

LIVING NETWORKS

ANNIVERSARY EDITION



LEADING YOUR
COMPANY, CUSTOMERS,
AND PARTNERS IN THE
HYPERCONNECTED ECONOMY

ROSS DAWSON

LIVING NETWORKS

Leading Your Company, Customers, and Partners
in the Hyper-Connected Economy

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"This is one of the most exciting books I've read in several years. Ross Dawson deftly examines the evolution of networks, organizations and strategy. He has more than succeeded in his intent, which is to produce a practical business book that shows business people how to leverage networks."

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"The author has demonstrated that the success of his first book was no mere flash in the pan. His book is the one I would choose as a guide to understanding and action for the practical business person."

- **Bill Godfrey**, Editor, Change Management Monitor

About *Living Networks*: Anniversary Edition

Living Networks is being relaunched in its Anniversary Edition five years after its original publication by Financial Times/ Prentice Hall in November 2002, to revisit the foundations of our networked age.

Free chapter downloads of *Living Networks*:

www.livingnetworksbook.com

Ross Dawson's *Trends in the Living Networks* blog:

www.rossdawsonblog.com

About Ross Dawson

Ross Dawson is globally recognized as a leading authority on business strategy. He is CEO of international consulting firm Advanced Human Technologies, and Chairman of Future Exploration Network, a global strategy and events company. Ross is author of the Amazon.com bestseller *Developing Knowledge-Based Client Relationships*, and over 100 articles and white papers. Strong demand for Ross's expertise has seen him deliver keynote speeches on six continents and consult to leading organizations worldwide such as Ernst & Young, Microsoft, Macquarie Bank, Morgan Stanley, News Corporation, and Procter & Gamble. Ross's frequent media appearances include CNN, Bloomberg TV, SkyNews, ABC TV, Washington Post and many others.

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CHAPTER 9

The Flow of Services

Reframing Digital and Professional Services

Digital connectivity and integration are dramatically shifting the role of services in the economy. Software is being provided as a service, business processes are readily outsourced, and the functions of the firm can be broken down into defined modules. Professional services now range across a spectrum of business models ranging from digital services to traditional face-to-face delivery. The same drivers are resulting in the rise of professional networks as viable competitors to established firms.

In September 1998 John “Launny” Steffens, then vice-chairman of Merrill Lynch, was quoted as saying that Internet trading represented a “serious threat” to the financial well-being of Americans. A 38-year veteran of the firm who had started as a broker in Cleveland, his emphatic stance was supported by the 15,000-odd brokers who clearly saw the Internet as a threat to their own financial situation. Merrill Lynch’s clients didn’t see it quite the same way, and made their feelings known, often by setting up online accounts with the brokerage firm’s rivals. Just over a year after Steffens’ widely-publicized comments, the online broking service Merrill Lynch Direct was launched, garnering an award from the financial weekly *Barrons* as the number one online stock trading site within six months. The supertanker had begun to turn around, with Merrill Lynch shifting to actively present itself as an innovative provider of information-based services to its individual and corporate clients.

In order to transform itself, Merrill Lynch is using technologies that can embed business processes into software. You learned about web services in Chapter 2. These are the most important technology bet Merrill Lynch is now making, according to its chief technology officer, John McKinley Jr.¹ The firm is running literally hundreds of initiatives based on web services, helping both to integrate internal systems and to provide services to clients. One of its projects is a portfolio analysis system that integrates disparate account and product information from within Merrill Lynch, and market data from external partners. This assists its brokers in providing effective recommendations to their clients. However it goes beyond this. Selected clients are also being given access to the new systems, offering real-time analysis and insights on their portfolios directly over the Internet. The broker sitting in Merrill Lynch’s offices no longer acts as an intermediary to these high-value services, and top clients are now receiving a whole spectrum of services, including both interaction with highly-skilled advisors and a suite of online offerings.¹

In this chapter we will examine the evolving world of services. Digital services—those that can be delivered online—are becoming central to the economy. Connectivity is allowing both software and business processes to be delivered as services. Now the development of web services is creating a new modular world of business, not only making it easier for companies to fine-tune the selection of what they perform in-house and what they outsource, but also enabling firms to become both consumers and producers of services and business processes. The world of professional services is closely linked to the rapid development of digital services. Professional services strategy must make traditional face-to-face services and new online services fit together seamlessly. Professional networks, that bring together best-of-breed experts from around the world in tightly-knit teams, will become increasingly important in the economy, and challenge traditional business models.

Services go online

Submitting travel and entertainment expense claims is the bane of every businessperson's existence. For the companies that employ them, it is a time-consuming, error-prone process that takes valuable resources from more productive efforts. Application service provider (ASP) Outtask—among its comprehensive suite of online services—allows its clients to automate the entire process, from entering the expense claim to reimbursement, and subsequent integration with the company's accounting systems. Employees can access the system wherever they are, whenever they want, and the company can concentrate its efforts on what it does best.

This is a simple example of how the blossoming of digital connectivity is transforming how services are delivered and used. As companies and consumers get access to reliable and secure bandwidth, whole new worlds of possibilities open up. As you have seen earlier in this book, software is increasingly being delivered as an online service, and it is becoming far easier to outsource business processes while keeping them closely integrated with the organization's core activities.

