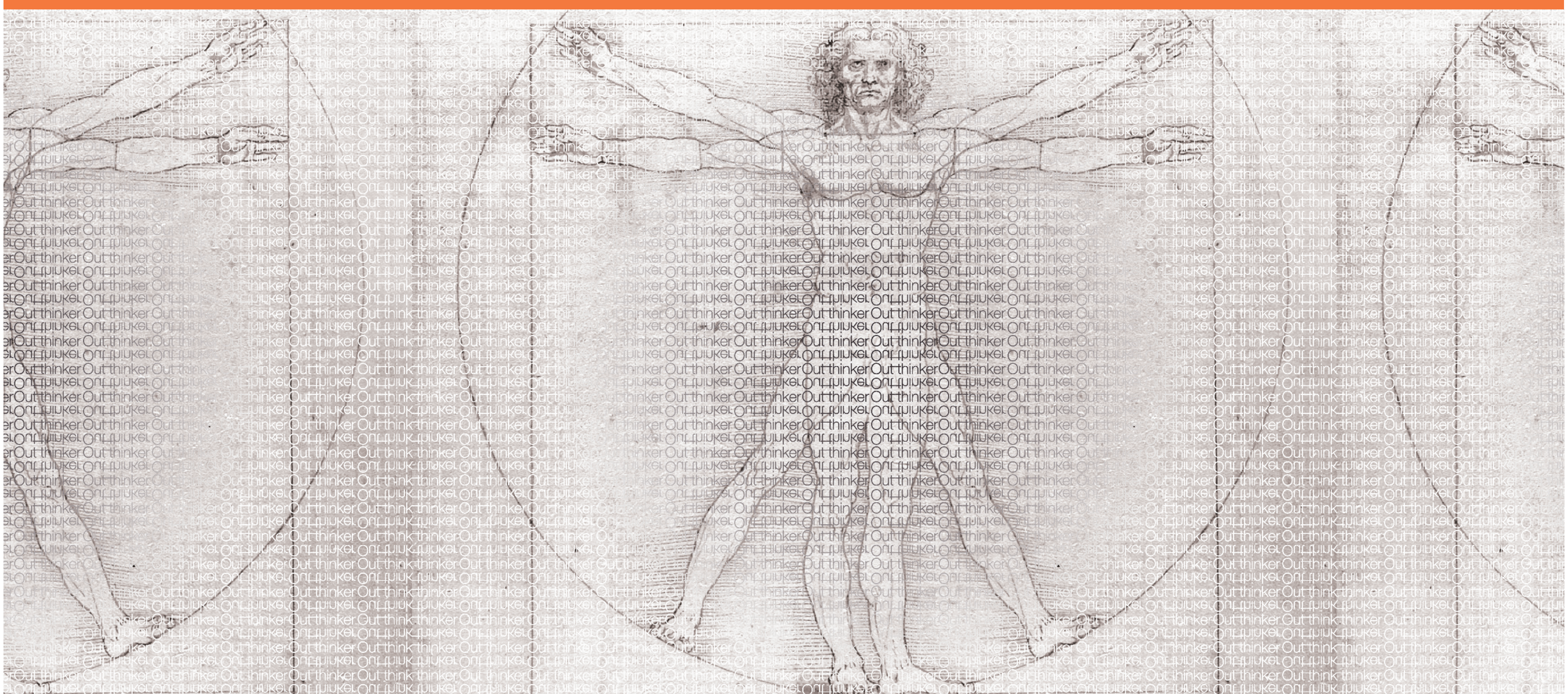
The 10 Most Competitive Tech Companies in the World

As calculated by Outthinker LLC (www.outthinker.com)



February 2014

Outthinker LLC
1440 Broadway
23rd Floor
New York, NY 10022
+1 (212) 380-7919

The 20 Most Competitive Tech Companies in the World

February 2014

At Outthinker we follow the philosophy that an idea is only innovative if adopted. We follow Chicago University Professor Michael Csikszentmihalyi's distinction of there being two types of creativity. "Little c" creativity is coming up with something new and different. But "big c" creativity changes things because it is adopted and changes the world.

As Steve Jobs put it, "Innovation is creativity that ships."

Which is why we look with some skepticism upon many of the innumerable lists of most innovative or admired companies. Too often they pass the "this is cool" test but not necessarily the "this is going to change things" final. They are creative, but is the list's writer to judge if they are innovative? We think that, by definition, the writer cannot.

