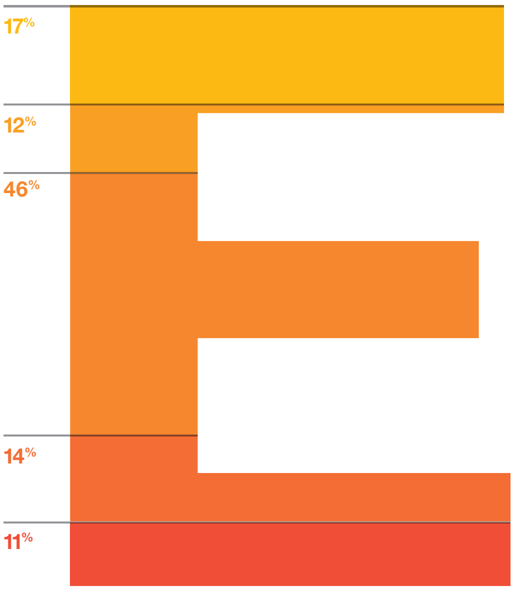


Reinventing the rules of engagement

CEO insights from the Global C-suite Study

IBM Institute for Business Value

Chief Executive Officer insights from the IBM C-suite Study

This report draws input from the 4183 CxOs we interviewed as part of IBM's first study of the entire C-suite. It is the 17th in the ongoing series of CxO studies developed by the IBM Institute for Business Value. We now have data from more than 23,000 interviews stretching back to 2003.

Total CEOs interviewed	884
Japan	149
Asia Pacific	105
Europe, Middle East and Africa	404
North America	123
South America	103

Reinventing the rules of engagement

In the first installment of our Global C-suite Study, we spoke in person with 4,183 top executives covering more than 20 industries to find out how CxOs are earning the loyalty of digitally enfranchised customers and citizens. In this report, we delve more deeply into the perspectives of the 884 CEOs we interviewed.

Every two years since 2004, we have met with CEOs and public sector leaders around the world to understand their points of view on issues ranging from globalization to talent. For many years, CEOs consistently identified market forces as the biggest driver of change. Then in 2012, CEOs for the first time placed technology at the top of the list of issues they believed would exert the strongest influence on their organizations and strategy.

This year, CEOs again ranked technology first. Believing the impact of emerging technologies on their organizations will be profound, CEOs anticipate three areas for action:

- Embrace disruption
- Build shared value
- Dare to be open

Embrace disruption

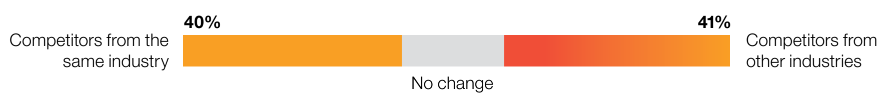
Every era has its breakthrough innovations. Our era has the runaway kind. Runaway innovation sets off when new connections form at massive scale, linking institutions and individuals with diverse experiences and disparate objectives. Ideas circulate more freely, combine in new ways and break through paradigms with greater frequency.

Runaway innovation is insatiable. It captures the imagination of individuals and empowers customers and employees alike to challenge the status quo — *leaving organizations to catch up*. It jumps from one industry to the next, bringing down once formidable boundaries and radically reshaping enterprise purpose.

More than two in five CEOs now expect their next competitive threat to come from organizations outside their industries (see Figure 1). These new competitors aren't just set to steal market share. They are upsetting whole industries; reinventing *how* value is created; and redefining what *constitutes* value. An almost single-minded focus on "capturing" value for the benefit of the individual organization is giving way to innovation that drives *mutual* value for the widest group of stakeholders possible — customers, employees, partners and shareholders alike.

Figure 1

Around the corner: *A growing number of CEOs face challengers from outside their industries*



Moreover, every enterprise is laboring to catch up with innovations taken up initially by individuals. First, employees brought their mobile devices to work; next, they brought social networks inside. This led to entirely new ways of working — the social business. Most recently, the “sharing economy” — where individuals trade with each other for everything from places to stay overnight to business services — has created a new construct for commerce. That’s a competitive threat unimaginable just a few years ago.

