

The 21st Century Corporation

Using Business Virtualization To Unleash the True Power of Innovation

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When was the last time you had a Kodak moment? Or made it a Blockbuster night?

Sadly, you may not remember. Those once-mighty companies experienced drastic drop-offs in market share after being outpaced by new innovations.

Whether the culprit was digital cameras or digital downloads is moot. The real issue is that these companies' long-term strategies were built around the moments when *they* were the ones driving market disruptions. Once more rapid change in their respective markets arrived, those same strategies proved to be fundamental disadvantages.

They are certainly not alone. In the past, companies found great success when a specific idea or innovation disrupted the status quo of their industries. Moving forward, they would entrench their core strategy, competency, business processes, infrastructure, and culture around that singular breakthrough.

Today, that familiar model for success is being upended.

Speed and quality of innovation are driving shareholder growth while innovation cycles get shorter and shorter. Constant change is the new dynamic, and agility is more essential than at any point in business history. With disruptions occurring at a dizzying rate, organizations are forced to move at "Internet speed" as they attempt to adapt to "the new normal" (however it is defined in any given year or month). Older companies, especially, struggle to keep pace. And with those market disruptions arriving so rapidly, the same fixed assets, cultures, and business processes that once held companies in such good stead become a fundamental liability, an Achilles' heel when fast-paced challenges arise.

Compounding the problem, as older companies struggle with their legacy cultures, out-of-date processes, and outmoded infrastructures, smaller and more nimble competitors are stepping in to drive their own disruptions. One measure of how volatile the markets have become is the simple fact that in 2011, only 24 percent of firms on the 2011 U.S. Fortune 500 list were there 25 years earlier.¹ And while 87 percent of companies experience a severe revenue stall, only 11 percent recover.² Projecting forward, it's likely that only about one-third of today's major corporations will survive as significant businesses for the next quarter-century.³

Given these challenges, how can a company transcend the legacy and weight of its own successes to both survive and thrive in the 21st century? How can it learn to innovate at *Internet speed*, while gaining the crucial agility it needs to roll with multiple market disruptions? And given the extraordinary pace of change, how can businesses maintain their understanding of, let alone *predict*, what is valued in the marketplace?

¹ Cisco IBSG, 2011; Fortune 500, 1987, 2011.

² Olson and van Bever, *Stall Points*, 2008.

³ Baselinemag.com, 2009.

A 21st-Century Strategy for Innovation: Business Virtualization

The Cisco[®] Internet Business Solutions Group (IBSG) sees *Business Virtualization* as the key to 21st-century innovation. Business Virtualization is the ability of corporations to engage and disengage with internal resources or ecosystem partners in a dynamic and real-time fashion, without regard for ownership and location of physical and human assets. In short, collaboration across the entire ecosystem is crucial, and almost *everything is a service*.

Beyond increasing the speed of innovation, Business Virtualization also helps organizations focus their investments where and for as long as they are needed. When everything is a service, non-core processes can be consumed more efficiently.

Once empowered and streamlined by Business Virtualization, a 21st-century corporation is able to focus on the core basis of advantage; it becomes more concerned with retaining customers for long-term gain, rather than for discrete, short-term product sales. Essentially, these businesses are not physically constrained by location; they can deliver experiences anywhere and anytime, virtually; they can extend their sensing and analysis right to the customer; and they can make decisions closer to real time and closer to the customer.

Cisco IBSG undertook a careful study of 222 companies, focusing on the 64 that are thriving in this period of rapidly accelerating change. Those companies stood out in startling ways. For starters, they accounted for 53 percent of the total market capitalization in 2011. The top 64 firms have created \$780 billion in shareholder value in the last six years; the other 158 have *lost* \$547 billion.⁴ Cisco IBSG also found that the leading players boasted new product development times 30 percent faster than the average.⁵ And the best-in-class time to market added 60 percent in innovation sales.⁶

Foremost among our observations of successful companies is a trend toward hyper-innovation driven by steps to make those companies more *virtual*. It is no longer “productivity for productivity’s sake” that will determine success; instead, it will be the quality and speed of innovation. Business Virtualization—with a high level of collaboration, lighter infrastructure, and much faster decision making—is the way to do this.

