Capgemini: Preparing for digital transformation

Capgemini is facing its biggest challenge in its 45-year history, as it navigates the downturn in public sector spending

by Danny Bradbury

Overview

Capgemini is a consulting, technology services and outsourcing company that employs 115,000 people in 40 countries. Headquartered in Paris, its background is in IT services, and it has secured several very large outsourcing contracts in the UK.

The company is in the middle of a broad push towards integrating business and technology consulting more closely, while also focusing on a move into other markets, particularly those in emerging economies and Asia.

PHOTO: CAPGEMINI

The year 1967 was a big year for technology in France. It launched its first nuclear submarine and took the wraps off Concorde.

And, in 1967, in the sleepy alpine town of Grenoble, Serge Kampf founded Sogeti. That company would later acquire two IT services companies – Cap and Gemini Computer Systems – to form one of the largest IT consulting shops in the world. Like many technology firms, Capgemini is now reinventing itself, to meet the challenges posed by the economy, cloud computing and the growing commoditisation of IT.

Capgemini is structured into three main groups: Capgemini focuses on systems integration and outsourcing; Capgemini Consulting handles pure consulting work; and Sogeti focuses on local professional services, with a heavy emphasis on software testing.

The early years, 1967-75, were a time of growth and acquisition. Within eight years of its inception, the business had established itself in 21 countries.

The group expanded into Europe and North America from 1975-89. It also retooled, switching from 'capital-intensive machine solutions' to intellectual services, recasting itself as a strategic consultancy company. A pivotal point for the company, however, came in 1990, according to Kampf. In the 2010 annual report, he describes the "*Rencontres*" in Marrakech in June of that year. These regular annual meetings serve as strategic calibration sessions for the company. It was during this meeting that, he says, "we decided to launch the second stage of the Capgemini rocket".

The second stage involved new strategies for growth, primarily through acquisition. It cherry-picked firms, including United Research (1990), and the Mac Group (1991). This helped it to gain momentum.

From then until the present, the company focused on local professional services and outsourcing. It also consolidated offshore development processes through its Rightshore service, which mixes offshore development and near-shoring in countries such as Poland and Spain.

However, probably the most significant purchase made by the company was the consulting division of Ernst & Young, which it acquired in 2000. The workforce grew by 50% overnight and another metric – the deliciously named 'revenue per brain' – grew from €110,000 to €140,000.

Christine Hodgson, chairman of Capgemini UK, who was named woman of the year at the 2011 Everywoman Technology Awards, says the acquisition (which she characterises as a merger), gave the firm a platform to launch more heavily into larger public-sector contracts.

"That was strategically very important, because it increased the range of offerings that we had, and so it was a critical step, for example, in the winning of the Inland Revenue [Aspire] contract," she says, adding that neither organisation would have won that contract on its own.

The merger, which was decided in October 1999 and completed the following March, came at a crucial time for Capgemini and the computing industry as a whole. While the lawyers were thrashing out the details, the clock flipped over and the new millennium began. Capgemini had spent the past few years helping clients to fix their computing systems so that they wouldn't fall foul of the millennium bug. It was a busy and lucrative time.

"The absolute flip of that was the speed of the decline in those subsequent two years," Hodgson says, recalling the 'dot bomb' collapse of the IT sector between 2000 and 2002. "That spike between pre- and post-millennium – I've seen nothing like it since."

That wasn't the only big change that took place at the turn of the millennium. Kampf, who had headed up the company for 35 years, ceded the post to Paul Hermelin as CEO, and took the role of chairman. Hermelin steered the firm through that recession and has remained CEO. In 2010, Kampf was reappointed as president, with Hermelin moving to vice president in addition to his group CEO role.

Now, Hermelin and Kampf are focusing on new challenges: growth and recovering from the recent financial crisis are two. Another, however, is adapting to what Hermelin calls the "industrialisation" of the consulting business. Price pressures and an economy against the ropes are forcing the firm to adapt, he says.