So when we look for innovation, we look for unique strategies that are having a measurable impact on their market.

Over the last three months we assembled a massive database of over 6,300 companies, tracking 5 to 10 years of data on 105 factors including sales growth and profit margins, in order to pan from these the most competitive companies in the world today.

Here we share the results of our first analysis: the 10 most competitive technology companies in the world. These are outliers that break industry-standard barriers of performance. They grow faster, produce higher margins, and generate more shareholder value than their peers and have sustained this level of over-performance for five years or more.

This level of performance cannot be achieved with good execution, a successful product, or healthy industry trends alone. These companies are doing something more. They are adopting disruptive strategies competitors are not responding effectively to. They are shaping the world. They are Outthinkers.

Before we introduce who these Outthinkers are, we want to briefly tell you who they are not.

1. They are not (only) fast-growing. Achieving a year or two of exceptional revenue growth is not that difficult if you are willing to cut your margins. These companies have broken this trade-off. They not only grow faster, they do so while being more profitable.
2. They are not lucky. They are sustaining their outperformance over a five-year period – a lifetime for many tech firms.

3. They are not the little attackers. We only chose companies that were larger (in terms of market capitalization and enterprise value) than the average of the tech sector. These are substantial companies, all over $1B in revenue, that are out-innovating the smaller innovators.
4. They are not Wall Street fads. A frustrating fact for those looking to truly understand business competition is that stock price often bears no relation to firm performance. "Mr. Market," to borrow Warren Buffett's term, gets excited and loses interest erratically. These companies are different. They are growing significant value over the long-term.

These are companies that, over the past five years, have produced a combination of faster revenue growth, higher EBITDA margins, and greater enterprise value (EV) increases. We chose these metrics because:

- Faster revenue growth means they are stealing market share
- Higher EBITDA margins means they can charge higher prices and/or sustain a lower cost structure
- Greater EV appreciation means they are converting their performance into value

For each company, we calculated a "competitiveness score" by multiplying its normalized five-year average performance across these three dimensions. On average, technology companies achieve a competitive score of about zero. This is because while some grow fast, they do so at the cost of margins. While some achieve great margins, they price themselves too high and can't grow.

The top 10 most competitive technologies break the norms and achieve competitiveness scores of about 0.5 and above, all the way to a record competitiveness score of 3.86 for Apple. Note that Google is in the running to appear in our "Most Competitive Communications Companies." They are not classified by our database as part of technology sector. See the "Methodology" section below for a more complete discussion.

10 Most Competitive Technology Companies in the World

January 2014

"The Outthinker Tech 50" by Outthinker LLC

Rank	Name	Description	5 Year: Total Revenue Growth (Percent)	5 Year: Average EBITDA Margin (Percent)	5 Year: Total Enterprise Value Growth (Percent)	Competi-tiveness Score*	Annual revenue ($billions)	Outthinker Score**
1	Apple Inc.	Founded in 1976, Apple spent decades as the underdog to the Microsoft-Intel PC world. But over the past 10 years its unique strategic focus on design and an integrated system, set against the common dogma that performance and open systems would win, has proven out.	537	31	135	3.86	170.91	6
2	Cognizant Technologies	Created as Dun and Bradstreet's internal IT services unit, Cognizant spun out and went public in 1998. It offers clients a bundle of custom IT consulting, technology, and outsourcing to healthcare, financial services, retail, manufacturing and logistics clients.	244	21	110	0.75	0.01	3
3	Red Hat Inc.	Originally formed in 1993 as AAC Corp and renamed Red Hat in 1999, this company became the poster-child for and is now arguably the leading player in the open source software movement.	183	21	171	0.75	1.13	4
4	Oracle Corp.	Founded in 1997, this enterprise software company focuses on applying cutting edge Oracle technology to help clients simplify complex business and operations. It offers database and middleware software and applications.	106	44	27	0.70	37.18	2
5	Qualcomm Inc.	As covered in our 1999 book Hide a Dagger Behind a Smile, Qualcomm began unlocking exponential growth when it abandoned asset-heavy infrastructure businesses and focused instead on creating and licensing wireless chipset and software technology.	116	38	45	0.69	24.87	5
6	Cerner Corp	This health care IT company helps hospitals, corporations, and government organizations operate more efficiently. Its platform combines clinical, financial, and management information systems, manages electronic medical records, and delivers information to physicians, nurses, other medical providers.	75	29	186	0.62	2.67	3
7	Akamai Technologies	This company's "Application Performance" solutions improve its clients' operations by enabling enterprises to connect with their employees, suppliers, and customers. Its technologies help enterprises manage large files, deliver media, and distribute software.	116	39	14	0.57	1.37	4
8	VMWare Inc.	VMWare is arguable the leader in the virtual soultion space, enabling businesses to improve efficiency, availability, flesibilty, and manageabilty by seperating application software from the underlying hardware. They are also well poised to compete in "cloud computing."	247	25	14	0.56	3.77	3
9	Activision Blizzard	Though it has experience tough times recently, this software entertainment company has grown into one of the largest producer of online and consol games.	221	28	-	0.55	4.55	1
10	Nuance Communications	With an enviable lead in text-to-speech solutions, dication applications, and predictive text technolgoies, this company, the maker of Dragon Naturally Speaking is also rumored to be the technology behind Apple's Siri.	174	21	92	0.47	2.39	3