The shift to providing software as an online service rather than as a packaged product has been driven by both vendors and clients. Software firms—and often their shareholders—prefer receiving ongoing revenue rather than the intermittent lump sums resulting from major sales or the pressures of quarterly reporting. Clients can often reduce costs—especially for the initial capital investment—and free up management to focus on core issues rather than technology. Our ability to connect to the networks almost anywhere and anytime means that using software over the web is an increasingly viable alternative to having it installed on our computers. Service firm Always-on—and a multitude of competitors—provides Microsoft Office software as an online service, available for a monthly subscription fee. Services such as Yahoo! Calendar or Hotmail fit the same model of giving online access to computing resources, except that they are available for free.

The pace of the shift to providing software applications as an online service has been slower than some early evangelists proclaimed. One of the major concerns of potential clients has been their dependence on connectivity. If communication goes, so does their access to software. The other vital issue is the ability to integrate external applications with internal systems. Both of these are becoming less problematic over time. Networks are becoming more resilient and robust, with uptime almost always exceeding that of in-house computer systems, and as you have seen through this book, systems integration is swiftly becoming easier. However it means that many ASPs are starting to include integration services as a core part of their business, rather than simply providing their clients with access to software.

The only services that can't be delivered via digital connectivity are those which require physical presence. Installing PC boards, haircuts, and massages all require—at least for the meantime—a person to be there. High-value professional services are also commonly based on face-to-face interaction, as we will discuss later in this chapter. However all other services can be provided online. You probably only communicate with many of the departments of your company through e-mail or telephone. When was the last time you went to visit your accounts receivable staff? As connectivity and integration drive business, it now makes virtually no difference whether a business process is performed inside or outside your company.

Outsourcing business processes

Automatic Data Processing (ADP) set up business in 1949 to provide outsourced payroll operations. Clients provided information in print or on the telephone, and keypunch operators entered this onto cards for processing by mainframes. Payroll quickly became widely outsourced, because it was a highly information-intensive process that only needed to be performed fortnightly or monthly, thus making it suitable for the early batch-processing systems. Now connectivity has enabled the explosion of business process outsourcing, commonly abbreviated to BPO. Just about every business function can be performed outside the company, even those that require both constant access and deep integration into other parts of the firm. Not so long ago the accounts department was a staple of every organization. Now not just accounting functions such as order entry, purchasing, and billing are being regularly outsourced, but also other operations usually considered a core part of companies, like human resources and even sales, are being executed externally.

Business functions are increasingly automated, but they also often require people. When in 1999 BP Amoco and Pricewaterhouse Coopers announced a billion dollar outsourcing agreement, it included the transfer of 1,200 finance, accounting, and IT professionals.³ However the defining issue with most BPO is that the primary interface with the client organization is digital, which enables it to be easily integrated. As the ability to integrate systems improves further, companies will be able to select far more precisely what is a core competence of the firm, and what is better done outside.

The other key issue is transparency, which enables companies to get full and free visibility of operations, even if they are run externally. Flextronics, a contract electronics manufacturer that makes equipment for firms such as Microsoft, Ericsson, Cisco, and Motorola, provides its clients with total transparency into their outsourced manufacturing operations. As Flextronics manufactures Microsoft's Xbox game console in its plants in

Mexico and Hungary, Microsoft executives are given a single real-time view into global operations, down to the details such as shop floor data and inventory turns. Essentially they are able to see the same degree of information on production and order fulfilment as Flextronics executives. The operations may be outsourced, but the degree of transparency and integration means there is virtually the same information flow as if they were performed in-house.

The new modular world of business

Norwegian insurer Storebrand runs the pension plans of over 390,000 staff for 6,500 firms, which means that its records for every one of these employees must be updated whenever his or her salary or personal details change. The system used to be that companies sent in data changes by file transfer, mail, or fax, and Storebrand's customer service representatives would then enter these into the central database, creating a substantial drain on resources for both the insurer and its clients. Since the required information was already on Storebrand's clients' human resources systems, it made sense to transfer this electronically, however it seemed a hopeless task to try to integrate Storebrand's mainframes with thousands of different computer systems.

Web services, as you saw in Chapter 2, are standards for how applications can find each other and integrate seamlessly. Storebrand worked with IBM to design and implement a new web services application. This enables its clients to update Storebrand's records on their employees from within their own payroll applications. The insurer is now looking to register the web service it has designed on a public directory, so other insurers or distributors can find the application and license it for use within their own applications, thus generating additional revenue for Storebrand.

The heart of web services is breaking down what used to be monolithic software packages and business processes into a set of modules. This is only possible because web services architecture allows these modules to integrate perfectly into each other, requesting information or tasks to be performed as if they were part of the one program, whether they are running on the same computer or on systems on opposite sides of the world. What may initially seem a relatively minor adjustment in fact has revolutionary implications for business.

Inside the organization, web services can change how the business processes and software that are the foundation of the company are developed and implemented. Flexible modules can be built, and then reused in other applications, or simply reconfigured to mean software functionality can evolve with minimal effort. Outside the firm, this powerful new set of technologies has the potential to allow totally seamless

integration of internal and external processes, vastly accelerating the blurring of organizational boundaries, and creating the potential for almost unlimited flexibility in designing and implementing the corporation. Companies must implement four key actions to take full advantage of the new world of web services, as shown in Table 9-1.

BENEFITING FROM WEB SERVICES

1. Use web services to integrate internally and externally
2. Modularize your business
3. Be both a consumer and provider of services and content
4. Experiment with new business models

Table 9-1: Action steps to benefiting from web services

1. Use web services to integrate internally and externally

The government of New Mexico has used web services to integrate a wide variety of existing systems to provide its employees with a single interface to all of their personal information. iv One of the greatest boons of the technology is the ability to give almost any range of systems a common interface so they can be easily linked together. Not only are significant costs saved in performing the integration, but any future initiatives to link data and systems internally can be vastly accelerated after the initial conversion.