Bye-bye industry boundaries

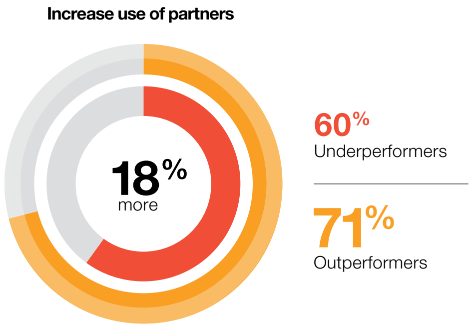
In the past, industries were disrupted when companies swooped in to attack large pieces of the value chain. Today, innovators and specialists offer a different proposition. Can they optimize a real-time supply chain better than you? Are they renowned for creating individualized customer experiences? Are they masters of augmented reality? Digital technologies, including analytics and cloud, make it possible to convene, orchestrate and optimize complex value chains, allowing many organizations to move into adjacent spaces outside their industries. Some will be your next partners, and some your next competitors.

New entrants are already leveraging technology to innovate and disintermediate discrete parts of the financial services value chain, for example. Peer-to-peer lenders have sprung up to match borrowers with savers. Telecommunications companies have created more convenient payment services on smartphones. And new entrants like Google Wallet and Square are disintermediating traditional payment mechanisms. Echoing the sentiment of leaders in other industries, one CEO observed, “Banking is needed, but banks…I’m not so sure.”

“Whatever we do, we should be asking: what is the impact for our clients?”

Dirk Vanderschrick, Member of the Management Board, Head of Retail and Commercial Banking, Belfius, Belgium

Figure 2
Branching out: *CEOs are expanding their network of partners in pursuit of innovation*



Ikea, a company that redefined how we think about furniture, is applying its expertise to home construction and hotels. Audio specialist Sennheiser partnered with Adidas to develop sweat-proof, movement-resistant earphones and an audio coaching device complete with a heart monitor. Others are integrating global positioning system (GPS) technology in athletic gear, allowing runners to map routes and run against their personal records — or those of friends.

Innovation turns a corner

The value of looking outside the organization is all too apparent. Almost half of CEOs expect their organizations to source innovation from the outside — participating in open innovation networks and joining up with new partners. Seven in ten CEOs of outperforming organizations are now primed to increase their partner network in the pursuit of innovation (see Figure 2). And already, one-quarter of CEOs are anticipating the time when some of those partners will come from among their traditional competitors.

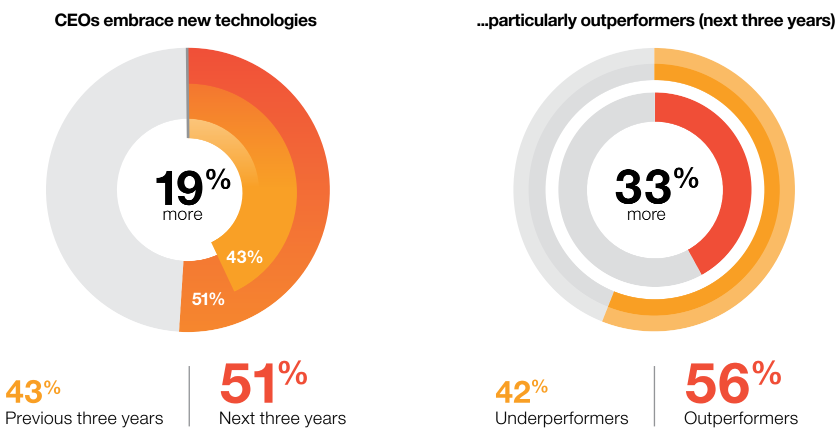
Leaders will need to think carefully about how they align strategic interests and divvy up the value that is created. Of equal importance will be how they integrate what is just as essential — a technical foundation to share big data across organizations, provide seamless customer experiences and adapt to frequent changes in their operating models.

Prepare to converge

Asked their strategy for guiding their organizations to the future, CEOs rank growing top-line revenue as their first priority. Embracing new technologies is second, and reveals what they believe will get them there: 51 percent plan to focus on new technologies in the next three years — up from 43 percent in the previous three years. CEOs of outperforming enterprises are pushing even further; they are 33 percent more likely than their peers in underperforming enterprises to make emerging technology the top strategic priority over the next three years (see Figure 3).