This is also one of the issues raised in a Gartner analysis of Capgemini. It highlights the transition to an industrialised model as a threat to the firm. It also cites long-term revenue viability in the commodity consulting market as a threat, along with margins and profits in strategic consulting domains.

Hodgson defends Capgemini's position in the market. "For sure, over time if you remain static and you're not developing your expertise, then it becomes a commodity," she says, but she disagrees with Gartner's analysis of the commodity consulting market. "I don't see consulting as a commodity in the way that you might refer to outsourcing," she protests. "We do a lot of work in digital consulting around digital transformation, and a lot of our competitors don't."

Digital transformation

What does digital transformation look like? The company signed a three-year agreement with the MIT Center for Digital Business to find out. It wants to work out how to drive digitisation into everything that modern businesses do, from its strategy, through its operating processes, to its employees.

Hodgson cites clothing manufacturer Burberry, as an example. "Its catwalk shows get front-page coverage," she enthuses, adding that the headline won't be about the product or the range.

"The headline will be about the company being a pioneer in technology because it's streaming the video live or tweeting the models live before they go on the catwalk. Everything it's doing has a digital angle to it," she says. "At its results announcement last year, the investor presentation wasn't just done by the CEO and CFO, it was done by both of them plus the CTO. That's incredible."

Cyril Garcia, head of strategy and transformation at Capgemini, explains that the digital transformation idea has evolved in response to changing market conditions, and in particular to new questions being voiced by CEOs. These include the best strategies for capturing and securing data and how well IT governance and business governance are aligned. Should they create dedicated organisations for new business? These are all on the table and driving Capgemini's strategy, Garcia says.

"Today, IT liberates business revolution, and if you want to gain market share, you have to be more productive on your IT investment," Garcia says. "We thought maybe it would be time to be more aggressive around three pillars."

The company is targeting not only technology partnerships with customers, but also business partnerships, to help drive innovations further into its clients' organisations. Underpinning this is a concept that Garcia defines as "intimacy". These changes must be made at a detailed, granular level to ensure that they stick and become part of a client's culture.

New service lines

Marrying business and technology isn't exactly a new concept, but the firm has also created a strategy to help drive these concepts into customer accounts. In 2009, it

Main services

- Finance and employee transformation
- Operational research
- Technology transformation
- Supply chain management
- Lean
- Strategy and transformation

UK clients

- Dorset County Council
- HM Revenue & Customs
- Ministry of Justice
- SIX Telekurs
- The Prince's Trust
- Vodafone

Key facts

- Revenue (2010): €8,697m
- Profit (2010): €280m
- Profit as percentage of revenue (2010): 3.12%
- Headquarters: Paris, France
- Employees: 115,000
- Founder: Serge Kampf
- Founded: 1967

created a series of five 'offerings' – in effect service lines – that will help it to channel these concepts through to its clients.

It divided these offerings into Energy, Business Information Management, Application Lifecycle Services, Testing Services and the grandly named Infostructure Transformation Services. In March 2011, it added a sixth: Business Process Management. The firm regrouped its process management solutions to offer BPM as a global line, complementing the other service offerings. BPM generally carries more margin opportunities than BPO, after all.

All these offerings were developed as part of the "Business As Unusual" strategy that the company announced in November 2011.

Capgemini already has a strong presence in multiple sectors. Energy, utilities and chemicals represent only a small collection. The public sector is an obvious strong point, while manufacturing is a traditional mainstay for the firm, particularly in outsourcing and BPO. Consumer products, retail and logistics is also a strong sector for the company, while telecommunications, media and entertainment stands to benefit particularly from its renewed emphasis on digital transformation. And its purchase of Kanbay International in 2006 considerably bolstered its presence in the financial services sector.