In this paper, Cisco IBSG will introduce the 10 core principles of Business Virtualization that accelerate and improve innovation through dynamic process design; explore some case studies of companies that have already accelerated their own pace of innovation; and make the case for other companies to act now to begin reaping the essential benefits of Business Virtualization.

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⁴ Cisco IBSG; Thomson ONE; Bloomberg / Businessweek; *Forbes*; *Fast Company*, 2006-2012.

⁵ IRI databases; BCG, April 2012; Cisco IBSG, 2012.

⁶ *Ibid.*

Enabling Collaboration—and Innovation—Across Business Ecosystems

No company is an island unto itself.

If you don't believe that, just try innovating alone in the 21st century. Today, companies simply cannot innovate fast enough by themselves; innovation demands collaboration across an ever-changing ecosystem of partners and highly flexible assets.

Business Virtualization is the key to accomplishing this.

A critical component of innovation today is the ability to rapidly deploy assets when and where they are needed—at any time and by utilizing high-level collaboration. Those resources can be internal or external, demanding a new level of collaboration. But whether driven by employees or partners, they need to be deployed dynamically, with immediacy, agility, and flexibility. Software as a service (SaaS) is just the beginning. An organization must think of utilizing almost *everything as a service*—engineering, design, accounting, whatever—on an on-demand basis.

Companies must also identify their core competencies, and then seek to enhance those processes with partners who can add value in essential ways. When delivered within an as-a-service model, non-core, “contextual” processes will no longer need to be internal, freeing up crucial infrastructure for more essential tasks.

Even five years ago, such high-level collaboration was only being imagined. What makes it possible today is technology: advances in cloud computing, particularly on-demand infrastructure services; the proliferation of mobile devices; the radically shifting ways in which people work and share ideas; and a new and higher level of network intelligence and collaboration technology.

In fact, technology doesn't just make Business Virtualization possible—it makes it *imperative*. The rapid pace of innovation will force companies either to adapt or fall behind. Business Virtualization will allow 21st-Century Corporations to counter new disruptions with a leaner infrastructure and more flexible internal business processes. By also relying on the domain expertise of outside ecosystem partners, these companies will be able to engage and disengage those third-party resources in a dynamic, real-time manner, with less concern for ownership. Given high-level collaboration tools and outsourced cloud services, the very location of those physical and human assets will become less relevant.

Beyond that, as 21st-century corporations embrace Business Virtualization, there will be a shift from a “physical” to a “virtual” business model:

- Companies that are used to driving their business value through “tangible” physical or financial assets will be forced to adopt virtual, innovation-driven values. “Intangibles” such as speed to market, intellectual property, and the creation of a unique, differentiated customer experience will be paramount (see Figure 1). Among innovative companies, intangibles already fuel 43 percent of shareholder value.⁷
- Many assets that are now fixed will become variable. For many companies, scaling and agility currently depend on large, capital-intensive physical assets. This can result in significant excess capacity when provisioning exceeds need. With Business

⁷ Sources: Cisco IBSG, 2012; Thomson ONE.

Virtualization, however, costs are tied directly to usage, optimizing asset utilization (when almost *everything* is a service, each service can be called upon only when needed). Overall, businesses can “right size” their operations, becoming much leaner and more efficient in the process.

- In the past, businesses were rooted in place. Relationships with employees, suppliers, partners, and customers dictated a location-centric approach. Business Virtualization is *location-agnostic*. It leverages experts from both inside and outside the organization to drive scale and scope. Effective collaboration is possible anytime, anywhere.

The 10 Principles of Business Virtualization— and the Companies that Live Them

In Cisco IBSG’s engagement work with innovative companies, we have observed organizations embracing different dimensions of Business Virtualization. But regardless of where they are in adopting the concept, patterns and essential steps emerge. These organizations need to establish the foundational agility required to maintain their competitive advantage; they require a tighter focus and investment on their core competencies while seeking outside service options for many non-core processes; and they aim to establish and manage a dynamic ecosystem of partners.