* = normalized sales growth X normalized EBITDA X normalized EV growth

** = measure of company's likeliness to maintain its competitive advantage

Source: Outthinker LLC (www.outthinker.com), Bloomberg, TIAA-CREF, Gale Net, Outthinker Analytics

Implications

We have already researched the rationales that investors and strategy experts give for the breakthrough performances of these firms and over the coming weeks we will dive deeper. But immediately, five implications jump out at us:

1. The Apple hype is real: We have long been cautious of the seemingly insatiable investor appetite for Apple, but when we step back we see clear evidence that Apple is doing something different. While it's less profitable than the average technology company (hardware is by nature less profitable than software), no other company, even smaller ones, can match the sales and value growth Apple has generated. You can see this in its competitiveness score but in addition, when we inventoried what compelling competitive advantages Apple enjoys, we count at least five, more than any other company on the list. *How many competitive advantages do you have and how can you find more?*
2. The "cloud" and "devices" are driving profit growth: At least 5 of the 10 companies that made the list, according to investors and strategy experts, owe their success in part to being ahead of the curve in "cloud" computing and a multi-device world. Those were Cognizant, VMware, Nuance, Akamai, and Cerner Corp. *How will the cloud and devices change your business and are you ahead of the competition in preparing yourself?*
3. "Fourth options" still rule: We believe all disruptive companies win by introducing what we call "fourth options" – strategic options that others will not copy or respond effectively to. This means doing things that competitors will <u>choose</u> not to copy, even if they could. As we work down the list of these top 10, analyzing reasons analysts and management gave for their performances, in each case we identified at least two compelling "fourth options." The one exception was Activision Blizzard which enjoys some powerful gaming franchises (World of Warcraft, Diablo, Skylanders, Call of Duty, etc.) but few evident sustainable advantage beyond these brands. *How do you generate new "fourth options" and protect those that you have?*
4. Borrow a road: Three of the top 10 owe their success at least in part to borrowing someone else's road, securing distribution partnerships that propelled growth and profits. Qualcomm, Akamai, and Nuance Communications all adopted strategies in which they distribute technology <u>through</u> other players. *Whose road could you borrow?*
5. It doesn't take much: We use a particular method for scoring the competitive advantages of a company. The methodology gives a calibration level between 0 and 16. However, we rarely find companies calibrated above 5 or 6. Of the top 10, we believe Apple calibrates the highest at 8 (out of 16). Most of the remainder calibrate in the 3 to 5 range. Only Activision has a lower score. These numbers are low relative to what we see in other industries because technology is a fast-moving business in which advantages often erode quickly. However, for the thoughtful strategist, this creates an opportunity. Since everyone has difficultly finding sustainable advantages, those who <u>can</u> find them reap exceptional rewards. Just one sustainable strategic innovation

can put you far enough ahead of the competition to deliver you an impressive run of abnormally high returns. *Visit 8p.kaihan.net to calibrate your competitiveness and then look for ideas for elevating above your peers.*