A new way of articulating offerings

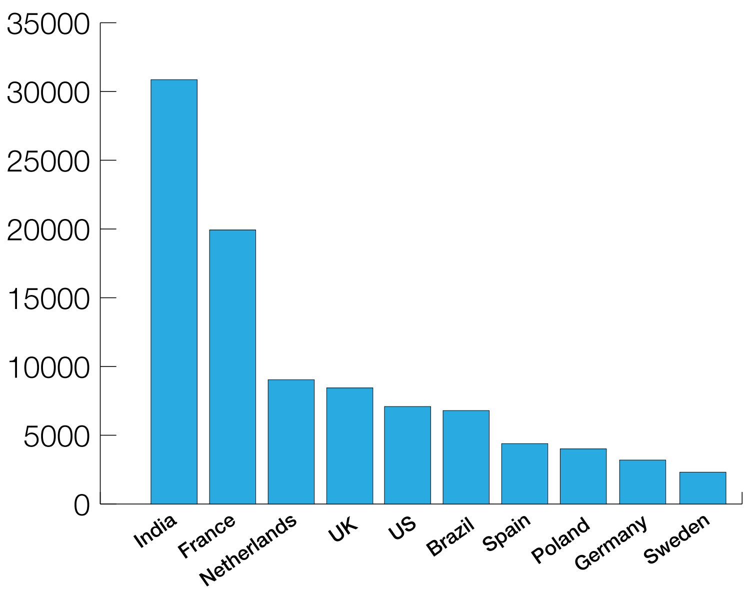
Why was energy the only vertical? What about defining health care as a target offering? After all, those retiring baby boomers have deep pockets and even deeper health issues.

Hodgson explains that energy was an industry buzzword. "We had a strong presence," she says. But for the most part, the idea was to create the offerings as a way to wrap concepts such as 'digital transformation' more attractively for vertical markets.

"If you look at the history, we've been more punctuated by individual deals," she says. "We feel there's more repeatable business to be had, by being more offer-focused. It wasn't replacing what we do, it was supplementing it."

The energy offering is a good example of how Capgemini is blending business and technology to move itself further up the value chain. Garcia describes how the firm is merging outsourcing and consulting with operations and business analytics in its

Top 10 head count by country



Source: Capgemini

Key executives

• **Christine Hodgson** is chairman of Capgemini UK plc and a member of the Capgemini Group executive committee. She also chairs the Capgemini UK Sustainability Board.

• **Nigel Martin** is CEO of Aspire, HM Revenue & Customs' contract with Capgemini for the provision of IT services.

• **Tom Blacksell** is vice president – head of Capgemini Consulting, UK. He has 20 years' of industry and business advisory experience.

• **Andy Mulholland** is global chief technology officer. He joined Capgemini in 1996 with 13 years of experience in senior IT roles.

• **Una Du Noyer** is vice president of Infrastructure Transformation Services. She consults FTSE 100 clients on all aspects of infrastructure strategy.

Worldwide board of directors

- Serge Kampf, chairman
- Paul Hermelin, vice chairman
- Daniel Bernard
- Yann Delabrière
- Laurence Dors
- Michel Jalabert
- Phil Laskawy
- Bernard Liautaud
- Thierry de Montbrial
- Ruud van Ommeren
- Terry Ozan
- Pierre Pringuet
- Bruno Roger
- Pierre Hessler
- Geoff Unwin

systems control and monitoring operation. It is focusing on end-to-end real-time monitoring via IP networks. This is the impetus behind its launch of a smart analytics system for utilities.

Its energy business is buoyant. In summer 2010, it signed a €500m contract extension with Canadian utility Hydro One, under which it will continue to outsource business processes and IT. It has also snagged contracts with Anglian Water and EDF Energy in the UK, and BC Hydro in Canada.

Bolstering its existing presence in the energy market, Capgemini also purchased Swedish firm Skvader Systems in 2010. Skvader installs and manages smart meters, which it operates using its own software. Skvader's charging mechanisms are new for Capgemini; it charges its clients based on the number of meters being monitored.

