

Under the Buzz

Commentary on Business Strategy Issues for Executives in Enterprise Systems & Software Companies

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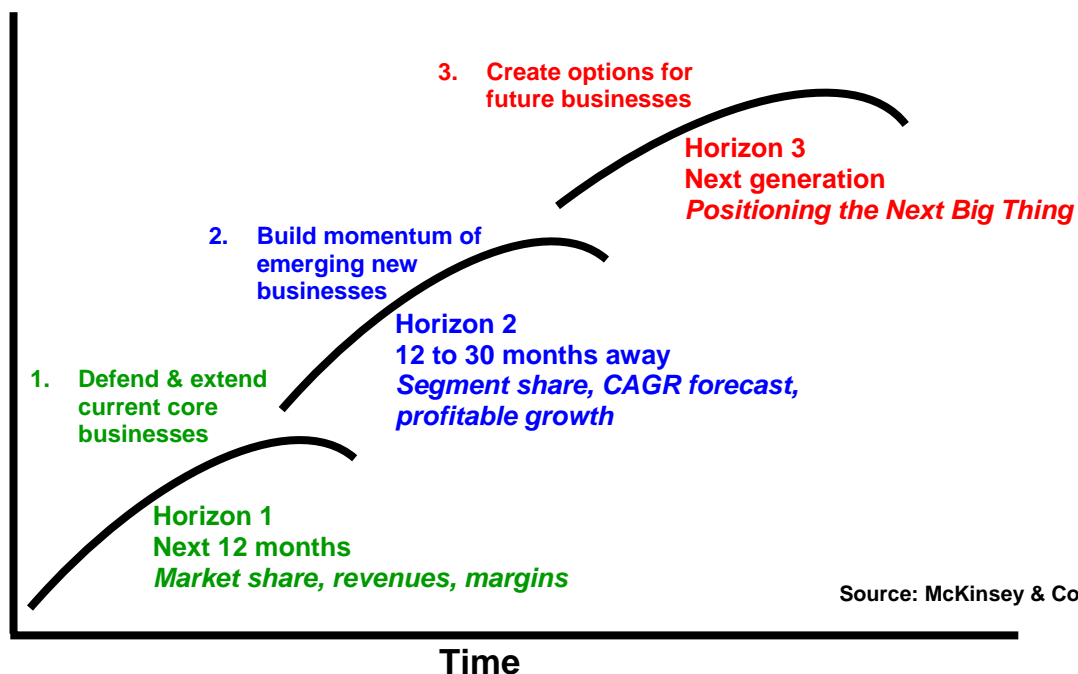
Filling the Strategy Vacuum

How to Plan Effectively Across Multiple Time Horizons

While the enterprise software industry continues to pursue new paths to growth via product innovation, smarter sales strategy, and other approaches, it continues to be constrained by its own limitations more than any external factors. In fact, the most pernicious single threat that I see to the long-term viability of most companies is - believe it or not - a self-inflicted handicap that entrepreneurs and executives unintentionally impose on their organizations.

The "Horizon 2 Vacuum" is how I have come to refer to this problem. Horizon 2 is the middle portion of the Three Horizons planning concept first introduced by McKinsey & Co. in the late 90s(*), and since modified by our firm to provide critical metrics and other indicators to help executives manage their business across multiple horizons (see diagram below). Why is "Horizon 2" so important? This is my main theme in this article.

Three Horizons Planning Model - Goals & Metrics



My observation is that even the most successful players, starting with Microsoft, Oracle, SAP, and Symantec among software companies, and IBM, Cisco, HP, and Juniper among systems companies, experience frequent vacuums in their Horizon 2 portfolios that result in uninspiring or difficult-to-sustain growth. But while this vacuum creates discomfort for these larger players, it can - and frequently does - jeopardize the survival of midsized and smaller tech companies on a daily basis.

Which brings me to my first point. Despite what executives and boards say about the capital markets' preoccupation with quarterly earnings, as a justification for their own short-termism, investors are actually focused on gauging both a company's performance and its health for the long term. This is because when an investor buys a share in a company, the company's past performance is already priced into what they pay for it, and their reason for acquiring the stock is that they are betting that the company's future performance will be even more profitable in the short and long term.

Therefore, what investors look at is a company's portfolio of businesses, and what they want to see is that there are one or more credible businesses for each time horizon. Thus, in Horizon 1, they want to know how the company is managing to defend and extend its current core businesses; in Horizon 2 they want to see how the company is actually building momentum in emerging new businesses (rather than just talking about doing so, or failing to do so in any clear and meaningful way, which is extremely commonplace); and in Horizon 3 they want to hear about future opportunities that the company intends to develop in a way that conveys an exciting and credible vision.

What the Three Horizons are Really About

So, at a more detailed level, what do these horizons consist of and where are the challenges in managing the three together in a balanced manner in order to project a company's short and long term value? Here are the key metrics and "anti-metrics" that indicate whether a business is performing adequately or not in this timeframe:

Horizon 1 is about executing today's existing business and revenue plan; the horizon is, shall we say, from now to 12 months out; key metrics to gauge success are market share, revenues, or margins, or a blend thereof.

Horizon 2 is about managing emerging product and/or service offerings to initial adoption and eventually market segment leadership and dominance; the horizon covers the midterm - shall we say, the next 18 months or so; key metrics include segment share, profitable growth, and CAGR, or a mix thereof.