Often even larger benefits come from being able to integrate with the systems of external partners, who frequently use completely different hardware and software. Dell uses web services to publish updated manufacturing schedules on its extranet every two hours. This allows all of its suppliers to readily take this information and integrate it directly into their own systems, which helps to bring Dell's plant inventory to sometimes as low as three hours. Another service implemented by Dell generates automated queries to its suppliers' systems on order status. This results in maximum visibility of the supply chain flow for all participants.⁵

Clearly it is not always straightforward to integrate applications across organizations. Companies like Grand Central and Bowstreet represent a new sector that provides the infrastructure and services to facilitate process integration between companies. This helps ensure reliability and security in business transactions, while taking full advantage of the power of the new technologies.

2. Modularize your business

Ford Credit provides online financial services to 12,500 car dealerships and 10 million individual car owners around the world, giving them access to account information, online payments, loan applications, and a wide range of other services. By early 2002 its developers had created 23 reusable web services that are combined into customizable applications. The modular designs have created an estimated \$15 million in savings. One of Ford Credit's largest software applications provides services to 5,000 branch offices. In shifting these applications to a browser-based environment that requires less computing power in the offices and allows workers to access services from wherever they are, Ford Credit has again taken a modular approach, saving costs and dramatically improving efficiency.⁶

The most powerful wave of emerging information technologies does not just enable a business to be broken down into distinct mix-and-match modules, it makes this a clear and powerful path to make a company far more efficient, and immensely more flexible. While the tools to achieve this are software-based, the design for this must be done at the level of business processes. Every company must start thinking about its operations in a new way. What are the distinct business processes that make up your organization? Which of those processes might you want to reuse in a different context? What elements of larger processes could be valuable as stand-alone processes or as part of other processes, either inside the firm or in other organizations?

These are key strategic questions for any company, and today, you have the ability to act on the answers to those questions. The issue of distributing specific business processes inside and outside the firm is at a lower level than the broad strategic issues discussed in Chapter 7, but the birth of the modular organization has a major impact on what strategic options are available to companies.

The flexibility of web services means that existing resources can be easily redeployed in any number of new ways. What is now required is the imagination to conceive and implement new business models.

3. Be both a consumer and provider of services and content

As it becomes increasingly easy to construct applications and business processes from modular components, companies can decide for each one of those modules whether to source it in-house or externally. In addition, if useful business processes are built inside the firm, these can then be sold to third-parties. GMAC Mortgage developed web-based applications for its own use that it has now chosen to provide externally, generating incremental revenue for work it has already done.⁷

Web services is comprised of a set of open standards. Most of the standards focus on how applications effectively send messages and integrate their functions in a secure fashion. However the web services modules that together create applications need to find each other. This is the function of the standard called Universal Description, Discovery, and Integration (UDDI). This is essentially a global database of web services, which allows anyone to search for modules that match specified requirements, identify where they are located, and immediately integrate them into their applications. All that is required is for companies to register their web services in the central UDDI database. Storebrand, mentioned above, is registering its services so that anyone worldwide can find and use them. This central repository of web services means that any firm can easily find and use the best services available, and in turn—if they are the best in their domain—to sell their services to a global market.

4. Experiment with new business models

Commercial real estate broker Collier International is using web services to integrate information on properties and clients from more than 250 offices worldwide. This makes it far easier for salespeople to pull together deals, and also creates a new, valuable resource that can be easily reconfigured. Collier plans to sell selective access to the global database to third parties.⁸ The flexibility of web services means that existing resources can be easily redeployed in any number of new ways. What is now required is the imagination to conceive and implement new business models.

These new technologies allow companies to think about services in a similar way to content. You can widely distribute and redistribute services, just as you can with information. Syndication, which as you saw in Chapter 8 is a well-established business model for content, in an intensely networked world is also an increasingly relevant model for other businesses. The development of web services means that anyone can be a publisher at minimal cost, gaining incremental revenue or enhancing brand by providing content or services for broad distribution. Even using existing approaches, new service models are possible. ASP Outtask, mentioned earlier in this chapter, distributes its travel booking services through travel agent Kintetsu, among others. Since compact web services modules can be easily found and used by third parties, companies will have to develop new approaches to pricing these effectively. Again, syndication business models provide a useful basis for experimentation.

Web services and the flow economy

When Bill Gates repeatedly says that he is betting the future of Microsoft on web services, you know there has to be a good business in there somewhere. Given the potential position of web services as providing the glue that holds together the entire world of commerce, it offers a fabulous case study of the dynamics of the emerging flow economy.

Inevitably, there is a fierce and multi-layered battle for standards. The lower layers of web services, including XML and some simple integration protocols, are by now clearly defined and effectively true standards. The really critical issue is whether web services developed using different types of software can work together. The Web Services Interoperability Organization was founded in early 2002 by Microsoft, IBM, Intel, and software provider BEA Systems. There will be many issues to iron out between the major players as the field of web services evolves and functionality increases, but it is in everyone's interest to see a system in which all computers can readily talk and integrate.