To put all of this into practice, organizations must *Envision*, *Enable*, *Execute*, and *Monitor* the processes of Business Virtualization. As a foundation for this journey, Cisco IBSG has identified 10 principles that will define the 21st-Century Corporation:

Envision

1. Choose your path of differentiation: product, experience, or cost.

Enable

2. Move decision making closer to the customer, and increase the level of collaboration within all levels of the business.
3. Advocate the use of partnerships to speed innovation across the value chain.
4. Align your business toward a greater share of annuity revenue models.
5. Leverage your virtualization infrastructure to increase new market entrance and lower cost.
6. Drive a “Work-Your-Way” environment with flexible IT consumption models (such as “Bring Your Own Device” to work).

Execute

7. Implement an open innovation model to increase speed and shorten the ideation-to-cash process.
8. Shift non-core services and operations to an on-demand, fixed-cost model.

Monitor

9. Build a listening infrastructure—create a sensing mechanism that allows for immediate reactions to customer feedback.
10. Instill the use of customer lifetime value as your key decision influencer.

As we have seen, some companies have met the challenge of hyper-innovation head-on and are already applying these 10 principles in varying degrees. But who are they, and what are their secrets?

Cisco IBSG has linked some highly innovative companies to specific principles. Here are a few examples:

- **Ritz-Carlton** has moved decision making closer to the customer (principle 2). The hotel chain empowers employees at all levels to use company funds for immediate resolution of guest complaints.⁸
- **Samsung** has advocated the use of partnerships to speed innovation across its value chain (principle 3). With its “Partners in Innovation” program, Samsung has empowered its channel partners to provide innovative products and solutions to customers, thereby enhancing the value of being a Samsung customer.⁹
- **Tesco** has leveraged its virtualization infrastructure to increase new market entrance and reduce risk (principle 5). The retailer deployed a new set of Cisco collaboration tools, enabling it to support international growth and reduce operating costs by implementing its operating model faster in new geographies.¹⁰
- **GE** has implemented an open innovation model (principle 7). The company is working on a new global crowdsourcing platform that aims to reduce time taken to design and manufacture complex “cyber-physical systems.” It brings together a global community of experts and offers a showcase for their ideas.¹¹
- **Target** has built a listening infrastructure (principle 9). Its POS Data analysis is predicting important events in the customer’s life and pitching products accordingly. It uses customer data stored under unique guest IDs to optimize operational variables such as loyalty programs and delivery times.¹²
- **IBM** has instilled the use of customer lifetime value (CLV) as a key decision influencer (principle 10). Its CLV-based resource allocation tool was used for its marketing programs, resulting in a revenue surge of \$20 million (a tenfold increase) without any changes in the level of investment.¹³

One company that epitomizes Business Virtualization in action is Zynga, creator of FarmVille and other games. The company, which boasts 250 million active users,¹⁴ follows the philosophy of “scale fast or fail fast” and drives innovation through its *intangible* assets. As a result, the company is incredibly light on infrastructure, processes, and employees. Outside cloud-based partners assist with core innovation, but Zynga also outsources nonessential, back-office services. Zynga developed 17 new games in 2011, and typically its usage can spike between 1 million to 60 million users within days.¹⁵ But by launching on EC2, Amazon’s scalable, pay-as-you-go cloud service, Zynga paid only for the capacity it needs. Today, Zynga utilizes a combination of its own cloud infrastructure and outside services. Based on

⁸ Cisco IBSG, 2012; annual reports and press releases, 2009-2011.

⁹ Cisco IBSG, 2012; *The Asia Career Times*, July 2011; annual reports.

¹⁰ Cisco IBSG, 2012; annual reports; Forrester, November 2011.

¹¹ Forrester Research, 2011; Mass Hightech, April 2012.

