking to shift to subscription-based solutions to attract, retain, and/or grow the customer base. However, such a change in the business model affects the entire organization: it can introduce short-term risk to revenue, customer attrition, and profitability targets, especially because the transition often takes longer than initially planned. Executives must harmonize their go-to-market strategies and sales incentives, the development organization's deployment cycle to align value with customers, and back-office infrastructure support for the quote-to-cash collection process. A lapse in execution on any of these matters typically results in customer retention issues and missed results. Another common example of a business model shift is a legacy hardware centric company converting to a portfolio dominated by software. Executives have been enticed to change business models by the attractiveness of increased margins, however this may create disruption when maturing new capabilities, R&D approaches, sales strategies, channel partnerships, etc.

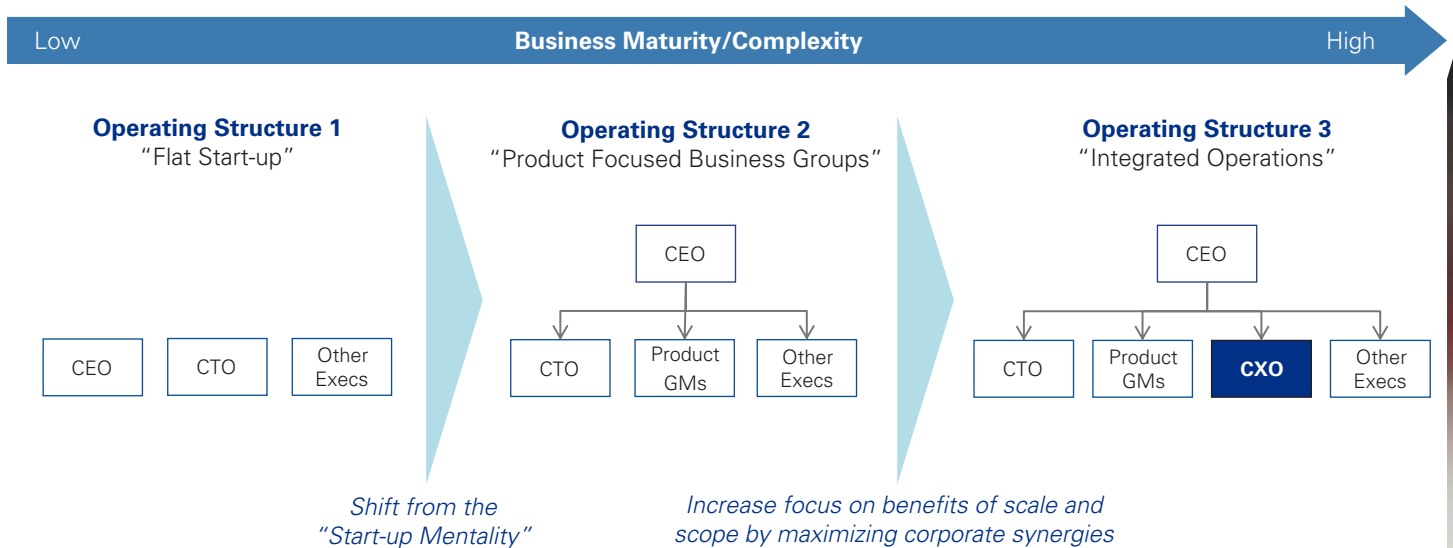
Launch or integration of new businesses is a key value driver in the technology space, and its challenges are felt throughout the organization. Technology companies generally use acquisitions as a method of innovation (and faster-to-market times) or develop new business units to support successful R&D ventures that eventually launch for commercialization. However, companies are faced with the challenges of aligning the back-office infrastructure and operating models of two businesses (organic or inorganic) as well as integrating brands, people and culture and goals and incentives. Integration processes are rarely straightforward, and poor execution generally restricts the organization's ability to achieve management's strategic goals and financial targets. There are examples of technology companies that have acquired tens or even hundreds of companies before they chose to address an integrated business model and supporting operating model. Some of the challenges observed are rationalizing the cost structure and associated accounting, optimizing the product portfolio, deploying the sales and marketing strategy, etc.

For the most part, growth strategies and initiatives are well defined, i.e., there are many approaches to determining market or acquisition attractiveness. The next step is to extend the business model decisions to understanding the implications on the core business processes and operating model. Either business case will require executives to deploy a strategy-through-execution approach to monetize the value of the business decision. If deployed effectively, a well-rounded evaluation of the business will help maximize the value of the growth strategy and improve the speed of implementation.