Figure 3

Tech at the top: *CEOs of outperforming organizations are pushing further, faster*



"We want to provide an experience that makes a difference."

Isidoro Unda Urzáiz, CEO, Atradius, Netherlands

> *"We are facing important changes, therefore we should take full advantage of our situation and transform our way of doing things by harnessing new technologies."*
>
> CEO of a major retailer, Europe

This intensified focus on technology is warranted. Most CEOs view mobility as core to innovation, for example. Yet just 43 percent believe their current mobile strategy enables them to conduct business regardless of the location. Many CEOs also admit that they don't fully understand how to structure their enterprises as social businesses, or apply social technology to customer interactions. That can be a drag on their ambitions for collaboration.

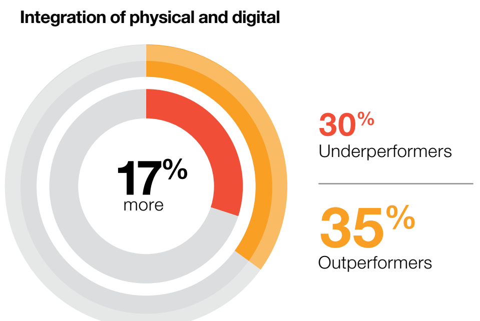
The challenge looms larger when you consider that all of these nascent technologies are just beginning to *converge*. As social, mobile, analytics and cloud technologies intersect and amplify each other, entirely new possibilities take shape. Any strategy to capitalize on them will have to favor continuous iteration, make room for widespread experimentation and bring together not just the experiences and ideas of the C-suite, but also an expanding partner base.

Converging technologies push the envelope on digital innovations. But the biggest disruption most often occurs at the intersection of the physical and digital. "Wallpaper stores" — virtual retailing on subway platforms — allow commuters to shop in transit and receive the goods soon after they return home. Medical monitoring devices in everything from smart phones to asthma inhalers are redefining personalized healthcare. And 3-D printing, combined with open-source design, is dramatically lowering the price of costly prosthetics — an innovation jumpstarted by a man in South Africa who lost his hand in an accident, and set out to make a new "robohand" himself.[1]

Yet the vast majority of CEOs heading both outperforming and underperforming organizations admit that they still haven't got an integrated digital and physical strategy (see Figure 4). What's holding them back? CEOs cite their biggest challenge as understanding how to use social media. But they are also struggling to quantify its return on investment with the distractions posed by competing priorities.

Organizations face a choice: They can wait for the entrance of a strong new competitor to spur them to action. Or they can push past institutional inertia and transform now.

Figure 4
Hanging back: *Only one-third of organizations have integrated their digital strategies into their physical infrastructure and products*



"We are adopting new technologies, business processes, and thought processes in order to enable rapid change, growth and innovation within our business."

CEO of a leading professional services and technology business, United States

Taking action:

Move out of bounds

Competition is coming from unexpected places — organizations that have honed new capabilities and mastered new business models by serving markets different than yours. Bringing together people from different industries, backgrounds, regions — and even generations — will be essential to predict and respond to new competitive threats. Expanding partnerships to deepen innovation capabilities will speed the discovery of new technologies and new business models.

Create experimentation spaces

Runaway innovation requires places and spaces where people can think, interact and experiment. The creation of these innovation spaces should be a priority. These should include: 1) Physical spaces where co-located people with different backgrounds can cross-pollinate each other's ideas. 2) Virtual spaces where large numbers of people across different locations can focus on specific topics. 3) Personal spaces where individuals can take time away from their day-to-day activities to focus on strategic possibilities.

Build business ecosystems

Business environments are beginning to evolve from markets to ecosystems. Technologies like cloud make the complex orchestration of ecosystems possible. Organizations that identify new ways to serve customers holistically will define new business ecosystems and benefit the most. Finding partners with the right strategic and technological fit will be essential.

Build shared value

Many organizations are facing disruption from new competitors. A growing number are inviting their customers to disrupt them *first*.