Where the true competition lies is in the platforms that are used to develop web services software. Microsoft's offering is its .NET platform, that allows developers to use almost any programming language, but the resulting software can only be run on Microsoft operating systems. Virtually all of its competitors, including IBM, Sun Microsystems, and BEA Systems, use an open standard framework for software development called Java 2 Enterprise Edition, or J2EE for short. This means that software developed on any of these platforms can—in theory—be readily moved across to run on other hardware or even operating systems. The key factor that will tip this standards battle is the software developers themselves. If developers prefer a particular software environment and become familiar with it, then it will be easier to hire people with those skills, projects will tend to use that platform, and more developers will acquire those skills. Microsoft in particular is expert at wooing the developer community, however the flexibility of J2EE is currently attracting many developers.

An oft-quoted illustration of the potential of web services is the stock ticker available on many websites. This discrete service can easily be provided by a third-party and integrated seamlessly into a website, as long as everyone agrees on the necessary standards. However once this is achieved, this also means that if another firm offers you the same stock ticker for a penny less, you can almost press a button to change suppliers, rather than having to go through any effort to integrate the new service. This shows how both content and services can quickly become commoditized through the widespread implementation of web services. When everything slots seamlessly into everything else, and the only things that make a difference are quality, brand, and price. Quality will always make a difference, however in many cases brand is becoming less visible. Increasingly price is coming to the fore in selected suppliers of modular services and content.

This shift will make relationships with end-customers more important than ever. If you control the customer relationship, then you are entirely at liberty to pull together whatever services and content are required from a vast community of potential suppliers. Their offerings are highly commoditized, and you can take the vast majority of the value created. This

was exactly Microsoft's thinking when it initiated .NET My Services. This suite of personal services for consumers takes full advantage of web services to provide complete integration of almost every way in which an individual would want to tap the flow economy. The central concept is providing a secure database that allows consumers to store their personal information, and to choose exactly how they make that available to third-parties, either to enable them to receive better service or in exchange for value in some form. The information that can be stored includes people's personal details; contact files; where, when, and on what devices to contact them; financial transactions; and a wealth of other vital data. For example, you could book your travel arrangements with all your usual preferences automatically taken into account, pay for them, share your calendar with the people you're meeting, and get both you and your contacts immediately alerted if there are any changes to travel schedules.

Microsoft's initial objective was to offer this powerful system on a subscription basis to consumers. The software giant was positioning itself to effectively control consumers' access to the wealth of the flow economy, attempting to dominate the increasingly important flow element of relationships. However in early 2002 it had to stop and reconsider its initiative. The main problems were that other major corporations had no intention of letting control of customer information shift to Microsoft, and consumers were reluctant to entrust it with all of their personal information. Microsoft has recognized that the center of the information world is no longer PC platforms, but rather access to a whole world of integrated online services. However this enormously valuable positioning will not yield itself easily, and the battle for this space has but begun.

Easy connectivity and integration—epitomized by Web services—have given us a new modular world of business, in which processes can be broken down into software elements, and then recombined to result in powerful and flexible ways of doing business. However not all services can be embedded into software. Highly-skilled professionals play an important role in providing customized, knowledge-based services on demand. The worlds of digital services and professional services are now merging.

The evolution of professional services

Ten weeks after desktoplawyer.co.uk launched an online legal service for no-contest divorces, it captured six percent of the market for British separations.⁹ Why contribute to your lawyer's new sports car fund when you can do it all for £59.99, including telephone support? Corporations are benefiting from the same trends. Clifford Chance, the world's largest law firm, established NextLaw in 1997 to provide online legal services to its corporate clients. Australian law firm Blake Dawson Waldron—among its many innovative online initiatives—implemented for one of its large

retailing clients an Advertising Copy Advisor, which is an expert system that examines the text of proposed advertisements and asks a series of questions to the copywriters. It then provides initial recommendations to the company's in-house counsel on the degree of legal risk posed by the advertisement, and highlights any specific areas for concern.

Not just lawyers, but professionals of all stripes, including accountants, consultants, financial advisors, advertising executives, and engineers, are discovering that digital services and connectivity are beginning to transform their world. So far the impact has been minor in most quarters, but the pace is rapidly accelerating. Professionals can no longer rely on a steady flow of supplicants coming to their door and paying them handsomely for their time when in some cases technology can assist in providing comparable services at a fraction of the cost.

The rapid evolution of connectivity has led to the emergence of three distinct types of professional services, as illustrated in Figure 9-1. Digital execution covers services that are provided end-to-end by digital systems, with no human involvement. Britain's convoluted car tax legislation means that determining whether cars should be leased or bought is a complex calculation based on cost, marginal tax rates, planned usage and more. Deloitte & Touche has launched an online system that provides recommendations for car acquisition plans, and sells this not only to individuals, but also to companies managing their employee benefits, and even accountants who find it easier to use the service on behalf of their clients than do the calculations themselves. Digital interface refers to situations in which people are performing the services, but the interface and delivery of those services is entirely digital. PricewaterhouseCoopers' tax division has implemented Online Consulting Services, which gives online answers to specific tax questions within 48 hours, priced by the question. And of course the traditional approach of face-to-face professional services remains. Increasingly there must be a good reason for people to bear the cost of these highly interactive services, such as gaining knowledge and capabilities that would not be possible online.