New business models

New business models such as this are driving Capgemini's strategy. It is exploring new types of revenue model as it tackles new delivery mechanisms, such as cloud-based services.

"We talk about new business models a lot. The possibilities are endless," Hodgson says. She acknowledges, for example, the opportunities inherent in subscription-based contracts, where customers choose from a menu of cloud-based services and have them delivered à la carte.

"The more sophisticated end of the market addresses attitudes to risk and sharing in the benefits," she adds. A contract with a revenue-generating opportunity could bring the opportunity for Capgemini to share in that revenue. Charging on a per-meter basis is an example. If a smart meter programme takes off, the value of the contract is directly proportional to its success. "The skin in the game will be a share in the upside that the client may generate."

All this requires a shift in customer thinking, however. Customers have to evolve beyond pure cost-based outsourcing, in which they strive to slash costs by outsourcing operations, to a strategic outsourcing arrangement, in which they rely more on partners to add value to their operations.

That's a crucial challenge in the current economic climate, not least because about 70% of Capgemini's revenues come from the public sector, which continues to make swingeing cuts.

Hodgson says Capgemini plc has already stepped up to help government clients slash costs. The process began last summer, when IT service providers were invited

Timeline

1967
- Founded in the French city of Grenoble by Serge Kampf

1975
- Acquires two large IT services companies, CAP and Gemini Computer Systems
- Established as a European leader, present in 21 countries

1989
- Reaches 13,000 employees
- Revenues hover around €1bn and the company is fully listed on the Paris Bourse

1990
- Builds a world-class management consulting practice through a series of strategic acquisitions, beginning with United Research

1991
- Reports first drop in revenues (10% compared with the previous year)
- Acquires Mac Group in the US
- Capgemini Group University founded; hosts more than 10,000 managers and employees between 1992 and 1994

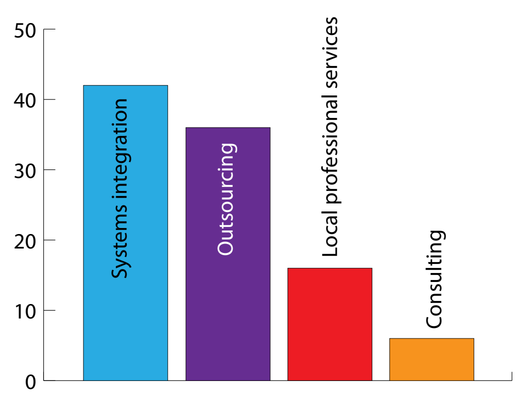
1993
- Acquires Gruber Titze and Partners

1996
- Between 1996 and 1999, sales nearly double and headcount soars from 26,000 to 40,000

1997
- Acquires Bossard in Europe

1999
- Voted European Company of the Year

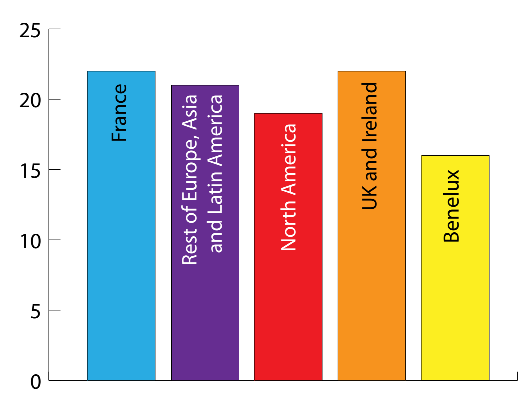
Revenues by business



Breakdown of revenues by business (% of revenue)

Source: Capgemini

Revenues by country



Breakdown of revenues by country or region (% of revenue)

Source: Capgemini

to negotiate new contract parameters with government. “We were one of the first of the 19 to go in and discuss what cuts we could make across all our contracts,” she recalls.