CEOs told us that shaking up the status quo in their organizations is a priority. Some are even asking: Who could better challenge assumptions than our customers? Yet a surprising proportion of CEOs worry that their colleagues in the C-suite are out of touch with customers (see Figure 5).

The generational divide created by mobile and social media is one cause for concern. As the CEO of an international energy company put it: "Our board believes they know and understand social media. They truly don't. They aren't users and they can't fully appreciate the impact social media will have."

But the same technologies that have created this generational divide have also produced the means with which to ask customers and citizens what organizations can do differently. And, increasingly, digitally enfranchised customers of all ages are sharing their views loudly and freely on social networks — creating advantage for organizations with the capacity to listen.

Figure 5
Alarm bells: *Some CEOs fear their C-suite colleagues don't understand how customers are changing*

My C-suite executives do not understand changes in our customers or the marketplace

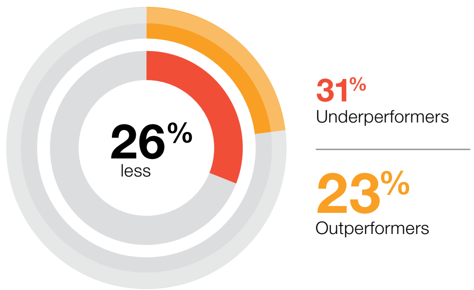
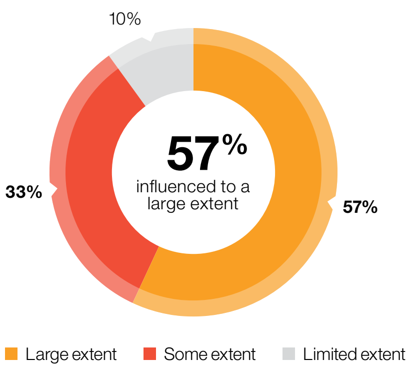


Figure 6

Weighing in: *CEOs say customers now have considerable influence on their organizations*

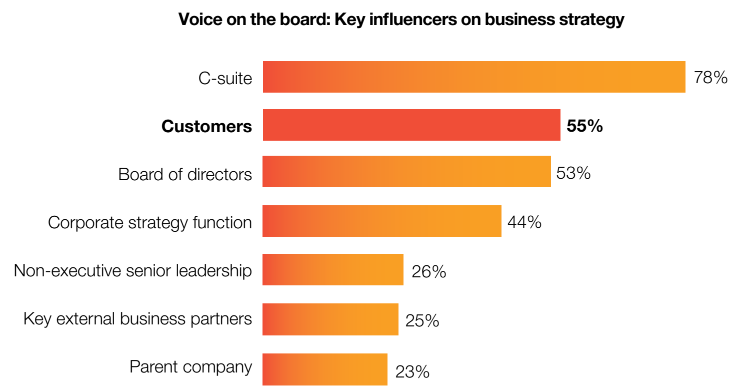


Leading CEOs are going even further. They are looking for new ways to proactively engage their customers and get their direct input — not just on their products or services, but on every aspect of their organizations. They are motivated to act with urgency, to change course, even shift their strategies based on the direct influence of the customer. Six out of ten CEOs told us that their customers now have significant influence on their organizations (see Figure 6).

CEOs are ready to share control of areas typically considered their domain — the strategic vision and business strategy of their enterprises. In fact, CEOs rank customers second only to the C-suite in terms of their influence on organizational strategy — ahead of the Board of Directors and Corporate strategy function (see Figure 7).