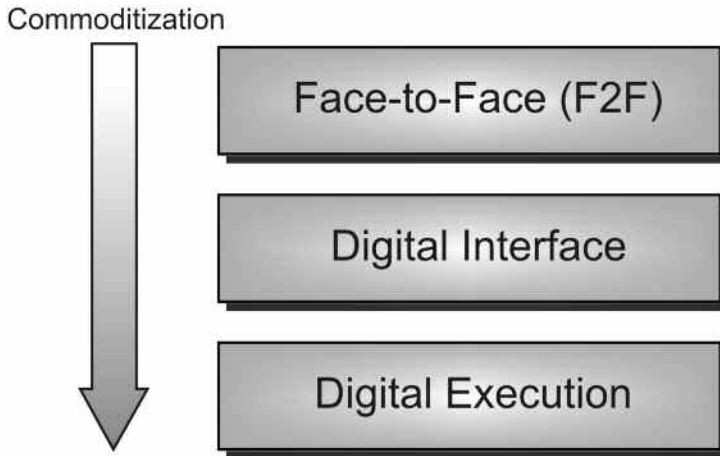


Figure 9-1: Three types of professional services in a digital world

In the middle ages, professional guilds punished their members with expulsion and sometimes worse if they revealed the secrets of the trade. The livelihoods and prestige of professionals were based on keeping information exclusive. Today, the transparency of our highly-connected world means that professionals usually no longer even attempt to keep most information from their clients. Almost all large professional firms have been publishing documents and newsletters for their clients since before the Internet era, and by now have largely shifted those information services online. In some cases they can charge for access to high-value content, however there is constant downward pressure on prices. Their competitors will frequently offer similar information for free in order to attract the attention of prospective clients, and hopefully win lucrative projects. The McKinsey Quarterly, the journal of prestigious consultancy McKinsey & Co, used to be distributed only to clients, but is now available for free online. At the same time, many less complex services are gradually shifting to lower cost alternatives, such as do-it-yourself kits for simple legal matters.

After giving access to information online, the next phase for professional services firms has been to implement digital interfaces to their services. This can be more efficient for both the service firm and its clients. However as soon as face-to-face contact disappears and services are accessed electronically, there is a tremendous degree of commoditization. Clients see only the interfaces and results, and these can begin to look very similar between competitive offerings. As a result, price—and in turn the ability to provide the service at the lowest cost—become the driving issues. In fact the best way to reduce costs is to take people out of the process as much as possible, shifting to digital execution service. Expert systems are not ready to supplant people in every field, but in some cases they can begin to provide low-level advice, or facilitate people in performing their tasks.

The translation industry handily illustrates these trends. Because texts used to have to be physically transported back and forth, clients had to use local translators, unless they were prepared for long delays. The advent of e-mail and the Internet made the process far swifter, and meant that it became easy to use the best or cheapest translators wherever they were in the world. Translation firms—which already almost always had their work performed

No firm can ignore that at least some elements of the services it provides can now be performed digitally, more effectively and at lower cost than by traditional methods.

by independent professionals—broadened their scope to work with translators worldwide, and focus more on the quality assurance function. Today, you can get a rudimentary machine translation for free on Altavista, Google, and other websites.

What many translation services do now is use machine translation to get a first draft of a translation, then use cheaper professionals to edit the text into something readable, and sometimes to check the meaning of the original when in doubt.

One of the dominant trends in professional services today is implementing collaborative tools to interact with clients. This itself is blurring the boundaries between face-to-face services and digital interface services. Professionals can work closely with their peers, with clients in different locations, and if necessary professionals from other firms, in order to execute projects. For example New York law firm Davis Polk & Wardwell regularly uses online “deal rooms” to work with clients on large projects, inviting the investment banks, consultants, and accountants involved in the deals to participate, resulting in a far more efficient process. In addition, these collaborative systems result in far greater transparency to clients. They can see what goes on as it happens, significantly shifting the client-professional relationship.

These dramatic shifts in professional services are relevant to almost every company. Most firms today offer professional advice and consulting services in some form, either as a defined part of the business, or sometimes simply as an increasingly necessary element of the sales process. Firms like IBM and Hewlett-Packard, that used to be simply hardware vendors, are now major providers of professional services. Chemicals company Buckman Laboratories offers consulting on knowledge management as part of the services available to its largest clients. United Parcel Service provides logistics consulting. Every company must consider how professional services—in its new multi-tier form—fits into and enhances its complete range of offerings.

The new professional services strategy

Not long ago now professional services consisted of a single, clear business model. Provide highly-skilled professionals to clients, charge them out by the hour, and pick up the difference between the fees and the professionals' salaries. In the space of just a few years, the situation has become far more complex. No firm can ignore that at least some elements of the services it provides can now be performed digitally, more effectively and at lower cost than by traditional methods.

When Ernst & Young released its groundbreaking online service Ernie in 1996, it was the first major professional services firm to delve into this challenging territory. Ernie provided prompt e-mail answers to specific questions, and a number of online tools such as an IPO Advisor to help young firms through the process of raising capital. In the gradual evolution of its suite of online services, Ernst & Young Online now provides a complete interface to the firm's online services, including the same online answers to client questions, personalized news, interactive tools, and flexible team rooms that allow messaging and discussions both between executives in a client firm, and within engagement teams. Ernst & Young is now seeking new channels to distribute its online offerings, for example offering its Online Tax Advisor and other services as part of FinancialOxygen's capital markets trading hub.

Ernst & Young's initial strategy was to target its online services to medium-sized enterprises that were not yet large enough to merit a full-scale relationship with the firm, but could grow into substantial clients if they were developed early. Since then the primary focus has shifted to providing a spectrum of services to its large corporate clients, mainly to provide the benefits of digital services as a key part of its "full-service" offerings. As shown by its deal with FinancialOxygen, it also sees its online services suite as a business development tool, and to address markets it cannot effectively service face-to-face.