Outthinker Score Estimates of Most Competitive Tech Companies

			8P assessment								
Rank	Name	What investors say	Product	Price	Place	Promotion	Positioning	Processes	Physical	People	Score
1	Apple Inc.	- Dominant brand, customer loyalty, and product portfolio - Unique culture and design ethic - Untapped growth opportunities in China - Leading postitions in key content and services	1		1		1		2	1	6
2	Cognizant Technologies	- Strong management - Well position in Social, Mobile, Analytics and Cloud (SMAC) segment - Unique US-leadership/ India operations structure (Two-in-a-Box client engagement model)					1			2	3
3	Red Hat Inc.	- Fully commited open-source (v. proprietary) technology - Sells the "service" of continual updates to open source coding, rather than coding itself	2				1	1			4
4	Oracle Corp.	- Strong salesforce management practices - Successful at automating, standardizing, and centralizing business processes - Leading position in providing corporate database management to large corporations - Aggressive M&A strategy	1				1				2
5	Qualcomm Inc.	"- Strong portfolio of proprietary technology - Focus on scaleable licensing business (instead of hardware) with almost 90% operating margins - Culture: one of Best Places to Work, strong engineering/ technical cutlure	1		1		2			1	5
6	Cerner Corp	- Obamacare changes make company's offerings more improtant to hospital systems - Helps solve a major problem for lage base of customers (more than 2,600 hospitals, 9,000 facilities) - Act like a niche data cloud provider (a niche VMWare, EMC, F5 Networks)	1				1	1			3
7	Akamai Technologies	"- Considered part of the "backbone of the internet" - Increases in video delivery, software downloads, gaming and social media should drive company's growth - Large salesforce and distribution relationships (e.g., IBM, Cisco) create advantage -	1		1		2				4
8	VMWare Inc.	- Established position as market leader in virtualization (55%) of market - Plan to transform into a cloud management provider - Focus on strategy called "Empower the multi-device era" put its ahead of fast-growing segments - Strong partner in EMC (which owns significant share of VMWare) but a pure-play software company (no hardware)	1		1		1				3
9	Activision Blizzard	- Strong franchises in World of Warcraft, Diablo, Skylanders, Call of Duty and Starcraft - 2008 merger of Activision and Blizzard created scale economies	1								1
10	Nuance Communications	"- Through acquisition has lead position in key segments such as: healthcare, text to speech, speech to text, natural language understanding, clinical language understanding, voice biometrics, digital personal assistants, enterprise solutions, automotive, TVs, mobile devices, smart phones and more. - Carl Ichann's Icahn Enterprises has invested heavily in the company - License of technology to Apple and Samsung mean it benefits for every phone and tablet sale of those companies	2				1				3

* = normalized sales growth X normalized EBITDA X normalized EV growth

Source: Bloomberg, TIAA-CREF, Gale Net, Outthinker Analytics

Methodology
First, our research partner, TIAA-CREF, assembled a global database of 6,300 publically traded companies, tracking revenue growth, profit margins, shareholder return and 102 other factors. We then sorted this list by industry sector, separating, for example, technology firms from those in financial service from consumer cyclical companies.

We calculated their 5-year average sales revenue growth, 5-year average EBITDA margins, and 5-year growth in enterprise value. We normalized each of these and multiplied them to calculate a "Competitiveness Score" for each company. So, for example, a company that produced 5-year average revenue growth, EBITDA margins, and EV growth equal to the sector average would receive a Competitiveness Score of "1."

We chose these factors because:

- Sustained higher revenue growth is an indicator that a company is expanding market share and therefore has created an advantage that delivers a superior product or service
- Sustained superior EBITDA margin is an indicator that the company has achieved a competitive advantage that produces a lower cost structure, an ability to charge higher prices, or both
- Superior long-term Enterprise Value growth is an indicator that a company is able to translate fundamental performance into value

To get a high score a company typically must perform well across all three dimensions. Many companies can temporarily grow faster by cutting prices and margins. Many can increase value by managing investor sentiment well, but fail to produce superior business results. To be an Outthinker a company must stand out from the crowd. It must prove it has a strategy that enables it to grow as fast as, be as profitable as, and generate as much value as its peers while it's simultaneously outstanding in at least one of these.

We removed smaller companies from the list, focusing only on the largest 50% (about 3,100 companies in total) because generating a high competitiveness score is relatively easier for smaller companies to do and so can indicate simply that they have a lot of growth still to do, not that they have necessarily adopted a disruptive strategy.

Finally, we dug deeper into the top performers in each sector, looking at their strategies, seeking to better understand the reasons for the performance, in order to identify what disruptive competitive advantages they have created.

For more information

Kaihan Krippendorff
CEO, Outthinker LLC
kaihan@outthinker.com
+1 (212) 380-7919
www.outthinker.com