Figure 7

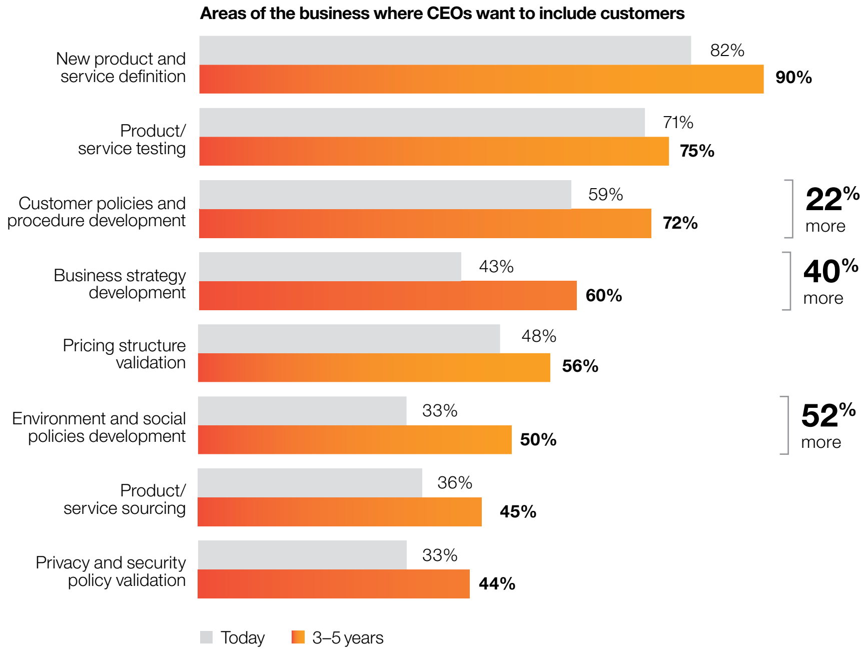
Power players: *CEOs think customers wield more influence than all but the C-suite*



In the next few years, a growing number of CEOs expect to include customers in every part of their business, from pricing structure to product testing (see Figure 8). Surprisingly, though, CEOs rank customer influence relatively low on the issue of security and privacy. While 60 percent are ready to include customers in their organization's development of business strategy, just 44 percent are considering what their customers have to say about privacy.

Figure 8

Ear to the ground: *CEOs want to include customers in many more areas of their business*



"We're using external suppliers and customer workshops to bring the voice of the customer into our enterprise. We're also looking at brands we admire in other industries and meeting people from these companies to find out how we can adapt their experiences to our enterprise."

Paul Matthews, CEO, Standard Life, United Kingdom

> *"You have to 'marry' with your customers and share experiences, good or bad, to gain trust."*

CEO of a major professional services business, Europe

Every effort to better understand customers and personalize products, services and experiences to their individual expectations is predicated on accessing and sharing the abundance of data that is now *potentially* available for use. What customers are willing to share will depend in large part on how organizations protect their privacy.

This is not an area where organizations can afford to make assumptions that their current or future plans are good enough. Instead it requires ongoing validation over time, both internally and with customers, as both norms and expectations are changing rapidly.

Let go of the reins

For some organizations, like Honeywell, the best approach to acting on customer influence is a customer board of advisors who convene regularly to collaborate with senior leaders. Typically, these groups tackle topics ranging from the organization's business strategy and emerging trends that could reshape a company's product offerings, to its innovation initiatives. Such boards are made up of customers who bring different experiences and viewpoints to the table. Typically, they make a long-term commitment to each other — striving to act on exchanged ideas.

Some organizations are crowd sourcing their corporate philanthropy — inviting customers to submit ideas for worthy causes, and giving them the deciding vote. Some companies turn to social networks to ask all their customers what new products and services they'd like to see next. One smartphone producer in China, Xiaomi, not only asks its customers on Weibo to vote on such questions, it releases a new version of its operating system each week in response. Its customers continuously experience the direct result of their influence.

When organizations seek customer influence, they cede absolute control in pursuit of mutual value. Inevitably, they transform strategy as a result. And in many ways, the capacity to act on customer influence — to iterate and change direction with considerable frequency — is just as transformational to their operating structures.

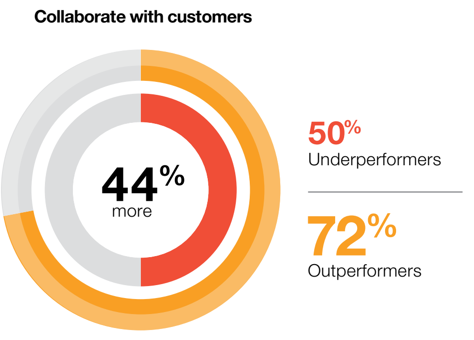
All together now

Bringing customers inside the business and creating an agile operation that can act rapidly and repeatedly on their input requires courage. But the best leaders understand that the benefits far outweigh the risks. It's no accident that 72 percent of CEOs running outperforming enterprises have built organizations that collaborate closely with their customers (see Figure 9).