In this new world, professional service firms must take five key steps in developing powerful strategies for success, as shown in Table 9-2.

DEVELOPING PROFESSIONAL SERVICES STRATEGY

1. Develop complementary business models
2. Design for lock-in
3. Implement flexible processes, sourcing, and quality assurance
4. Create knowledge-based relationships
5. Actively migrate clients

Table 9-2: Action steps to developing professional services strategy

1. Develop complementary business models

Professional services began as a single core business model. It has now evolved to cover an entire spectrum of distinct business models. These businesses, ranging from traditional face-to-face consulting to websites, can each be treated as independent operations with their own profit responsibilities. However today one of the fundamental planks of professional services strategy is making these business models complementary.

Few professionals are sympathetic to the idea of their firms offering online versions of services that have up until now paid them well. However an increasing number of firms have recognized that if they don't commoditize their own offerings, someone else will, taking away part of the business, and in addition eroding their client relationships. You have a choice between demonstrating leadership, or being forced to respond to others' moves.

This first step is simply coming to terms with the fact that part of the services that they offer can be performed online. This can open up many possibilities. These digital services can be offered to a whole new class of clients such as smaller companies or those in other locations or countries. Be-Professional, a UK joint venture offering online compliance services for small companies, has become a free-standing business that has opened up an entirely new market for its founding firms, and Ernst & Young launched Ernie with the intention of building relationships with up-and-coming businesses that it could then sell its higher-value services into. Other firms have offered their online services to major clients for free, to consolidate the relationship and keep competitors out.

The way the three types of professional services complement each other depends not only on effective cross-selling from one to another, but also on a balanced application of available resources. The valuable knowledge, systems, and processes of professional firms can be packaged and sold in more than one way. The expert systems designed by Blake Dawson Waldron leverage existing knowledge to generate additional revenue. Ernst & Young Australia has developed a diverse suite of online consulting tools, including systems for companies to monitor corporate governance risk, evaluate tenders, and assess privacy legislation compliance.¹⁰ These begin to shift the firm from the traditional fee-for-service model to one of licensing intellectual property, that provides ongoing revenue once it is developed. The firm is generating income not just by signing up clients directly, but also by making the systems available to its sister firms globally.

2. Design for lock-in

Strong personal relationships are enduring. However when interaction shifts to the digital, it becomes far easier for clients to switch to other providers, so new approaches are required to help them to stay. In Chapter

4 you saw how being more effective at customizing information and services can result in powerful lock-in, since clients will lose a valuable resource if they change relationships. JP Morgan Chase's Executive View service provides its clients with customized websites that include not just information, news, and research on the firm's industry and peers, but also current indicative pricing of the likely cost to the client of raising capital today through loans or commercial paper.¹¹ As with any website, in order to get people to use a site regularly and increase familiarity, some of the services should include time-sensitive information and analysis, and be designed to become part of users' daily work habits. The most powerful lock-in is to integrate clients' actual business processes into extranet offerings. This requires understanding their processes, and designing systems that can match them exactly.

Temporary staff firm Manpower builds websites for its major clients, using the same look and feel as their in-house systems so that these can fit neatly into their intranets. The websites provide detailed stories, information, and instructions on how to go about sourcing and hiring temporary staff. Real case studies of how people at the client firm have had to find staff, and how they've successfully found them through Manpower, are presented in a lively style aligned with the client's culture. Guidance on how to go through the firm's internal approval procedures are given, along with contact details for relevant staff both internally and at Manpower. In addition Manpower changes its own ways of working if necessary, so that they are aligned with their clients' key processes. All this makes it easy for the client to use Manpower, and a major effort to change to use any of its competitors.

3. Implement flexible processes, sourcing, and quality assurance

Every day over one billion words are published, with almost all going through a proofreading or editing process. Editor.com is an online editing and writing service based in Australia that taps this potentially huge market, using both in-house and external editors. With its larger clients, that include Cisco, Merrill Lynch, and Ericsson, it tends to have a fairly traditional service firm relationship, with regular meetings and interaction. Its international clients can interact with Editor.com entirely online, from estimates through to final work completion. Given the nature of its work, the firm's operations are centered on quality assurance. Currently all work done by external contractors is checked internally by senior editors, though managing director Grant Butler foresees being able to get some of the company's most experienced external editors to take on that role once there is sufficient mutual familiarity and trust. Online workflow systems mean that the jobs can be assigned, performed, and checked seamlessly using editors around the world. It's now easy to find writers and editors anywhere in the world, sometimes prepared to work for very low rates, but Editor.com chooses to develop strong relationships with a small pool of experienced professionals. Its business is driven by providing quality output

to clients, so it would be counter-productive to use cheap external talent, and as a result spend far more in managing them and correcting their work.

Professional services delivered through a digital interface can still sometimes attract premium prices. Editor.com charges standard rates for corporate editing work, and Ernst & Young and PricewaterhouseCoopers both charge literally thousands of dollars for a single e-mail response to a question. However the reality is that as soon as clients interact using only digital channels there are keen pressures on prices, and in turn on costs. Firms must be as efficient as possible. Clear, streamlined internal processes must be established if digital interface services are to succeed. If these are implemented in an existing professional services firm, one of the most important issues is allocating work to professionals. The workflow of the digital interface services must be integrated into the existing work practices, by identifying staff that have the expertise and time to respond to incoming work. It is also critically important to design remuneration systems so that staff are motivated to allocate their time appropriately between traditional projects and incoming digital work. Whether work is performed internally or externally, the quality assurance function is critical, both to ensure work is up to standard, but also to maintain consistency of style and approach. If work is performed externally, then the entire operation becomes one of designing effective workflow processes, managing external contractors, and providing quality assurance.