Horizon 3 is about defining and evangelizing a compelling vision of how your company is going to contribute value to major customers in the future via technologies and expertise that are still in the nascent stage; in approximate terms, this horizon covers the timeframe outside of 30 months away as far as 5 years from now. Key metrics indicating whether the company has managed to position the company's Next Big Thing in compelling terms include one or two successful custom projects with visionary customers who understand that some of the elements of the new technology are missing or need to be developed as they go; the number of pragmatist and other customers who cite your company's long-term vision and roadmap as a key component in their decisions to buy the company's Horizon 1 and Horizon 2 offerings; thirdly, the number of industry analysts who cite the company's vision in their magic quadrants (Gartner) and other models.

The main problems for tech company executives in managing across these three time horizons - even if they don't do so consciously - tend to fall into one or more of these related buckets:

- (a) Executives and employees get bored with today's offerings and today's growth, competition, problems, and obstacles; "metal fatigue" sets in, and people look for new things to get excited about (the *bright shiny object* syndrome);
- (b) So they look to the future, invent some new concept or architecture that they can portray on beautifully-structured PowerPoint slides; they plug this into their product roadmap to make it seem more real and immediate, and start evangelizing it as something customers can buy now and install very soon;
- (c) However, customers, having been burned by other vendors in the past, sense that something isn't right because they read their news and confer with colleagues, so they decide that the "future" thing is just that - something that may or may not turn out to be valuable at some point in the future;
- (d) Meanwhile, vendors have managed to convince themselves that the Next Big Thing is indeed available in the immediate future, so they ramp resources and expenditures on marketing and feet on the street - only to encounter a deafening silence or at best, one or two friendly customers to try out the new offering in "pilot" projects;
- (e) What's happened in this short pantomime is that the company has forgotten to insert something tangible and achievable into Horizon 2 in the form (preferably) of a target set of customers with a shared serious business problem that can be substantially addressed with the new offering, and can thus demonstrate the all-important evidence to skeptical and supportive customers alike - i.e., evidence of the actionable steps to ascend the "staircase to heaven." By not finding a single, visible target market to adopt their new offering inside a complete solution to a mission-critical problem, they frequently end up with a big hole (or vacuum) in the 12-30 month horizon.

In the past, categories that today have finally achieved respectability but endured many false starts because of the instant-gratification anxiety in tech companies include ERP (the category formerly known as MRP I, then MRP II), Sales Force Automation, Business Intelligence, Data Warehousing, and many others. In today's enterprise software marketplace, there are a number of supposed "next big things" such as Customer Experience Management, RFID, IP Telephony, Identity Mgmt, SOA, and so on, that are still relatively nascent. Most of the time vendors with a vested interest in one or more of these emerging categories do little more than reiterate their predictions that "2007 will be the year of (category name)" and then launch new marketing and sales fire drills to create demand wherever they can see potential customer demand. Unfortunately, by behaving as if the future is now, they mislead their most loyal customers and prospects and end up wasting resources and time on inconclusive sales campaigns.

Why Horizon 2 is So Challenging

Even when customers are aware of these horizons, they have a tendency to treat them differently in their management and planning systems as well as their organization and allocation of resources:

- **Financial systems tend to overstate the value of Horizon 1**
 - Where all the execution and accounting action is
- **Strategic planning tends to overstate the value of Horizon 3**
 - Where all the beautiful things live
- **Organizations fail to come to grips with the realities of Horizon 2**
 - Where growth and market power must come from
 - World of transition and contradiction
 - Looks ugly compared to either of the other two horizons

Why is Horizon 2 so hard for tech companies to deal with? To start "at the top," large and maturing companies lose the requisite humility - and the institutional memory - to go back to the days when they were first successful and invest in one or two tightly focused Horizon 2 initiatives. Instead, they kick off a half-dozen or more new initiatives at any one time. Since no single initiative is treated as mission-critical - with penalties for failure - most of them fail or achieve

moderate results at best. Medium-sized companies tend to imitate large companies, indulging themselves in the same hubris as befalls their bigger brethren; and small companies believe that time is too short to focus and discipline themselves, because they fear losing out to larger competitors.

Best practices for Managing Across the Three Horizons

In order to manage the three horizons effectively, we recommend the following approach:

- **Force a horizon-based allocation**
 - Make management declare a target percentage of resources for each horizon
 - Block migration of resources across horizon boundaries
- **Apply different metrics to each horizon**
 - Measure Horizon 1 like an accountant
 - Measure Horizon 2 like an investment analyst
 - Measure Horizon 3 like an industry analyst
- **Hold managers accountable by horizon**
 - Do not let performance in one horizon substitute for performance in another

Besides these guidelines, there are a host of organizational steps to manage across the three horizons, including deploying ad hoc cross-functional teams composed of fast-track inventor/entrepreneur types on short missions with clear objectives and measurement criteria. On the external front, executives must learn to conduct a different dialogue with key stakeholders principally customers, analysts, and partners - to remind them of the company's necessarily multi-faceted business objectives.

(*) "*The Alchemy of Growth*" (1999) co-authored by Mehrdad Baghai, Stephen Coley, and David White. Also, "*How to Escape the Short-Term Trap*," article authored by Ian Davis of McKinsey, published in the *Financial Times*, April 2005.

Under the Buzz offers commentary on enterprise software and systems business and management issues. The goal is to provide provocative and accurate insights into the latest events and thinking shaping this continually evolving technology sector. *Under the Buzz* also provides commentary on strategies for building sustainable competitive differentiation and maximizing market valuation.

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