The company’s other lines include business information management. Its business information management offering became evident in 2009, when it said it would increase the number of business information management consultants by 3,000. That gave it 7,000 business information management consultants overall globally, 1,000 of which were based at a new centre of excellence in India.

Since then, it has bolstered its presence in this market. It first purchased Avantias, a BI firm in France, then snapped up Minneapolis-based BI Consulting Group, which focuses on consulting for Oracle Business Intelligence and Enterprise Performance Management Systems.

Capgemini’s efforts in this area have paid off. In January 2012, it was chosen by Unilever to manage a three-year global business intelligence project, in which it will create the consumer goods company’s first enterprise data warehouse, to gain real-time data on its global customer base. Again, the focus here is on digital transformation and spanning the technology and business operations for its clients.

Its application life-cycle services offering is designed to help clients to manage the life cycle of software applications, not just through development, but also through maintenance. When announced at the end of 2009, Capgemini said it would be supported by 15,000 people across the globe. Half of its 20,000-strong Indian workforce would be involved in supporting the service line, it said. It also retrained 5,000 application consultants and managers over six months to support the project.

Since then, it has fleshed out its offerings in this area. In late 2010, it launched SAP Life-cycle, a subscription-based service to help develop and manage SAP implementations on an ongoing basis.

In 2011, it announced an agile legacy life-cycle service in collaboration with IBM. Again testing the boundaries of Capgemini’s experience with a subscription-based business model, this service is delivered via centres of excellence in the UK and India, along with others in the Netherlands and the US.

In August 2011, it netted Nordic company EnterCard, which issues credit cards. Capgemini was chosen as the application maintenance and development services company to support EnterCard’s delivery of new products and services to the market. The five-year agreement was worth €30m.

Shortly after launching the application testing services line, Capgemini integrated its software testing resources into a new offering. It took software testing resources from across the group, marrying them with testing resources within Sogeti, its local

2000
- Acquisition of Ernst & Young Consulting

2002
- Paul Hermelin installed as CEO
- Capgemini and EMC form global strategic alliance to accelerate customers’ journey to the cloud

2007
- Acquires Software Architects and expands US operations

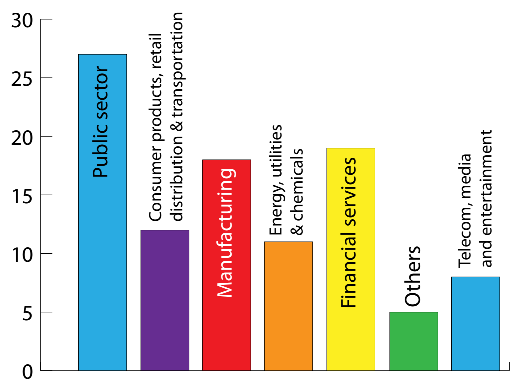
2008
- Extends outsourcing activities in the Netherlands

2009
- Acquires Nu Solutions

2010
- Acquires 55% stake in CPM Braxis
- Acquires German IT services provider CS Consulting GmbH

2011
- Consolidated revenues announced €2,378m for Q3
- €500m bond issue

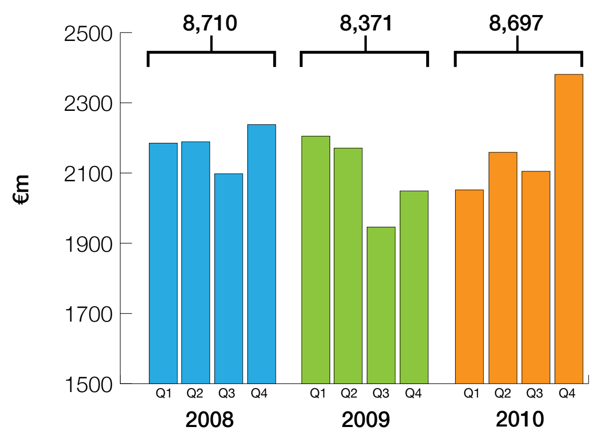
Revenues by sector



Breakdown of revenues by sector (% of revenue)

Source: Capgemini

Revenues by quarter



Source: Capgemini

services business, giving it 6,400 testers and 11,000 application specialists across 40 countries.