Such CEOs recognize that, as value chains atomize and industries converge, new ecosystems will emerge. These ecosystems will be organized around activities that are meaningful to customers. For example, airlines will transition toward a travel experience ecosystem and automotive companies will transition from a focus on vehicles to mobility. Individuals, as well as institutions, will directly participate. Think of that eventuality as the "everyone-to-everyone economy."

Figure 9

Close work: *CEOs of outperforming enterprises are more likely to make customer collaboration a top priority*



Taking action:

Blend the virtual with the physical

The opportunities to learn from customers' actions — where they go click by click, or step by step, and what they do in real-time — holds great promise. Virtual closets, cars, and showrooms model the real world and provide an up-close view of customers' actions. Digital displays and mobile services create the kind of individualized service — and understanding — that can influence organizations to rethink everything from how they engage customers to how they deliver their products and services.

Learn with your customers

Virtual events and contests are a great first step in customer co-design and co-development, creating an environment to experiment and learn about the benefits of customer collaboration, as well as the challenges. Don't view these efforts as a marketing exercise or promotion, but instead focus on soliciting and capturing ideas that can be brought back to the research and development divisions.

Operationalize your customer community

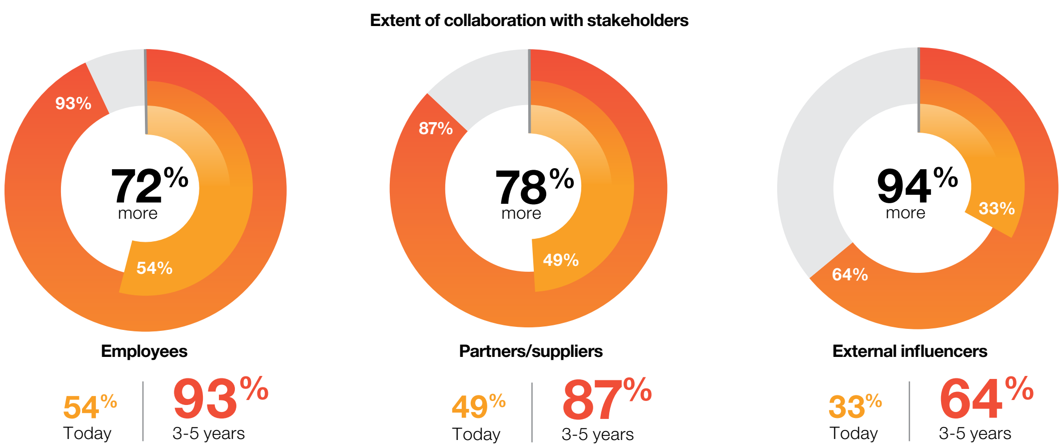
Some organizations have established communities of customers that provide service and support to each other, effectively "outsourcing" their operations. Look for opportunities to bring customers into your operations or sales and service functions. But keep in mind that the community's members are not your employees and can't be managed as such.

Dare to be open

The benefits of collaboration have long been apparent. The "science" of collaboration is just emerging. We are beginning to better understand *how* collaboration works — how to foster human connections across complex networks, create new models of engagement and cultures of transparency.

CEOs know they can't afford to wait. In the past couple of years, they've gained experience — and benefits — from closer collaboration with customers. Now, they're prepared to extend collaboration more holistically across the full ecosystem. The number who expect to collaborate with employees, partners and influencers will nearly double in the next three to five years (see Figure 10).

Figure 10
Double down: *Collaboration rapidly expands*



“We’re innovating in collaboration with our clients–promoting more interaction between our R&D function and ‘factories of customers,’ and opening up our minds.”

Stefano Porcellini, Group General Manager, Biesse SpA, Italy

As the propensity to collaborate has grown, organizations are evolving just about every facet of their businesses. For example, crowd funding, a popular way to finance everything from small projects to start-up businesses, is now being used *inside* organizations to select and prioritize innovation initiatives. These companies aren’t just giving their employees a vote, they are empowering them by giving them funding to allocate across projects.