Interestingly, many advertising agencies effectively implement this highly-outsourced model. The advertising concept is usually developed internally, but much of the execution such as design and media production is done externally, with the agency co-ordinating the external contractors. The ability to manage the work and provide quality assurance is a large part of the value created for the client, who would rarely be interested or effective at doing this.

4. Create knowledge-based relationships

Raves are not only for teenagers. Cap Gemini Ernst & Young's in-house think-tank, the Center for Business Innovation (CBI), regularly organizes its own brand of raves: invitation-only events that bring together top thinkers in their field for free-ranging discussion on themes like connectivity, the future of software, and the implications of economic webs. Designers visually map the discussion as it happens, resulting in colorful structured charts of the proceedings. In one rave, participants were given mobile devices that enabled them to buy and sell ideas on an open market, with the agenda of the second day chosen by the closing market value of the ideas. These raves are primarily intended to explore ideas that can be later applied in the firm's consulting operations, and to establish thought leadership, but similar approaches are also used with clients. The CBI hosted Nokia's Insight & Foresight Group, which is charged with

investigating emerging trends and selecting those that the company should incorporate into its practices. In a two-day session, the firm demonstrated to the group how complexity science can be applied to organizations, using interactive models and dialogue to generate ideas... and insight.

The highest level of value in professional services is enhancing clients' own knowledge and capabilities. Digital services can only go so far in achieving this, and rich interaction with very bright people remains essential not only to create fantastic outcomes, but also to build deep, lasting relationships. While most firms will find they need to offer all three tiers of professional services, the low-end digital services are always being commoditized, and the only way to maintain premium prices is to create true knowledge-based relationships. This requires developing enabling structures, processes, and skills to complement technology-based strategies. Relationships with clients need to be structured so that professionals' specialist knowledge is integrated into the clients' operations and decision-making. Processes to ensure knowledge is transferred to the client in the course of engagements should become part of standard practice. And professionals need to develop new skills, including understanding how their clients think, and interacting so as to develop clients' knowledge and capabilities. My book *Developing Knowledge-Based Client Relationships: The Future of Professional Services* gives detailed advice on how to implement effective knowledge-based relationships with sophisticated clients. This is the only way to maintain differentiated, extremely high-value services in a world of driving commoditization.

5. Actively migrate clients

The whole culture of investment banking revolves around the payment of the annual bonus, which can be a time of joy, commiseration, and sometimes obscene profligacy. One global bank based in Europe has made the bonuses of its foreign exchange salespeople depend on how effectively they migrate their large clients to using electronic trading platforms. Traders' bonuses are primarily based on revenue generated, but will only be paid in full if a sufficient proportion of the business has been done online. One of the many challenges of migrating professional services clients to online channels is professionals' fear of losing the client relationship, revenue, or even their jobs. This bank is making it crystal-clear what it expects from its salespeople.

Professional services firms should have in place detailed, current strategies for each of their substantial clients. One of the most important issues today is the desired balance of channels for service delivery, based on the client's profitability, business potential, and strategic importance, and the steps required to migrate the client. Risks and opportunities for the client relationship need to be taken into account, and sometimes it can be an issue of how to move clients to greater face-to-face interaction rather than

shifting them to digital channels. Just as for the overall firm strategy, these individual client strategies should be designed to make the different service delivery and communication channels complementary in developing deeper relationships.

The rise of professional networks

In Swedish, *ska* means “we shall”. SKA is also the acronym for Sveiby Knowledge Associates, a global consulting network that counts around 30 members from 15 nations, representing every inhabited continent. Karl-Erik Sveiby, a leading light in knowledge management and intellectual capital, wanted to bring together a global network of independent consultants, to try to provide them some of the benefits of working within a larger organization, without sacrificing the freedom of choice and flexibility of self-employment.

One of the glues that holds SKA together is the use of common tools and consulting frameworks. All members are licensed to run Tango, a highly participative workshop that helps corporate executives understand the dynamics of managing intangible assets in their firms. Many other structured consulting processes are used by SKA members, often under license, with the SKA administrative hub handling payments from users to the holder of the intellectual property. At the outset of the group, many of the processes used had been created by Sveiby, however the structure of SKA actively encourages all members to develop licensable consulting processes, with the knowledge that there is already a sizeable group of successful and like-minded professionals ready to apply them with their clients globally.

Each member of SKA has his or her own clients, all of which are registered in a central database, including contact details. The owner of a particular client relationship will bring in other consultants from the group as necessary; several major projects have brought together members from multiple continents. Every proposal submitted to a client must be posted on the group’s private website. Clearly this kind of openness can only happen in an environment of trust. The network has established a set of seven shared values, which provide a foundation for behavior by the members. It is a mandatory requirement for SKA members to attend the annual meeting, which so far has been held in Australia and South Africa, with the next one scheduled in Guangzhou in Southern China. Only by regularly meeting everyone else in the group can the necessary cohesiveness and trust develop.

Another professional network is also succeeding, using a quite different business model and approach. The founders of Axiom Legal saw that the clients of major law firms were paying extremely high fees which rarely

reflected the cost of the lawyers doing the work. Salaried associates do virtually all the work, and clients fork out a hefty premium to pay for both the swanky offices in prime

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real-estate, and the partners who sit at the top of the pile. The million-dollar plus packages of top legal partners consist primarily of the difference between the salaries of their associates and what clients are billed for that work.