Since then, it has upped its game in the world of software testing. In March 2010, it announced plans to offer testing as an on-demand service, hosted online. In June 2010, it joined with HP to launch an application testing service under a pay-as-you-go scheme. It launched the Oracle Software Testing Centre of Excellence in India that October.

In December 2011, it topped Ovum's 2011 benchmarking study of testing services. Ovum evaluated companies based on criteria including cost and value, customer responsiveness and test process capabilities. Capgemini excelled in the latter, the analyst firm said.

Expanding cloud-based services

The infrastructure transformation service plays host to Capgemini's cloud-based business, which is becoming an increasingly important part of its portfolio. This services suite, announced in 2010, was again launched in conjunction with Sogeti. It includes four offerings, ranging from datacentre optimisation and consolidation to virtualisation, unified communications and cloud computing.

Capgemini has since announced a range of partnerships and customer wins in the area of cloud computing. In July, it signed a global deal with Microsoft to deliver customer solutions around Windows Azure. It also committed to train 1,500 architects and developers on the Microsoft platform and to develop a dedicated offshore centre of excellence for Azure in Mumbai.

It followed up the Microsoft deal with a five-year partnership with EMC to develop cloud-based offerings. They will begin with storage as a service, on EMC hardware to be hosted at Capgemini datacentres. Other offerings will include messaging as a service for specific verticals.

"For me, the most important thing is to have a relationship with the CIO and to help them see the possibilities and the boundaries that can be pushed"

Christine Hodgson,
chairman, Capgemini UK

The EMC and Microsoft deals represent only two of six strategic group wide partnerships. Its other top technology partners include IBM, HP, SAP and Oracle. Capgemini had a presence in the cloud computing space before its major 2010 push, but it has since signed more deals on the back of a dedicated cloud service line. In addition to existing partnerships with Amazon, it also signed a 2010 agreement with the Royal Mail Group to provide cloud services as part of a broader business and consumer online service transformation strategy. Underpinning the contract was the goal of swiftly moving into new web-based business opportunities, with an emphasis on personal and SMB customers.

A marketing challenge

As Capgemini continues to push its strategic consulting services, it may run up against a traditional weakness. It has a lack of visibility among board members outside the CIOs, according to Gartner. That may not be a problem when it is selling simple IT outsourcing, but it could prove crippling as it courts other areas of the business to create a more joined-up approach to consulting. Without the rest of the C-suite on board, its digital transformation strategy is likely to die on the vine and it will find itself relegated to mere systems and software services once again.

“It has sales and marketing limitations,” says Andrew Milroy, vice president for ICT Research, Asia Pacific at Frost & Sullivan. “In common with a lot of these European players, it has struggled to get the same leverage as their competitors.”

He highlights a fundamental difference in the sales and marketing approach of North American firms compared with those in Europe. “The focus on sales and marketing is a very American thing,” he says. “The Europeans focus on capabilities and the ability to execute.”

“Some of our competitors may have stronger consulting arms, and we’re strengthening that,” Hodgson admits. “The CEO is often more familiar with our consulting arm than with our technology arm.”

In the meantime, she prefers to capitalise on the CIOs that ‘get it’ and use them as a foothold to address the rest of the board. “For me, the most important thing is to have a relationship with the CIO and to help them see the possibilities and the boundaries that can be pushed.” For a company with a stronger IT consulting division, however, that represents an additional hurdle, especially in this cost-conscious economy.