Collaboration is hardly a new concept for scientists, but some organizations are pioneering a new model for R&D that introduces a new application of crowd sourcing. Because consumer confidence and trust in science has eroded dramatically in recent years, these organizations—typically a consortium of industry and academia—are seeking independent verification from the start of research, rather than after it’s published. At the outset, research data, hypotheses, models and processes are crowd sourced to scientists worldwide to test, probe and verify—or not. Absolute transparency across independent parties with a wide range of backgrounds establishes “trust in the science” across the wider scientific community, consumers and regulators alike.

Giffgaff, a subsidiary of the UK-based mobile network O2, has redefined customer service as customer-to-customer collaboration by encouraging its users to help each other, awarding valuable points for successful interactions. It also invites customers to make business suggestions on its online boards, and doesn’t flinch from candid conversations about business considerations like profitability.

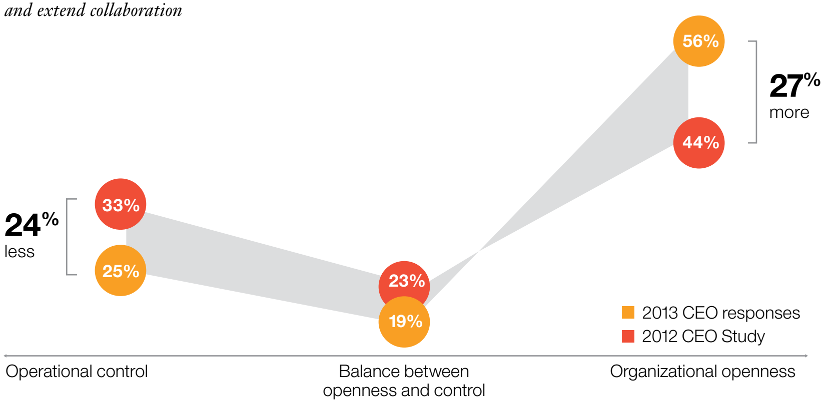
Open wide

In many respects, trust is the currency of social business. The other side of the coin is data. To facilitate both fact-based consensus and data-driven innovation discoveries, data must be democratized: made widely available and immediately accessible. We've seen in our studies that the most analytically sophisticated organizations share data more freely. Once they do so, it alters the power structure, effectively flattening the organization and creating a culture of openness and transparency.

CEOs in just about every industry have learned that customers, partners and employees that collaborate can go further, faster in an era of runaway innovation. Many are pushing the boundaries on their organizations as a result — opening up to empower collaboration among individuals, and moving away from command-and-control hierarchies. In just one year the number of CEOs determined to open up their organizations has increased an astounding 27 percent (see Figure 11).

Figure 11

Letting go: *A rapidly growing number of CEOs are opening up their organizations to empower individuals and extend collaboration*



"Let the data talk. Don't rely on opinion."

David Thodey, CEO, Telstra, Australia

Taking action:

Amplify collaboration with data

While the benefits of collaboration are well understood, the mechanics are less so. Analysis of optimal collaboration structures and processes can motivate and magnify the benefits. Look at network patterns within the organization to promote the collaborative models that will work best for you: capture and incorporate data from social platforms, screen new employees ahead of time for collaborative behaviors and measure outcomes with vigilance.

Redefine sharing

In an open and collaborative environment, everyone should be rewarded for sharing — and not just knowledge. Employees should be incentivized to share their skills, their experiences, their networks, and most importantly, a sense of common purpose. Reward criteria should reflect overall organization objectives — whether that is a plant manager supporting business growth, or an HR officer supporting the overall end-customer experience of employees.

Seek inspiration from millennial employees

For many employees, it won't be easy to be "open." Millennials, however, are already there. Collaboration, flexibility and creativity are part of their DNA. Generation Y can provide a valuable perspective on how collaboration might work best across the organization. By establishing millennials as reverse mentors or coaches, organizations can encourage openness and shared engagement.

New rules of engagement:

Open organizations are redefining the ground rules on collaboration. New approaches emerge from these examples:

Get personal. Increasingly call centers aren't measuring how fast their operators handle a transaction. Instead, they're creating key performance indicators and tracking things like the "personal emotional connections" made.