¹ The Economist, Why good strategies fail – Lessons for the C-suite (2013) [Need exact date]

Maturing technology companies are becoming more complex every day, but to compete successfully with more agile start-up competitors, they need to match their level and speed of innovation. Eventually companies become so diverse that they evolve into an organizational model with a number of integration functions to leverage synergies and increase effectiveness.

Figure 4: Technology industry organizational maturity timeline



Source: www.theofficialboard.com; company websites, and KPMG LLP (US) analysis, 2014.

It is the responsibility of the CEO and supporting C-suite executives to help drive strategic growth strategies, in part by reducing business complexity and increasing the speed of integration. A sample of the top 30 technology companies (Figure 4) shows that more than 40% have a Chief Operating Officer (COO), highlighting the importance of an operations strategy. This number is expected to rise in the coming years as product offerings become more diverse. Similarly, companies have also chosen to invest in a Chief Marketing Officer (CMO), showing CEOs' commitment to creating synergies among their products and services across the markets they serve.

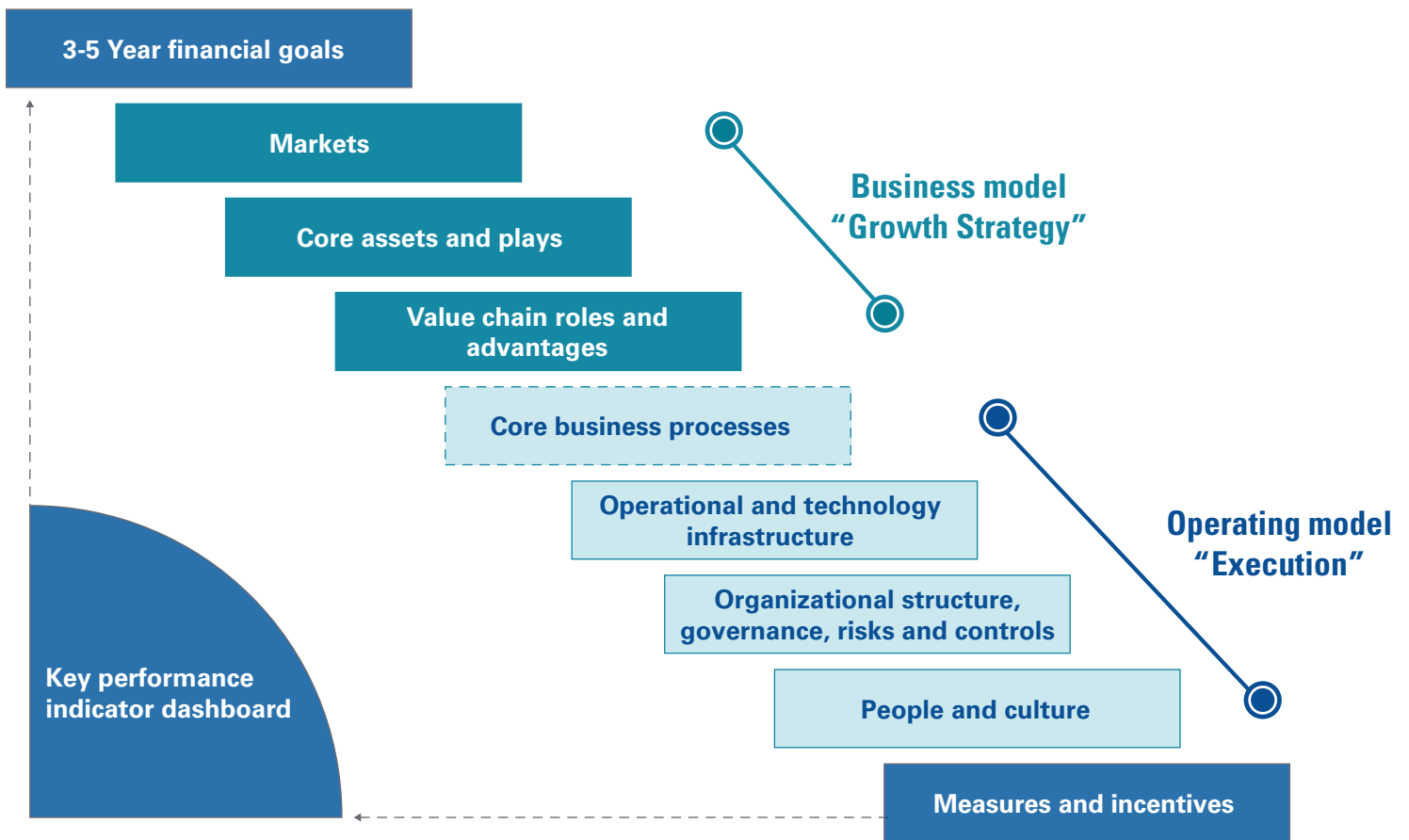


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Recommendation for Technology Companies to Stay Competitive

To remain competitive, large technology companies must clearly define their growth aspirations, establish a feasible business growth strategy, and align the operating model and appropriate capabilities to deliver on the strategy efficiently and effectively. Deploying an integrated strategy-through-execution approach will help companies guide the strategic planning processes and accelerate deployment of the growth strategy.

Figure 5: Strategy through execution approach



Source: KPMG LLP (US), 2014.



A well designed strategy links the implications of the business model to downstream operating model decisions (Figure 5). Thinking about the interrelationships of the business in the early stages of strategy formation will help companies lay the groundwork for an effective strategy and—especially important in the technology industry—help accelerate the go-to-market timeline. Companies that take this approach to improve their strategy execution will be better able to:

Create a seamless connection between strategic growth aspirations and operational implications.

Executive teams should define the end state of their growth aspirations and think through downstream implications and strategic alternatives. For example, strategy implications on operations may include a shift in sales channels, geographic footprint, strategic partners, information systems, or changes in cultural norms to foster the desired results of the strategy. Those that have been involved in corporate strategy know rolling out new growth platforms is a time consuming process, and when operation details are neglected, the process cannot deliver the intended results. Thinking through operating model implications early in the strategic planning process will allow for some of these changes to be done in parallel, rather in the traditional serial rollout that can take years.

Establish a systematic approach for aligning effective operating models to growth strategy plans.