An acquisitive strategy for growth

As the company tackles the transformation of its own sales strategy, it faces a formidable challenge: maintaining growth in a rocky economy. Recovery has been sluggish since the financial crisis, according to its annual report. In fiscal 2010, revenues had still not reached 2008 levels. Capgemini had clawed turnover back up to €8.69m, compared with €8.71m in 2008. Profit for the year in 2010 was a lamentable €280m, compared with €451m two years prior.

In addition to the new sales model, the firm is also banking on acquisitions to help shore up a shaky growth pattern. Nicolas Dufourcq, deputy general manager and CFO, predicted that acquisitions would account for half of its 2011 revenue growth, which was pegged at 9-10%.

Garcia calls the acquisition strategy a “string of pearls”. Capgemini bases its acquisitions on different axes. The first targets the fast-growing economies, particularly in Brazil and China.

In October 2010, the company paid €233m for a 55% stake in CPM Braxis, a Brazilian IT services firm. The Brazilian IT economy is set to boom, for a variety of reasons, including the 2016 Olympic Games in Rio de Janeiro and the forthcoming 2014 World Cup. Such events are well-known economic stimulators. But a relatively buoyant economy primed for growth, combined with a glut of natural resources and an enthusiastic base of US companies willing to set up regional headquarters in the area, make Brazil’s IT market prime territory for growth.

Clearly hellbent on making its acquisitions in rhyme, Capgemini also purchased Praxis Technology in China, in June 2011. Buying the company with net cash, Capgemini established a foothold in the Chinese market and this acquisition is unlikely to be its last in the region, which is expected to see a double-digit growth in its IT market for the next five years, according to IDC.

"You'll see more in the east. As a group, we look at it an awful lot," says Hodgson, adding that the Braxis acquisition was very well received and the group needs more like it. "But we are very choosy and the acquisitions are very selective."

The company has a stiff challenge ahead of it in emerging markets. It wants to derive 10% of total revenue from fast-growing economies between now and 2015, doubling it from today's percentage.

And moving into the Asia-Pacific market will be a difficult venture, warns Frost's Milroy.

"In common with a lot of IT service vendors beyond Australia and New Zealand, Capgemini has really struggled," he warns. "One of the reasons is that the IT services market still isn't very mature in most of Asia-Pacific." Outsourcing hasn't caught on culturally in the same way that it has in Europe and North America, he argues.

However, the Praxis Technologies acquisition is a sensible way to get into the Chinese market, he believes, because Chinese clients value local connections. Praxis is a relatively small company with between $8m and $10m in revenues, he says. "But it gives it a foothold."

India is another hot area for Capgemini. Hodgson argues that the company has begun focusing on the direct to market in India, rather than using it purely as a global delivery centre.

Garcia's second broad acquisition goal is portfolio evaluation. The company is strengthening its presence in key service line areas, such as mobility. This portfolio-based approach might explain its purchase of French company Prosodie, which focuses on multichannel online services, providing access to information in real time. Prosodie provides customised routing for call centres, for example.

"It does a lot of transactional online highly automated and standardised processes," explains Juan Sacchi, senior research analyst at IDC's European services team. "I think this is a very strategic move." He believes Capgemini will cross-sell Prosodie's services to existing clients.

Capgemini's other strategic acquisition focus is geographic reinforcement, strengthening its critical size in key areas. Perhaps the best kind of acquisition straddles these different axes, giving the company benefits in multiple ways.

"Our most sizeable acquisition was in Brazil, because we were very underweight there," Hodgson says.

Capgemini has proven itself in its core areas of consulting, systems integration, local professional services and outsourcing. It has experienced a number of challenging transitions in its past, as it engineered for growth. Now, with competition from the big four systems integration and consulting companies, it is under increasing pressure to innovate and transform itself into a more holistic player, with increased visibility among business level board members.

The company may face challenges, but with a strong executive, a judicious acquisitive strategy and solid partnerships among leading technology vendors, it is in an excellent position to sail smoothly through the next chapter in its long and respectable history.