¹² Cisco IBSG, 2010-2012; *Forbes*, October 2009; Eloqua; Socialbakers, Buddy Media, 2012.

¹³ “The Power of CLV: Managing Customer Lifetime Value at IBM,” Marketing Science / INFORMS, 2008.

¹⁴ Cisco IBSG, 2012; “How Zynga Uses the Cloud,” Charles Babcock, 2011.

¹⁵ Ibid.

careful analysis of gamers' usage patterns, a new game is migrated to the private cloud, the hybrid cloud, or killed.¹⁶

In case studies, Cisco IBSG found an abundance of other large companies and start-ups that are already taking advantage of these new business paradigms. A new business model and another example of a virtualized business, Kickstarter.com is pioneering a crowd-funding platform that enables the public to subsidize conceptual projects. Essentially, the concept is *venture capital as a service*. Anyone with a good idea can submit a proposal to Kickstarter, and anyone who feels inspired can invest. So, sensing the need for a virtualized business, Kickstarter carved out a niche. In the process, it became highly virtualized. The start-up partners with Amazon Payments, which handles the receipt and disbursement of the funding. And, Kickstarter's funding source is not a tangible asset. Indeed, Kickstarter's main asset is not about money, but about the intangible ideas behind its technology and how it takes advantage of the network. Started in 2009, the company's run rate in 2011 was \$99,344,382.¹⁷

Similarly, CrowdFlower.com is an innovative, highly virtualized start-up that crowd-sources talent, becoming, in effect, a "people-as-a-service" partner. Billing itself as the "World's Largest Workforce"—including data analysts, scientists, writers, artists, and engineers—CrowdFlower.com aims to solve problems that include product categorization, business lead verification, and content creation. One company that utilized CrowdFlower is eBay. James Rubinstein of eBay described the partnership this way: "CrowdFlower gives us the on-demand scalability, flexibility, and speed of the crowd that we need to improve eBay products."¹⁸

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Getting There from Here: Stepping Up to the Challenges of the 21st-Century Corporation

The companies we have highlighted are already reaping the benefits of Business Virtualization. They are leaner, lighter in infrastructure thanks to outside partnerships, and highly collaborative both inside and outside their organizations. In varying degrees, they are *living* the 10 Principles of Business Virtualization.

Given the trends and dangers we have already discussed, other organizations have a great need to act now in order to accelerate the speed and agility of their own innovations. As we have seen, in 2011, only 24 percent of firms on the 2011 U.S. Fortune 500 list were there 25 years earlier. And the future may be even less kind to companies that do not accelerate their speed of innovation. Business Virtualization—enabled by cloud, mobility, and collaboration—is the way forward.

¹⁶ Ibid.

¹⁷ Business Insider, 2012; Kickstarter.com, January 2012; POF, May 2012.

¹⁸ CrowdFlower.com, 2012.

Those technologies are just the first step, however. Indeed, cloud, mobility, and collaboration make it possible for enterprises to be dynamic and focus on speed of innovation. But Business Virtualization goes beyond technology—it requires new business models, new software architectures, and new business entities and partnerships to make it all possible.

In this brave new world, the senior technology executive will become the most transformational business leader. He or she will move beyond the status quo, translating requirements into technology direction, while also being uniquely responsible for enabling and managing Business Virtualization. Cisco IBSG's 10 Principles for Business Virtualization can provide a guideline for the process.

Kodak and Blockbuster, and many others like them, did not see over the horizon to the massive market disruptions that upended their business models. No doubt, the next five years will bring equal or much greater disruptions throughout the marketplace. It is up to decision makers—in particular, senior technology executives—to ensure that their organizations are prepared.

Business Virtualization is the key to meeting the challenges of the 21st-Century Corporation.

More Information

Cisco IBSG (Internet Business Solutions Group) drives market value creation for our customers by delivering industry-shaping thought leadership, CXO-level consulting services, and innovative solution design and incubation. By connecting strategy, process, and technology, Cisco IBSG acts as a trusted adviser to help customers make transformative decisions that turn great ideas into value realized.

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