By design, business models and their supporting operating models shift over time. When companies plan for this shift, they benefit from the consistencies derived from evaluating their business on a recurring basis. An important first step is to identify trigger points that will prompt reevaluation of the business and operating models. Examples include acquisitions and separations, rollout of new product lines, large shifts in market demand, changes in consumer buying behaviors, or geographic expansion. Once the recurring cycle and trigger points have been defined, evaluation tools and approaches need to be established to speed up the process of strategy deployment. Many effective tools and approaches are available; companies need to determine is the most appropriate tools for their business and leadership team.

Right-size assets and capabilities to improve alignment and focus on strategic plans. When growth strategy plans have been established and the operating model interdependencies understood, many assets will no longer align with the future of the business or add value as they once did. All too often businesses during periods of growth ignore undervalued assets. Divesting of these assets benefits a business by 1) assisting with self-funding growth plans and 2) enabling improved focus and alignment on the future vision for the business. Considerable research identifies “lack of focus” as an attribute that leads to unsuccessful CEOs. Our experience suggests the same goes for the rest of the business, and maintaining focus on growth plans by divesting undervalued assets will improve the end delivery and reduce business complexity. For example, a Silicon Valley company going through separation optimized two separate cost structures and deployed a team to optimize operations in parallel with deploying a growth strategy investment. Doing these activities in parallel allowed this company to realize its strategic agenda much quicker than if it did these activities in series.

Increase transparency on goals and expectations for all stakeholders. Fine-tuning the operating model in parallel with the strategy rollout will be difficult without stakeholder participation. Early engagement with partners across the value stream will help leaders coordinate the insights that affect decision-making as well as the potential impacts of changes associated with the strategy. To increase the speed of strategy deployment, changes spurred by innovation cannot be deployed in series. Many elements must work together to improve response time, and employees, suppliers and distribution partners all have key roles to play. Experience shows that developing phased implementation plans to coordinate strategy implementation increases time to market and thereby helps maintain competitive advantage.

Recommendation for Technology Companies to Stay Competitive

The speed of industry growth, the amount of innovation spend, and the rate of innovation cycles are together prompting technology executives to seek new ways to efficiently and effectively bring their innovation driven growth strategies to market. Deploying an integrated strategy-through-execution approach will help companies guide the strategic planning processes, accelerate deployment of the growth strategy, and drive business value.

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