Back it with cash. Organizations that provide superior customer service are giving employees the autonomy (and funds) to respond to customers' needs directly and in the manner they see fit.

Give to get. In a social enterprise, the knowledge you amass matters but so too does how much you share with others. Now expand that thinking to partner networks. How do you measure, reward and incent behaviors like sharing?

Trust in time. Organizations that communicate with candor on external social networks recognize that there is not always an immediate return—some customers won't be satisfied. But they believe such exchanges build trust between the brand and its customers over the long term.

Make it a minute. Time is compressed on anything and everything—and especially your responsiveness. The trade-off for speed is often precision; getting comfortable with a new balance is critical.

"We're empowering people, encouraging decision making and creating a culture where both success and failure serve as learning experiences."

John Trobough, President, Narus, United States

From our questions and conversations with the leaders of public and private institutions alike, it's apparent that the vast majority of leaders are putting a new emphasis on collaboration across their organization — and inside the C-suite. And outperforming organizations are ahead of the game. Indeed, 92 percent of outperformers report that their C-suite works in a collaborative and collegial way. CEOs told us that the top traits they hoped to cultivate across their leadership teams were attributes like "open-mindedness to the world," "better understanding of the art of the possible" and "seeing around the corner."

Leaders are intensely and personally focused on the convergence of technologies — and not simply to enable their strategy. Instead, they recognize that emerging technologies are what make entirely new strategies possible.

In the face of runaway innovation, there are leaders in every industry and region who are not satisfied to simply catch up with their competitors or their customers. They are determined to push ahead — and be the source of innovations that change our world. To get there, they've opened up their organizations to new ways of working, and they're leading from a position of trust.

How we conducted our research

This report is the third installment in our ongoing Global C-suite Study, the seventeenth such IBM study to focus on the C-suite and the first to cover six major roles simultaneously. Our aim was to get a better understanding of the opportunities and challenges the members of the C-suite face, and how they are working together to support their organizations.

Between February and June 2013, we met with 4,183 top executives, representing a wide range of public and private sector enterprises in more than 20 industries and 70 countries. They included 884 Chief Executive Officers (CEOs), 576 Chief Financial Officers (CFOs), 342 Chief Human Resources Officers (CHROs), 1,656 Chief Information Officers (CIOs), 524 Chief Marketing Officers (CMOs) and 201 Chief Supply Chain Officers (CSCOs).

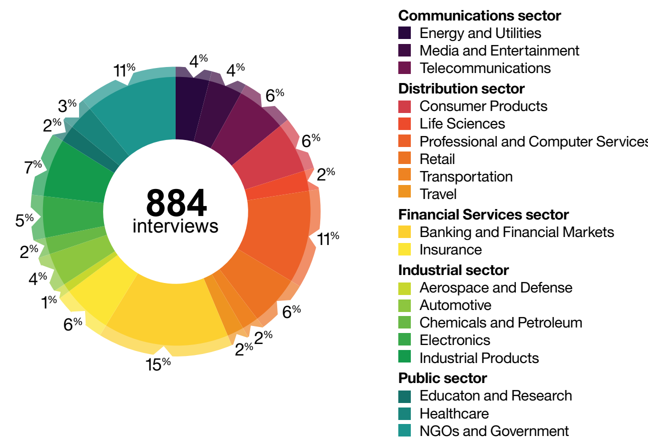
This installment focuses on the responses of the 884 CEOs from 67 countries who participated in our study (see Figure 12). It also compares their responses with those of the 3,299 other CxOs who contributed to our research.

We normalized the data to eliminate geographic distortions, using actual regional gross domestic product (GDP) for 2012. We also normalized for overrepresentation of individual roles, using a quota process to randomly select from oversampled CxOs.

Our research includes an analysis of the differences between the responses of CEOs in financially outperforming enterprises and those in underperforming enterprises, based on how CEOs assess their own organizations. We asked CEOs to rate their organization's three-year revenue growth and profitability relative to that of their industry peers. Enterprises that excelled against both measures were classified as outperformers; those with low rankings were classified as underperformers; and the rest were classified as peer performers.

Figure 12

Sector spread: *We spoke with CEOs from more than 20 industries*



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