Axiom was set up to provide the same quality of advice as the top New York law firms, with a substantially lower cost to the client. Partly because it is a virtual organization, it finds it easier to get its lawyers out to its clients' offices, which helps drive the hands-on way of working with its clients in-house counsel that is Axiom's trademark.

Clearly individual lawyers are not able to provide the same level of service as large firms, as they do not have access to the same resources and diversity of experience. Axiom established a similar infrastructure to that a large law firm would have, with complete libraries, support staff, and knowledge management systems to allow its lawyers to work closely together and tap each others' expertise. It then set out to recruit the best lawyers, going through a stringent selection process, but in return being able to offer work flexibility, higher income, and an escape from the intense office politics of partnerships. The enormous demand to join the network has allowed Axiom to be very selective in its recruitment. The firm's attorneys all gather for a monthly meeting, as the firm is still primarily based in the US North-East.

These two cases represent very different manifestations of the new brand of professional networks. In SKA, highly independent but like-minded consultants congregate because of the mutual value of sharing their practices, tools, and sometimes clients. Axiom Legal presents a centralized corporate face to the world, and implements innovative structures for performing legal work that can benefit both lawyers and clients.

Professional networks, although hardly a new phenomenon, are rapidly rising in importance. Their evolution is being driven by both the new ways of working enabled by connectivity, and the swift shift to professionals working as free agents. Corporate clients are increasingly happy to consider independent professionals as service providers, and in some cases actually prefer effective professional networks to expensive global firms with cookie-cutter approaches. The bottom-line is that for many types of business, professional networks are increasingly viable competitors to large,

established firms. This is already apparent, but will become more obvious in coming years. We will cover some of these issues from the perspective of the individual in Chapter 10.

Success factors for professional networks

In many years as a keen observer and participant in nascent professional networks, I have seen considerably more failures than successes. Clearly there is no one successful model or formula—any number of extremely different approaches can work. However there are six common issues that all professional networks must address in order to result in real benefits to their members.

- **Structure and leadership.** The reality is that few professional networks are truly self-organizing—there needs to be a core team which leads the group and co-ordinates its functioning. Axiom Legal represents one of the more centralized professional network models. The capital required for the necessary infrastructure is raised by a company at the core, and a specific offer of labour for pay made to the participating lawyers. Swedish management consulting firm Consultus similarly provides a central administration facility for its affiliated consultants. At the other end of the spectrum some small groups of professionals informally agree to pay referral fees to each other. However this isn't sufficient to provide the fully integrated service that creates the real potential benefits to professionals and clients.
- **Coherence.** Most failed professional networks stumble because the individuals in the network do not have enough in common or anything to bind around. Trust is essential for a network to work, and for that network members need to share beliefs and values. Rob Pye, founder of the consulting network c-people, refers to the importance of “shared purpose”. One of the most important decisions made by any network is its recruitment policies. If it is too easy to join, the risk is the network will become a database of contacts, however bringing complementary skills into the group can create value for everyone, as long as their attitudes and approaches are aligned. If the overly rapid expansion of a network results in insufficient trust between all members, its ability to function can suffer dramatically.
- **Clarity.** The basis for any network is a set of principles or working guidelines for how members work together. Their clarity is the foundation of success. Transparency is essential, so all members can see precisely where any money is flowing in the network. SKA has clear principles and guidelines in place, and its accounts are completely visible to all participants.

- **Identity.** One of the dilemmas for a professional is whether to promote his or her own brand, or that of the network. The solution for most professionals is to keep their own identity, and in addition show their network membership on their business cards and marketing material. The Delphi Consulting Network, based in Raleigh, North Carolina, consists of seven independent consultants who brand themselves individually, as well as with the network name. They have had enough experience working together to be able to manage the dual branding with their clients.

- **Relationship ownership.** Probably the most sensitive aspect of professional networks is sharing clients. The reality is that there are many professionals who are simply not suited to working in networks, because their attitude is to grab what they can. The level of trust within SKA enables them to post everyone's client lists for all other members to see. It is unambiguous who "owns" and manages the client relationship. While Axiom Legal effectively controls its client relationships, referral fees and incentives mean that its attorneys are actively interested in helping to broaden relationships and introduce their peers to clients.

- **Sharing value.** Loose networks can be fairly straightforward in simply providing access to referrals and resources when required. However in order to compete effectively with larger institutions, professional networks require more complex ways of integrating their work so that they can present a common face. C-people has bid for and won substantial projects. Its revenue sharing model is for the network member that sold the project receives 10% of the first year's revenue, 20% of revenue goes to the network hub for administration and overheads, and 70% is allocated between the project participants, with the split among them agreed before the project is begun. The flows of money within SKA are primarily based on licensing the intellectual property of other members, with the individual consultants simply invoicing the relationship manager for their time on services in the case of larger team projects.

Vital Connections: Chapter 9

Connectivity and integration are allowing a large and increasing proportion of services to be performed online. Software is being delivered as a service, business processes can be easily outsourced, and web services are creating a world in which companies are becoming modular. Strategy for high-value professional services strategy must shift to allow face-to-face and digital services to be complementary rather than competitive. The same drivers that are shifting services firms are enabling the birth of professional services networks, that are taking an increasingly important role in the economy.

Today, we are all professionals. We need to develop strategies to participate fully in the networks, and extract value proportional to our contribution. Chapter 10 shows free agents how to develop and implement successful strategies for a networked world.